

*„The Intertwining of Security and Economics
in Transatlantic Politics“*

Working Paper

July 4, 2002

*Transatlantic Strategy Group Conference
11 – 12 July, 2002, Berlin*

**Bertelsmann Foundation
Center for Applied Policy Research**

**Bertelsmann Foundation
Carl-Bertelsmann-Str. 256
D-33311 Gütersloh
Phone: ++ 49 (0) 5241 81 81 507
Fax: ++ 49 (0) 5241 81 81 984**

**Center for Applied Policy Research
Maria Theresia Str. 21
D-81675 München
Phone: ++ 49 (0) 89 2180 1338
Fax: ++ 49 (0) 89 2180 1329**

Transatlantic Strategy Groups on „Security“ and „Economics, Trade and Finance“

Transatlantic Strategy Group on Security:	Transatlantic Strategy Group on Economics, Finance and Trade:
Dr. Walther Stütze , European Chairman; Deputy Minister of Defence, Berlin	Caio Koch-Weser , European Chairman; Deputy Minister of Finance, Berlin
Dr. John Hamre , U.S. Chairman President and Chief Executive Officer, Center for Strategic and International Studies (CSIS), Washington D.C.	C. Fred Bergsten , U.S. Chairman; Director, Institute for International Economics, Washington, D.C.

The goal of the Strategy Group on Economics, Finance and Trade and the Strategy Group on Security is the development of policy recommendations for closer and more effective cooperation between the United States and Europe. In addition, the two Groups hope to create new networks among the "next" generation of transatlantic leaders in order to help maintain a firm foundation for the close alliance that has been so crucial to both for the past half century. The initial output from the Groups will be a strategy paper containing specific policy recommendations for a broader audience of key decision-makers in the United States and Europe.

Introduction

Transatlantic relations are changing in a fundamental manner. Instead of attaining greater symmetry, the relationship has become more and more asymmetrical. This asymmetry encourages U.S. unilateralism - even if it is of benevolent nature - and at the same time places constraints on the effective protection and promotion of European interests. A strategic partnership in both the security and the economic fields seems to lie well beyond reach.

Transatlantic relations have entered a new post-cold-war era. One of the major tasks facing policymakers and experts will now be to define a new paradigm of western policy in response to these fundamental political changes. Recent events have demonstrated that the notion of "total solidarity" is on the wane everywhere, primarily because the ways in which the United States and Europe perceive threats are significantly different. This is not a fundamentally new phenomenon, and in fact merely a continuation of developments which were already in evidence before 11 September 2001.

The Security Agenda

However, the deep impact which the events of September 11 have made on the United States and on the American view of the world continues to shape the nature of transatlantic relations. Partners and institutions that are of relevance or giving support in the current situation are at the center of the U.S. perception of the relationship. Those who remain indifferent or become a cause for concern will at the very least shift to the margins of the relationship. A new transatlantic agenda addressing the issues of the 21st century is needed, together with long-term commitments from both sides of the Atlantic, and a strong political will to implement the necessary changes. When acting together, the U.S. and Europe require communication tools that are more far-reaching than those now in existence. As the following list demonstrates, there are windows of opportunity in many areas: Greater transparency, closer cooperation, especially with regard to the sharing of intelligence; a conclusive security strategy; adequate burden-sharing focusing on output goals; effective cooperation between ESDP and NATO; ongoing common support for the stabilization of southern central Europe; re-engagement in the Middle East peace process; a common strategic approach to the second round of NATO enlargement; and establishing closer political and economic ties with Russia.

Europe needs the attention and the normative power of American foreign policy. Conversely, America can significantly benefit from the resources of European economic power as a pillar of its peace and security structure - not only in the Middle East and in Africa, but also in trouble spots in Central and East Asia and Latin America. To this end, Europe must become more strongly involved in negotiations and political settlements. Developing solutions to global challenges - be it the environment, migration or social and ethnic conflicts - is not about preserving the primacy of security policy. Those who wish to make a real contribution in this area require partners and coalitions. And Europe and the United States together represent the ideal critical mass.

If the transatlantic partnership were to weaken, rivals of the West might play America and Europe off against one another by manipulating global competition between various economic

blocs. At a time when East Asia is unfolding its economic and demographic potential, such transatlantic rivalry would be detrimental to both partners.

Against this background we suggest that the Strategy Group on Security should focus primarily on the following three aspects of the transatlantic security agenda: the fight against terrorism, the future of NATO, and the new strategic partnership with Russia.

1. The Fight against Terrorism

International terrorism, although not a novel phenomenon, has added a new dimension to security, to homeland defense, and to defense policy. New concepts need to be developed for the security forces in order to professionally organize security, and to take strong countermeasures against professional terrorism. Combating terrorism is a task which affects all policy areas.

Having declared war on terrorism, and having specifically described Iran, Iraq and North Korea as the “Axis of Evil”, the United States must now back up its message with appropriate political and military action. As this emerges, partners and institutions that are of relevance in the current situation will be of central importance to the U.S. Those who remain indifferent or are unable to actively support America’s war against terrorism will move to the margins of U.S. perceptions.

The changing nature of transatlantic relations also affects institutions such as NATO, the cornerstone of U.S. engagement in Europe. After the first invocation ever of Article 5 of the Washington Treaty, only a few NATO member states were able - for a variety of reasons - to make a military contribution to the war in Afghanistan.

However, it was clear from the very beginning that the U.S., having been the main target of the terrorist attacks, and being the strongest military power, would organize and lead the response on the basis of its own assessments. Nevertheless, the start of the military operations made European efforts to build a European Security and Defense Policy (ESDP) - designed to enhance crisis management and rapid reaction capabilities - appear to be a fair-weather approach to responding to a crisis, and not a robust and practical instrument capable of tackling today’s strategic military missions.

The discussions should focus on the following issues:

- Establishing a credible anti-terror coalition
- Addressing the root causes of terror
- Enhancing control of WMD and ensuring non-proliferation
- Rebuilding Afghanistan
- Improving relations with the Arab countries
- Supporting and rebuilding “Failed States”
- Enforcing sanctions and establishing a common policy vis-à-vis Iraq
- Ensuring the security of the information infrastructure essential to economic globalization: preventing “cyber war”
- Facilitating a viable peace in the Palestinian/Israeli conflict
- Playing a peace-keeping role in the Indian/Pakistani disputes over Kashmir

2. The Future Role of NATO

NATO's current role as a mutual defense alliance is clearly at stake. There is growing evidence that NATO does not have a future as a purely military alliance. The current strategic situation requires local, regional and global crisis management, and not only territorial defense against massive military threats. Terrorism is clearly a global threat that calls for action on various different levels.

What does this mean for the future role of NATO? For a lengthy period there was considerable restraint in regard to the enlargement of NATO. A cautious and small-scale enlargement based on the available military capabilities was considered to be a possibility. Furthermore, there was the notion of “out of area or out of business”.

NATO now intends to go ahead with large-scale enlargement. The cooperation of Russia has been secured through active involvement in internal NATO decision-making. And the military discussions are now only concerned with specific security policy challenges, with out-of-area power projection in which geographical location hardly plays a role. What kind of alliance will emerge as a result of this new view of NATO? The answer may well be differentiated cooperation within NATO itself. What would this look like?

One way of looking at differentiated cooperation within NATO is to see NATO as a two-story building. The first floor would comprise collective security organized on the basis of large membership and some collective defense capabilities needed to orchestrate joint defense operations. The second floor would comprise advanced power projection capabilities based on national or collective intervention and peacemaking forces. Entry to the second floor would be based on clear-cut output criteria and the readiness to engage in strategic contingency planning and action.

Differentiated cooperation of this kind makes it possible to redefine the role of NATO and to adjust its tasks to the current political challenges. NATO would continue to be a strategic community.

In this area group discussion should center on:

- Strategic community or institution without a mission?
- Reflecting and defining the future role of NATO: operational and strategic issues (interoperability), capabilities, military budgets, military action, etc.
- Criteria for sensible NATO enlargement?
- EU and NATO: Separate enlargement processes or on the way to partnership?
- Parallel EU and NATO enlargement processes? (Turkey?)
- Common EU and NATO mechanisms and consultation procedures in the preparation of military operations?
- The “new cooperative relationship” with Russia within the NATO framework

3. A New Strategic Partnership with Russia

The crucial question remains: To what extent will the consequences of September 11 strengthen integration and cooperation between East and West, instead of moving toward single-issue short-term action. If Russia continues with its policy of becoming a modern European nation, the U.S. and the EU will be faced with the challenge of its growing

importance. Future developments depend on Russia's strategic choice of continuing to proceed with modernization.

The European Union and its member states fulfill several of the prerequisite conditions for a modernization partnership. The EU is the foremost customer for Russian exports, and, with a share of about 40 percent, EU member states are the biggest direct investors in Russia. The Union is also the most important provider of technical assistance to Russia. Furthermore, the support given to the central and east European candidate states in the shape of a combination of impending membership and external rule-setting for internal development has been a unique success story in the context of stabilizing transition processes. If and when Russia sets new goals for its transition, the Union should use its experience to stabilize internal Russian developments. EU policies implemented in TACIS, the technical assistance program, and ECHO, the humanitarian aid office could easily be adapted to meet the additional requirements. There is still no clear-cut concept for the structure of a common European economic area, though the transformation of security-related cooperation into a wide-ranging partnership might lead to renewed action in this area. Taking into consideration the requirements of Russian modernization, the economic relationship should amount to more than Russian energy exports to Europe.

Furthermore, the United States and Russia have recently experienced a period of rapprochement. Both countries share a common interest in combating terrorist networks. By sharing intelligence on these groups and by granting overflight rights, Russia can provide a great deal of assistance. Russia also has considerable influence in Central Asia, and may be able to persuade its allies, including China, to support the U.S. in its war against terrorism, especially with regard to providing military bases. The efforts at rapprochement recently led to the signing of the Rome Declaration and the establishment of the NATO-Russia Council, which provides Russia with the opportunity to cooperate in defensive action against common threats, and thus to become involved in a comprehensive catalog of NATO tasks.

In this area the discussions should concentrate on the following aspects:

- The U.S.-EU-Russia security pillar in the fight against terrorism, in the Middle East crisis, in Iraq or Israel, etc.
- Stabilizing Russia by establishing closer political, military and economic ties with the U.S. and the EU
- Possible Russian NATO membership (after fulfilling accession criteria)
- Environmental security: EU-U.S.-Russian cooperation in the disposal of nuclear waste and in nuclear facility security

Outlook

The Atlantic Alliance is in the process of changing in a fundamental manner. While Russia is moving closer to the Alliance, longstanding members are talking openly about weakening transatlantic ties. The worries expressed by the United States and its European allies with regard to the transatlantic relationship suggest that there is ignorance about the key role that the Alliance played in the the defense of the single most powerful group of nations which subscribe to the principles of freedom, democracy, the rule of law, equal rights and the market economy. These efficacious principles continue to attract an increasing number of new members. Even though they may not be enough to preserve the cohesion of the Alliance, they are of vital importance to the long-term success of the new transatlantic relationship. The lack

of confidence about the future role of the Alliance seems greater than the universal respect for the strength of the transatlantic relationship throughout the decades of its existence, its ability to adapt to new challenges and to deal with them as they occurred. Without the Alliance, East-West confrontation could have been neither successfully managed nor overcome; the unification of Germany might not have materialized and Western Europe would not have been able to start the process of integration leading to a pan-European Union.

September 11 confronted the Atlantic Alliance with a threat fundamentally different from anything it anticipated. The fact that the United States invoked Article 5 in response to the attacks on Washington and New York was something that took every nation by surprise and led to uncertainty with regard to the future. However, no one predicted the bloodless collapse of the Soviet Union, nor the appeal in 2002 by the President of the United States that Americans and Europeans should overcome their distrust of Russia, and his invitation to the former Soviet Union to play a prominent role in the international war against terrorism.

It is time to accept that these fundamental changes in international relations necessitate a fresh approach to transatlantic relations. While collective defense will remain a primary Alliance task, international security assistance will become a new challenge. There can be no collective defense without the international security assistance provided by the United States. Whereas it would be true to say that European critics of so-called American unilateralism are certainly not constructive, American critics who maintain that Europe is not pulling its weight belittle the strategic importance of Europe's contribution in political, economic, and military terms. Thus it is time to identify and assess the critical role of a continuing transatlantic relationship for both the United States and Europe in the emergence of a new international system, and to draw the correct consequences for the Alliance on the levels of concept, contribution, and structure.

Crisis management, helping Russia to fundamentally reform its political system and society, arms control and non-proliferation, stability and security in the Middle East, development in and co-operation with Central Asian countries and in the Mediterranean area are in the interests of both the United States and Europe. Neither will succeed unless transatlantic relations are transformed into a genuine give-and-take partnership. The combined political, economic and military might of all the transatlantic partners is needed if the success of the post-war era is to be taken beyond Europe. In order to stop and reverse the current trend in transatlantic relations, there needs to be an open and honest discussion that provides answers to the following questions. Why are the partners drifting apart? What can be done to ensure that the Alliance is ready to face the challenges of the 21st century?

The Economic and Trade Agenda

Nowhere is the degree of transatlantic interdependence and the potential for future cooperation more visible than in economic relations. Trade and mutual direct investment show a steady increase every year and have doubled since 1990.

1. Toward a New Conceptual Foundation

The two sides of the Atlantic interact constantly in a myriad of bilateral (e.g., Transatlantic Economic Partnership), plurilateral (e.g., G-7) and global (e.g., IMF and WTO) fora. They sometimes cooperate effectively in these settings, e.g., at Doha last year to launch a new round of global trade negotiations, and after September 11 to fight the financing of terrorism.

But such cooperation is sporadic and fitful at best. At present, it is overshadowed by disputes and disagreements across virtually the entire range of economic issues including:

- trade, where a cycle of retaliation and counter-retaliation threatens imminently;
- environmental and energy policy, which are of course closely related;
- a wide range of international financial issues, ranging from fighting the abuse of the international financial system (e.g. tax evasion and money laundering), to the proper role of the International Monetary Fund in rescuing crisis countries, to development aid and replenishment of the resources of the multilateral development and environment agencies.

One key reason for the unsatisfactory state of affairs is that the Europe-United States economic relationship is devoid of conceptual foundation. The current tendency is to address each issue "on its merits" on a case-by-case basis. There is no overarching strategic framework to inform, and help shape, the individual decisions. Not surprisingly, the result is often a hodge-podge of decisions that are often ineffective and/or contradictory, leaving both sides dissatisfied.

Even more serious is the risk that continuation of this pattern will produce a cumulative deterioration of the relationship. The real possibility of an outbreak of trade war is the most obvious case in point. But the eroding effect of continuing disagreement on such issues as the Kyoto Convention and the terms of IDA replenishment, will inevitably take a major toll on the transatlantic partnership (as well as on the substantive issue-areas that are failing to be resolved).

It is quite conceivable that these economic disputes could spill over into the broader political and security arenas, as they have in the past. The transatlantic security relationship, enshrined in NATO, has been amazingly resilient throughout the history of that organization - even when its own purpose and effectiveness was being questioned. There remain substantial communities of interest between Europe and the United States, ranging from their similar cultural heritages to their huge economic interdependence through trade and especially investment. But the absence of Cold War, and the differences of views that have now emerged on such central foreign policy topics as the Arab-Israeli conflict and policy toward Iraq, suggest that further escalation of tensions on the economic front could tip the broader scales in a negative direction (and perhaps vice versa).

One of the chief purposes of the “Future of Transatlantic Relations Project” of the Bertelsmann Foundation, with its parallel security and economic groups, is to consider such interactions between the two components of the overall relationship. The project will presumably seek both to avoid problems that one area could cause for the other and, indeed, to look for new strategies within each that could positively affect the other and steer the broader relationship onto a more satisfactory course.

2. Challenges for the Transatlantic Partnership

It is essential to recognize, at the outset of our project, that these current disputes and absence of any overarching concept reflect a number of deep differences between Europe and the United States. Many Europeans resent America's strategic dominance and recently superior economic performance. Many Europeans dislike, even reject, America's "buccaneer capitalism" by contrast with their own "social market economics." Most Europeans despise "American unilateralism" as opposed to their own alleged preference (realized in the context of Europe itself) for multilateralism and, worse yet, see the United States as "wanting to run the world with other people's money." Many Americans view Europe, for all its integration, as a squabbling cacophony of undynamic nation-states that fail to pull their weight in world affairs and look to the United States to do all the heavy lifting when the going gets tough.

For all these reasons, Europe and the United States need to make a renewed major effort to work out a strategic concept to guide their economic ties. One such concept would be a "G-2" Informal Consultative Mechanism for the world economy. Such a new mindset for the transatlantic relationship would have two major advantages: it would provide an overarching framework for economic ties between Europe and the United States themselves, properly placing such tendentious but essentially minor issues as beef and steel within a much broader context, and it would induce both to coordinate their approaches to the rest of the world in a manner that could provide constructive leadership over a wide range of global economic topics.

A "G-2" strategy would imply an agreement between Europe and the United States to see their bilateral economic relationship in the broader context of effective management of the global economic system. They would of course continue to pursue their "national" interests. But they would do so within the context of accepting responsibility for leadership of the international economic order and take their decisions on individual policy issues in that framework.

The world clearly needs such leadership and, for better or worse, Europe and the United States are the only two players who can provide it. Japan was once viewed as a potential partner in a leadership "G-3" but it never assumed a major role commensurate with its capabilities even when it had a chance to do so. Now its decade of decline, and over the longer run the dramatic aging and likely sharp decline of its population, have led to its being challenged (by China) for leadership of its own region let alone a global role. China is obviously the rising power in both economic and security terms but its capacity for global leadership is still a decade or two away because it remains a very poor country, is not yet a full market economy and is obviously not yet a political democracy. Any new "G-2" Consultative Mechanism could of course be open-ended and add one or more rising powers when they reached an appropriate point.

By contrast, Europe and the United States are now strikingly similar in terms of their economic size and structure. Europe's population is about one-third larger (400 million to 300 million). America's economic output is about 20 percent larger at market exchange rates (\$10

trillion to \$8 trillion) but that superiority is due to the overvalued exchange rate of the dollar (as output levels were virtually identical in dollar terms in 1999 when the euro was created), which now seems to be in the process of being corrected. The external trade levels of the two are virtually identical at about \$2 trillion. They are equally dependent on external trade (at about 25 percent each for exports plus imports of goods and services).

To be sure, the US economy has performed considerably better than Europe's over the last decade or so. US productivity growth has increased sharply and now clearly exceeds Europe's. Job creation, in particular, has been much stronger in the United States. On the other hand, Europe's downturn in 2000-01 was much shallower than America's. Presumably because of its more extensive (indeed excessive) social safety net, Europe has suffered less backlash against globalization than the United States. But this fairly sharp difference in current performance must be taken into account in fashioning any new "G-2" and could significantly complicate the process.

It should be noted, however, that Europe and the United States have sometimes already functioned as a "G-2" in trade, where Europe has spoken with a single voice since the creation of the original Common Market and hence has wielded as much systemic power as the United States. Europe and the United States have gotten together sufficiently to move the global trading system forward through the Kennedy, Tokyo and Uruguay Rounds in the GATT/WTO - the three major liberalizing and rule-making trade initiatives in the postwar period. Even on trade, however, the "G-2" mindset seems to have foundered of late as indicated by the raft of current disputes. In addition, there are periodic cases where EU-US trade cooperation has hurt the rest of the world, such as their parallel abuse of antidumping policies and huge payments of agricultural subsidies. A renewal of their conceptual foundation is urgently needed.

The practical alternative to a "G-2" Consultative Mechanism is in fact not a broader group but rather a "G-1" consisting solely of the United States. By default, global leadership in fact often occurs through that device. Its frequent recurrence, however, is unhealthy both for Europe (which then feels simultaneously frustrated and ignored) and the United States (because the outcomes are normally unsatisfactory and a bad habit is encouraged). In the light of today's widespread concerns around the world over the unilateralist tendencies of the United States, this would be a particularly opportune time to launch a "G-2" approach to global economic management - with beneficial spillover to world politics and security issues, and hence to the other component of the Future of Transatlantic Relations Project.

Adoption of the "G-2" concept would have profound implications for both Europe and the United States. Europe would have to organize itself to speak with a single voice on a much wider array of issues, including all those specifically addressed by the "G-2," as it has previously on trade but only a few others (competition policy and some monetary issues via the European Central Bank). The United States would have to support such increased European integration and accept full European partnership even though its superior economic performance of late, as well as its overwhelming military strength, tempt it to opt for a "G-1". Both adjustments, however, seem considerably less costly than continuation of the unsatisfactory status quo.

Even the most effective "G-2" would not of course be able to run the global economy by itself - nor should it try. In today's pluralistic world, small industrial countries and many emerging market countries must be brought into the management of the system in order to re-establish its legitimacy. Hence the multilateral institutions are more important than ever and there is room for a G-7, G-20, G-77, regional groupings in other parts of the world and many others. But an informal steering mechanism at the center is a necessary, albeit not a sufficient, condition for global prosperity and stability. Only Europe and the United States can create and maintain such a group, at least for the foreseeable future.

3. Specific Issues

A "G-2" Consultative Mechanism would of course be useful for its members, and acceptable to the rest of the world, only if it could deliver improved performance and policies by Europe and the United States on important tangible issues. Within the conceptual framework and new mindset of a "G-2", there are many specific topics that our Transatlantic Strategy Group could address in an effort to provide a basis for such progress. Six seem to be particularly good candidates because they are both of central importance and sufficiently difficult that our governments are having major problems in resolving them: trade, international finance (including the respective roles of the two regions' capital markets), the energy/environment complex, immigration, corporate governance and global poverty. After considering these six, and perhaps others that will come up in our first discussion, the Group might want to choose two or three for its initial focus.

Trade is an obvious candidate because Europe and the United States already stand on the brink of a trade war - despite their history of cooperation in this area in the past, suggesting a substantial deterioration of the relationship. Part of the remedy might be to remand some of the current disputes to the new Doha round in the WTO including the FSC issue via a fresh look at the system's tax rules, aircraft via reconsideration of the Subsidies Code and regional deals (e.g., EU-Mercosur and NAFTA) via a strengthening of the relevant WTO articles. Another alternative, which is complementary, would be to broaden the "peace clause" in agriculture, which was agreed to preclude new WTO cases in that contentious area until the end of 2003, to cover additional sectors and perhaps to extend it until the target date for completing the Doha round (2005).

The basic point on trade, however, as on all the other specific issues, would be to see each specific dispute within the broader "G-2" strategic management context rather than as a bilateral mercantilist struggle. Such a change in mindsets would go far to promote constructive resolution of the individual disputes, a much stronger transatlantic relationship and a much more functional global trading system.

A second important and difficult area is international finance. Here too there is an important conceptual and structural issue: the creation of the euro, which over time can be expected to play a steadily growing international role and could eventually move up alongside the dollar as a global key currency.

So far, however, the euro has been consistently weak against the dollar. Partly as a result of the correspondingly strong dollar, the United States is running annual current account deficits of almost \$500 billion (5 percent of GDP) and hence must attract net foreign capital imports of over \$2 billion every working day to balance its books. These deficits are again rising rapidly (about \$100 billion in 2002), are projected to reach 7 percent of GDP (about \$800 billion) by 2006 and come on top of an international debtor position that already exceeds \$2 trillion. Unless all economic history is repealed, the dollar will fall sharply - by at least 20-25 percent on average - within the next few years. Recently, the process might have started.

The results of a fast and sharp adjustment would be severe for both America and Europe. A sharp decline in the dollar would almost certainly mean a jump in inflation, higher interest rates and another dip in the stock market for the United States. A sharp rise in the euro would hurt Europe's competitiveness in the short run and further retard its sluggish economic growth. Both thus have substantial incentive to avoid a "hard landing". In addition, the far-reaching impact on the rest of the world of a sizable US current account correction would be a

major topic for a "G-2" (and hence for our Group). Therefore both sides should have ample incentive to start consulting and cooperating closely in this area.

One important aspect of the international monetary issue is the relationship between the European and American financial markets by 2005. Europe is working hard to complete the integration of its money and capital markets, and its success in doing so will probably go far to determine the pace at which the euro assumes a major international role - since this is an area in which the US markets are still superior on most counts. Indeed, the euro is unlikely to seriously challenge the dollar for international currency supremacy until the European financial markets come to approximate those in the United States. Hence the intensive interaction between the two sets of markets will have far-reaching economic and even political consequences, and should also be managed within the conceptual framework of a "G-2".

A third key area is the environment, of which energy policy is of course a major component as well as an issue of critical independent importance. Here the two sides of the Atlantic are at loggerheads. On global warming, Europe is starting to implement the Kyoto Convention while the United States, starting with a unanimous vote in the Senate well before the advent of the Bush Administration, has denounced the entire concept. On energy, European prices are three to four times as high while the share of gas-guzzling SUVs has reached 50 percent of all additions to the US motor vehicle fleet.

A complex mix of conservation, fossil fuel production, alternative energy sources, financing techniques, foreign policy and even military postures is of course involved in devising coherent policies in this area. Europe and the United States could learn considerably from each other's experiences and should, at a minimum, avoid contradicting each other's approaches. Cooperation to date has been limited to the most rudimentary of defensive measures against the OPEC cartel, the creation of strategic oil stockpiles via the International Energy Agency in the OECD, and some joint financing mechanisms (as via the World Bank). These issues have become increasingly crucial due to recent and prospective events in the Middle East.

A fourth possible topic is migration, which also has a wide variety of crosscutting effects across all of our countries. The recent French and other European elections highlight the political importance of the topic but it has already been having a major impact on national economies and social cohesion. The topic is one of the most difficult that our governments are likely to face over the foreseeable future.

Migration has been conspicuously absent from most international discussions, whether in the WTO concerning possible new international rules for labor markets (to complement those on the movement of goods, services and capital) or bilaterally across the Atlantic. This might in fact be an issue-area where "G-2" cooperation would focus more on transatlantic leadership of a new global debate, and possible multilateral rule-making, than on tangible bilateral initiatives. However, Europe and the United States might also be able to learn a good deal from each other's experiences in responding to the issue, particularly with the increasing similarity of ethnic origins of some of the groups migrating to both (e.g., from the Muslim world). The pros and cons of migration are obviously seen differently in different countries in our transatlantic region and a discussion of those disparities, as well as some of our more common views, could be extremely enlightening and an essential prerequisite for effective policy formulation.

A fifth issue to consider addressing is corporate governance. The Enron and related scandals in the United States highlight again some of the weaknesses of the "Anglo-Saxon model," and the US reforms that are evolving in their wake (e.g., a greater US willingness to

accept international accounting standards) may be helpful in renewing constructive transatlantic debate on the topic.

However, profound questions remain concerning the relative efficiency of the different governance models that exist across our countries. One component is the very different systems of corporate finance that persist, ranging from the *Hausbank* model in Germany to the heavy reliance on corporate bond and money markets in the United States. Different methods of board composition and responsibility may deserve a fresh look. So may the whole range of corporate infrastructure variables including accounting and legal standards, transparency and anticorruption approaches, and securities and other relevant regulation. This too is an area where "G-2" leadership could be important for the world as a whole, given the salience of these issues in recent financial crises in East Asia and elsewhere (and the competing alternative of "the Asian way" despite its recent setbacks).

A final possibility is global poverty. Particularly in light of September 11, security as well as humanitarian concerns suggest an emphasis on this topic. Africa could be an obvious focus, as at this year's G-8 summit. The specific topics involved cut across a wide range of economic issues: trade, private investment, foreign assistance, migration (per above) and numerous others.

The European Union and the United States have recently pledged substantial increases in both their foreign assistance levels and access to their markets for the exports of the poor countries. However, their aid levels are still far below the international norm (0.7 percent of GDP) and they persistently adopt new policies that retard market access (e.g., the recent US steel safeguards and farm bills). Concerted and bold new action by the "G-2" is essential if the poorest countries are to be given a genuine opportunity to emerge from poverty.

Outlook

Other issues could be cited for possible consideration by our Strategy Groups. However, it probably behooves us to focus on a small number of the highest priorities at the outset of our work.

We hope that this background paper will help pave the way for fruitful discussion of such possibilities at the initial agenda-setting meeting in Berlin. We look forward to the Groups' making initial choices that will both get it off to a good start and offer the prospect of its making a major contribution to the public debate within a relatively short period of time!