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E-NOTES

"A nation must think before it acts." - Robert Strausz-Hupé

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THE CURRENCY OF POWER: ECONOMICS & SECURITY IN U.S. FOREIGN POLICY

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The following is the transcript of his Keynote Address to the FPRI Annual Dinner on November 9, 2015, on the occasion of FPRI's 60th Anniversary as well as the 25th Anniversary of FPRI's Marvin Wachman Center for Civic and International Literacy.

Thank you for inviting me to speak at the Foreign Policy Research Institute's 60th anniversary event. It's an honor to be with you. I have great respect for the contributions of FPRI and have been the beneficiary of its scholarship and publications over many years. I recall fondly my government service with the late Harvey Sicherman, who went on to ably lead FPRI for many years, and I am pleased that Alan Luxenberg has assumed the helm of this valuable institution. Thanks to all of you for supporting it.

In particular, I have appreciated FPRI's commitment to the study of history as a basis for understanding America's global engagement. FPRI's project to assist high school teachers to learn—and I hope, teach—lessons from America's wars produced a wonderful set of papers that I read avidly.

With that spirit of historical appreciation it is certainly appropriate to recognize that we are gathered on the eve of an important birthday—of the U.S. Marine Corps, founded in this very city 240 years ago. I am not sure that the Society of Friends had the Marine Corps in mind when they committed this metropolis to "Brotherly Love," but Semper Fidelis at least sounds like a fraternal virtue.

Since we are in Philadelphia, I will open with a local story, which I learned from my first professor of diplomatic history.

On June 20, 1782, the Congress of the United States, meeting in Philadelphia, approved the recommendation of an official Seal for the new country. This Seal was significant: It would both stamp important national documents and convey the Founding Fathers' vision to the world and future generations. Approval of the seal was no rushed decision. Indeed, since the committee to design the Seal had been created by a resolution of July 4, 1776, our forefathers had taken as long to agree on the Seal as to win their war of independence.

To help you recall the Great Seal of the United States, I need some technical support. But my audiovisual tools are limited. Therefore, for those of you with wallets, please check to see if you have a dollar bill. Conveniently for my story, the U.S. Treasury has reprinted the Great Seal of the United States on the back of your dollars.

In seeking approval of the Seal in 1782, Charles Thomson, Secretary of the Congress, described its design to the assembled representatives. The reverse of the Great Seal, Mr. Thomson explained, portrays an uncompleted thirteen-tiered pyramid of states, overseen by the eye of Providence. The Virgilian phrase above the image, "Annuit Coeptis," reveals that a higher force has favored our undertaking. Thomson also observed that the phrase below the pyramid, "Novus Ordo Seclorum," New Order of the Ages, signified "the beginning of a new American era" that commenced with the Declaration of 1776. As Professor James A. Field, Jr., explained, "It remains unclear whether [Thomson's use of] the adjective 'American' [in describing this new era] is to be construed as geographically limiting or as broadly descriptive…." "Much of American history," Field concluded, "is implicit in this question."

Of course, the new American era, this New Order of the Ages, required a new U.S. government, the product of yet another convention in Philadelphia. In contrast to other governments of the 18th Century, the new U.S. government was created for special, limited purposes: The Declaration of Independence states that governments are instituted to secure certain unalienable rights, among them life, liberty and the pursuit of happiness. The U.S. Constitution prescribes the powers of the American government, and the Bill of Rights specifies limits on those powers.

In the new era of 1776, individual liberty and initiative would be the spark of America's energy, at home and abroad. The Exceptionalism of America has been that America's essential power is found in the dynamism of its citizens—not in monarchs, aristocratic nobles, priests or clergy, officers with gold braids, or even ranks of government officials. Americans have been explorers, engineers, and entrepreneurs—also merchants, missionaries, mechanics, and mariners. According to your eminent local historian Walter McDougall, in his magisterial Throes of Democracy, America has been a country of "hustlers," too, with the full range of qualities associated with that term.

Those restless individuals shaped U.S. foreign policy, as well as the nation's development. Tonight, I will focus on one dimension of their intrepid spirit.

For America's first 150 years, U.S. foreign policy was deeply infused with an economic logic. I believe that the rise of the "national security" concept after World War II diminished America's appreciation of the economic dimension of foreign policy, and that we now need to rediscover our heritage of relating economics to our security.

Indeed, strategic thinkers of the late 18th and early 19th Centuries acknowledged this reasoning, and were highly attuned to connections among economics, national strength, military capabilities, and political power. Writers such as Adam Smith, Alexander Hamilton, and Friedrich List recognized the vital interrelationships, although they proposed different ideas on how to advance economies, societies, and statecraft. But the strategists who founded the "national security state" at the start of the Cold War transformed economics into the unappreciated subordinate of U.S. foreign policy.

At best, the role of economics in U.S. strategy has been assumed, not analyzed. We scarcely understand its effects on power, influence, diplomacy, ideas, institutions, and human rights. At worst, economic problems have become a justification for a "come home America" isolationism. And economists—absorbed with mathematical models and debates on Quantitative Easing and stimulus polices—are content to operate in their separate universe.

I would suggest that America's future foreign policy strategy should be founded on the recovery of that lost tradition of uniting economics and security. To gain perspective on economics and security from America's past, let's look back a few years… say—242 of them.

In 1773, a tribe of Bostonians threw 342 chests of tea into the harbor to protest taxes imposed to bail out the nearly bankrupt British East India Company. (Notably, they were careful not to destroy other property.) The incident was the most dramatic of waves of colonial "nonimportation" policies dating to the 1760s, early American efforts to employ trade as a tool of policy.

The new American republic was born amidst a world of mercantilist empires. Navigating around the trading monopolies of the established powers, the former American colonies fought for "freedom to trade." The young United States, under President Thomas Jefferson, experimented with nonimportation acts and even a disastrous embargo on foreign commerce in 1807. Ironically, it took the failure of Jefferson's trade sanctions, as well as the War of 1812, for the United States to start developing the manufacturing base that Alexander Hamilton sought and Jefferson opposed. Britain was not the only object of the new country's economic security policy. From 1801 to 1805, in the face of the Barbary pirates' attacks on U.S. ships, Jefferson rejected demands for tribute and instead sent the U.S. Navy to the shores of Tripoli—as memorialized by the U.S. Marine Corps hymn.

In an age when power arose from the expansion of territory, resources, people, and commerce, America's implicit strategy understandably concentrated on the North American continent and open immigration. Land and settlement provided security, especially when buffered by two vast oceans. Wielding a lost tool of diplomacy, the United States resolved disputes by buying lands: Louisiana; Florida; old New Mexico; California; the Gadsden Purchase; Alaska; and even the Virgin Islands at the start of the 20th Century. (Admittedly, in some cases use of force led to price discounts.) Ironically, Jefferson needed Hamilton's Bank of the United States and credit system, which the Virginian had opposed, for Jefferson's greatest achievement, the Louisiana Purchase. And there were the deals that fell through—such as Secretary of State William Seward's unsuccessful push to buy British Columbia in 1867—a land bridge to his new purchase of Alaska!

The theme of Western Hemispheric integration—a partnership of young democracies, not an empire—was advanced by Secretary of State Henry Clay in the 1820s, revived in the 1880s and 1890s, and found first fruits a century later in the North American Free Trade Agreement and then five more U.S. free trade agreements with Latin America. Today, the partners in those free trade agreements account for more than half of the hemisphere's non-U.S. GDP. In the 21st Century, comprehensive free trade agreements could turn out to be the ties that bind, like the alliances of old.

The Federalist Papers, the touchstone of American Constitutionalism, are replete with references to the need for a strong federal government to secure the United States' place among foreign countries, including through healthy commerce and credit. The founders understood the link between economics and security. In a prescient example, John Jay, in Federalist No. 4, cautioned in 1787 that trade with China and India could one day draw the United States into conflict with competitors.

The oceans that were barriers to armies became highways for the U.S. Navy and American mariners seeking markets. In 1854, Commodore Matthew Perry "opened" Japan to trade. By 1899, Secretary of State John Hay was resisting carving up China, as Africa had been, in favor of an "Open Door" policy to secure equal commercial opportunity. Over time, the U.S. maritime links with the eastern and western borders of the great Eurasian landmass also reflected a geopolitical logic: the U.S., as a maritime power, reaching across oceans from an island-continent, did not want one power to dominate Eurasia—whether the Nazi-German and Imperial Japan Axis or the Soviet Union.

This race through U.S. history is not intended to suggest that the American system was all about peaceful commerce. To the contrary, even if the connection was driven by interests and not explicit planning, the economic and security policies worked hand in hand. These interests were also infused with a healthy dose of what those generations called spreading "civilization," and what we call "values." With trade and the flag came missionaries and their schools.

As the United States settled its home continent around the opening of the 20th Century, a debate arose about expansion to territories beyond U.S. shores. Some wanted markets or coaling stations, and others sought to carry so-called "civilization" to foreign peoples. Some simply wanted to keep strategic places out of the hands of others. But "imperialism" did not sit well with many Americans, who proudly recalled that their new nation had freed itself from old empires. The U.S. War with Spain in 1898, precipitated by conflicts over Cuba, led the United States to acquire the Philippines (for $20 million) to keep the islands from being grabbed by others whose fleets were hovering. But the United States did not take Cuba. A few years later, President Theodore Roosevelt stirred up a revolt in Panama so he could build a canal that linked the two great oceans, commerce, and fleets of the U.S. Navy.

America's foreign economic policy also helped spur early interest in international law—what we now call "rules-based systems"—to resolve disputes. The United States was an active participant in the 1899 Hague Conference and lent its support to a convention to resolve disputes peacefully through third-party mediation, international commissions, and a Permanent Court of Arbitration.

The decades that followed continued the pattern of melding U.S. economic interests with foreign and security policy. "Dollar diplomacy," as historians have dubbed the strategy, sought to support U.S. enterprises in Latin America and East Asia through what we now call transnational actors—but in those days were railroad and mining engineers, bankers, and merchants. In World War I, Britain shrewdly played on the U.S. commitment to neutral rights on the seas to draw President Woodrow Wilson to its side against Germany and its U-boats.

After the war, reacting against what the United States viewed as the old European politics of perpetuated hostilities, America withdrew from European military security. Yet even during the 1920s and 1930s, the United States relied on banker- statesmen to negotiate debt and reparations to revive broken economies in Mexico and Germany. Reeling from the Great Depression, however, America withdrew from the world economy, enacting the Smoot-Hawley tariff wall to block imports and subverting a last-gasp effort for international economic cooperation at the 1933 World Economic Conference. Political-military isolationism followed economic retreat.

Then came 1941, and the United States again learned, through harsh experience, that economics and security were linked. Franklin Roosevelt had imposed embargoes on the sale of petroleum and scrap iron to Japan in response to Japan's invasion of China and its threats to Southeast Asia. Imperial Japan responded with a surprise attack on the US Navy at Pearl Harbor and a bold assault ranging from Malaya and Singapore to the Philippines in order to secure resources for its war economy. The United States, caught unprepared, paid a terrible price. Fortunately, the Japanese planners left the huge American fuel tanks in Hawaii untouched, revealing their economic security oversight. In 1942, the Japanese invaded American territory in the Aleutians, a reminder today that Alaska is the northern flank of the Asia-Pacific theater.

The end of World War II and the opening of the Cold War led to a sharp break in the American foreign policy tradition. The dawn of the nuclear age and the face- off between communism and the West required a new approach: a national security strategy. For the first time, the United States maintained a large conventional army, a significant part of which was based in Europe, with hundreds of thousands of other troops fighting in Asia over decades.

Contrary to Milton Friedman's idea that economic freedom is an end in itself and an indispensable means toward achieving political freedom, economics became a resource factor—and the handmaiden of the strategic policy process. The U.S. National Security Act of 1947 is full of references to new offices to mobilize people and resources for total war. Yet the Act did not even make the Treasury Secretary a statutory member of the new National Security Council. Ever since, the U.S. government has struggled to integrate economics into its national security strategies.

I think we need to rewrite economics back into the narrative of the Cold War and then consider the applicability of economics to US strategy today.

Even as World War II raged, the United States began creating new international economic institutions to address currency exchange rates, trade, reconstruction, and development. The United States and Europe then launched the Marshall Plan—and Europe created an economic community —to shore up the free world's economic foundations. The United States exported capital and imported goods to boost recoveries in Europe, Japan, and then South Korea and other developing countries.

The economic internationalists of the Bretton Woods system and the European Economic Community were not driven primarily by a plan for "containment" or to counter the Soviet Union. These strategists were trying to avoid a repeat of the economic causes of the political and security breakdown in the 1920s and 1930s. Only over time did the imperatives of the Cold War lead to a pragmatic convergence of the national security planners and the economic designers. Still, the national security model treated the economy as a source of benefits to be exchanged to support security aims. It assumed economics was about static sources of resources for the accounting and balancing of power.

This perspective of state power overlooked a vital reality: that sound economic policies are the underpinning of both individual freedom and national power—not only military power, but also the dynamism, innovation, and influence of the economy and society. The 20th Century concept of national security also overlooked how economic change can be a powerful force of its own in international relations.

President Dwight Eisenhower appreciated this distinction. He invested political capital in balanced budgets, controlling the size of government, and sound monetary policies. He recognized the underlying strength generated by investments in national highways, education, and science.

In the 1970s, the world economy stumbled toward a new reality of floating exchange rates, oil shocks, big bank loans of petrodollars to developing-world sovereigns, and stagflation. As the U.S. economy faltered, so did American influence.

Ronald Reagan intuitively understood the connection between national economic revival and foreign policy. His priority was to revive capitalism at home—and then extend it to the world. Margaret Thatcher, his stalwart ally, shared his vision. The promotion of global capitalism seemed to be disruptive to many, the antithesis of rebuilding an international economic system still reeling from the shocks of the 1970s. Yet, this very disruptive quality enables capitalism to respond flexibly and continually to technological and other changes.

The reform of capitalism was not just an Anglo-American venture. West Germany's commitment to sound economic policies and export competitiveness demonstrated that social market economies can work. East Germans watching West German TV saw the stark contrast between their grim existence in a "workers' paradise" and the lifestyles of their wealthier cousins. Japanese manufacturers responded to the oil shocks with a huge increase in energy efficiency.

The Soviet Union could not adapt to its economic challenges. It could not cope with changing information technology, new drivers of productivity and competition, and eventually $15-a-barrel oil. The U.S. intelligence community, geared toward the Cold War calculations of national security, largely missed the story. Soviet leader Mikhail Gorbachev, facing the combination of the democracies' economic regeneration, the U.S. military buildup with advanced technologies, and transatlantic solidarity, concluded that he had to reform communism. But his "perestroika" didn't work.

Reagan believed that international institutions should boost growth, opportunity, and human rights. Moreover, at a time of economic flux, the international economic system needed to adapt. Reagan did not want international rules to constrict domestic economic revival, and he stirred controversy by rejecting counterproductive international schemes.

In Reagan's second term, the United States steered the International Monetary Fund to a new role in the Latin American debt crisis. It led a major recapitalization of the World Bank to support developing countries' economic reforms and debt reschedulings—until banks could write down losses. In 1985, Treasury Secretary James Baker launched a process of international economic coordination in the G-7. The United States pushed to expand global trade through the launch of the

Uruguay Round of trade talks, completed much of that negotiation under President George H.W. Bush, and closed the deal under President Bill Clinton to create the WTO. Bush also initiated the Asia-Pacific Economic Cooperation (APEC) forum and negotiated NAFTA, which Clinton enacted.

The economic revitalization of the West helped to achieve its national security aims in Europe with hardly a shot fired. Europe was reunited. The European Community became a deeper, wider union and launched its own currency. Just as importantly, China, India, and other developing countries moved from planned socialism and import-substitution schemes to market competition. Over a decade, the number of people engaged in or actively affected by the world market economy surged from about 1 billion to four or five times that. Large movements of capital, trade, and people—all spurred by new technologies—created a new era of globalization

Yet the adaptation to markets on a truly global scale, integrating developed and developing countries alike, was bound to be complicated and disjointed. In the late 1990s, countries in East Asia and Latin America faced harsh financial blows and painful restructurings. The recovery strategies of some developing countries planted the seeds of a new problem: "imbalances"—whether of savings, reserves, trade accounts, or other dimensions. Developing economies in East Asia saved and exported more, and the United States and some European countries increased borrowing, consumption, and imports. Some economists maintain that the low prices of goods available from new suppliers led central bankers to persist in easy monetary policies for too long, risking widespread asset-price inflation, especially in real estate markets. Then the bubbles burst.

The institutions of the international economic system adapted incrementally, often with difficulty. In the 1990s, the economic firefighting of the IMF and World Bank made them principal targets of an anti-globalization movement. Unfortunately, neither international nor domestic supervisors of financial markets kept up with the innovations—or the frauds and foolishness that inevitably come with long boom periods.

The WTO added many new members. The trading system withstood terrorist attacks—and fears of more. But the travails of the WTO's Doha Round of trade negotiations, launched in 2001, signaled a new challenge. The traditional developed economies wanted the rising middle-income countries—China, Brazil, India, and others—to assume more responsibility for lowering barriers to trade, while all would offer special treatment for Africa and the poorest. The major developing economies, in turn, pointed to their large numbers of poor people and wanted to maintain special privileges. This debate reverberates today not only in trade, but in monetary affairs, investment, development, energy, and the environment.

One of today's vital economic issues—highlighted by China's challenge—is whether major developing economies can rely more on domestic demand so as to create more balanced growth models, domestically and internationally.

The 9/11 attacks concentrated America's attention on terrorism, homeland security, and the long wars that followed. Yet the connections of economics to the new security threats are also strong. When al Qaeda targeted the United States, it aimed for the World Trade Center—its twin towers the symbols of American capitalism—as well as Washington. In addition to shock and destruction, the terrorists wanted to strangle economic and political freedom.

Even as America fought in Iraq and Afghanistan and against terrorist threats around the globe, other forces of history did not stand still. China, India, and other emerging economies began to change the landscape of power. The failed political and stunted economic systems of North Africa and the Middle East sparked upheavals that have broken down old state borders and left the region in turmoil.

So how might a revival of an integrated approach to economics and security guide America's strategy today? Let me close by suggesting six ideas.

First, the United States needs the revival of healthy economic growth to be able to lead. This imperative is more than a matter of generating economic resources and preserving America's good credit, although both are vital. America's very identity on the global stage depends on its economic dynamism and ability to reinvent itself. The U.S. private sector continues to stand out among developed economies for its power of innovation—to be seen, for example, in energy, the use of Big Data, software, bio-engineering, and robotics. The U.S. Government, in turn, has been preoccupied with stimulus policies—fiscal and monetary—and has not paid enough attention to structural and productivity reforms that would boost the handoff of growth to the private sector. To offer just a few examples:

- Tax reform and disciplining the growth of entitlement spending would unleash a new surge of growth.
- An immigration reform that encouraged the world's talent to come to America would be good for both economic and foreign policy.
- And more competition, choice, and private sector investment in education and training services—combined with high standards—would help the American people develop their capabilities to the fullest while contributing to a larger national good.

Second, the U.S. should build a strong continental base through deeper North American integration. Consider the global weight of three democracies, of almost 500 million people, with energy self-sufficiency and even exports, more integrated infrastructure, complementary manufacturing and service industries, and a shared effort to develop human capital—through education, linked to workforce skills and pro- growth worker mobility policies. The international economic policies of the three North American countries are already closely connected—and over time I believe there could be closer alignment on foreign and security policies, too. Last year, retired General David Petraeus and I released a report on North America for the Council on Foreign Relations. It suggests how North America could be the "continental base" for projecting US power globally by deepening three-way cooperation and integration on energy, economic competiveness, security, and the building of a North America community.

Third, the U.S.—and I hope North America—needs a combined economic and security architecture that connects us with our principal partners on the western, eastern, and southern borders of Eurasia. The Trans-Pacific Partnership, TPP, and the Trans-Atlantic Trade and Investment Partnership, TTIP, could provide such an economic foundation. The TPP, concluded just last month, now faces the challenging hurdle of Congressional approval. TTIP is lagging. I hope the Administration will transform its rhetoric into creating sufficient momentum so that TTIP will be high on the agenda of the next President.

The complementary security challenge is to devise new strategic military postures that assure stability—based on new technologies and capabilities—embedded in alliance ties, especially with Japan, Korea, Australia, and ASEAN partners. NATO must also demonstrate the ability—and will—to defend its eastern members from Russian revanchism. Changing security responsibilities—especially in the Western Pacific, on the eastern frontier of NATO, and all across the realm of potential radical Islamic terrorist bases—require adjustments in U.S. strategies, equipment, positioning, and use of technologies. This transformation will not be possible if we continue Defense Department budget cuts. Equally important, the four security domains of land, sea, air, and outer space need to be complemented by a fifth—cyber. Cyber security will require an unprecedented partnership among the sectors of intelligence, security, and private enterprise. Cyber security is the new necessity for civil and national defense.

Fourth, the U.S. needs an international economic strategy to partner with rising developing economies seeking to overcome the Middle Income Trap. The initiative should combine trade liberalization efforts—in WTO negotiations and bilaterally—with innovations in multilateral development institutions and private sector investment. There are huge opportunities and needs, for example, in infrastructure, including through public-private partnership investments; in human capital, including though educational innovation and support for girls and women; in private sector services, including in areas traditionally seen as public, such as education, health, and water; and in financial markets, so capital is invested productively. The U.S. should customize political economy approaches to each major Middle- income country and with groups of countries—such as the Pacific Alliance of Mexico, Colombia, Peru, and Chile; ASEAN; and subregional groups in Africa.

Fifth, our continuing military ventures in Afghanistan and the wider Middle East need complementary economic plans. Successful counterinsurgencies—and fragile states—need a combination of security, effective governance, and economic development. The record demonstrates that local ownership of these responsibilities is fundamental to sustainable success.

Societal transformations depend on people assuming responsibility for their own future. We can encourage and support. We can help provide protected space to develop and demonstrate governance. We can help supply a cushion of time. But ultimately they must decide. And the Muslim world will need to face up to violent Islamic radicalism. We cannot solve that problem for Muslims, but we can support those who try.

Fortunately, there are now a host of successful political economy experiences from which others can learn and which can be customized for their own circumstances; the U.S. and multilateral institutions can assist in sharing this comparative experience. Economic openings will not solve all problems, but they are an important start. Economic openness and expanding middle classes can also offer a route to advance America's values,—human rights, the rule of law, political liberalization, and democracy.

Economic strategies, as in past wars, are also critical to defeating our enemies. The Islamic State's maxim is to "endure and expand." This imperative reflects the dictate under Islamic law that offensive jihad must be based on holding territory. We need to attack the economic underpinnings of this cruel Caliphate—its oil sales, smuggling, finances, and sales of antiquities.

We also need an economic humanitarian component—for strategic as well as ethical reasons. If the United States and its partners decide to help establish and defend safe zones in which a legitimate Syrian opposition to both the regime and ISIS can organize, these protected places could provide refuge for the millions of displaced Syrians. A well-organized humanitarian support mission—such as the one the United States created for the Kurds after the first Gulf War—could help build the legitimacy of an alternative Sunni movement. Also, Europeans should also now recognize that humanitarian support in Syria is vital to stemming the flow of refugees to the EU. A failure to act will leave millions of people without education for children, livelihoods, hope—and create a breeding ground of future disasters.

Finally, the U.S. needs to develop a satisfactory working relationship with China, which is in the midst of an historic transformation. We cannot predict the course of change in China. I continue to believe that the two countries have a shared interest in China's effective integration within the international economic, political, and security system that the U.S. led in creating—so that China would become a "responsible stakeholder" in that continually evolving system.

Of course, the U.S. and China will have differences to manage. And cooperation will be accompanied by hedging and balancing. If China acts aggressively, as it has in the South China Sea, it will provoke counter- reactions. The US needs to be positioned to offer appropriate reassurances about our defense of core principles—such as freedom of navigation—to Asian friends under pressure. Cyber attacks will need to be thwarted—and deterred—by countermeasures that raise the costs. This strategy will require a newly-designed U.S. governmental and private sector cooperation. But there are many mutual interests between China and the United States, too—for example, connected to China's structural economic reforms.

To manage China's rise, the U.S. needs to maintain its <u>own</u> power: through a strong, dynamic U.S. economy, with debt under control and sound credit; in a powerful North America; with alliances, partnerships, and institutions that extend U.S. power and influence cooperatively across the Pacific and Atlantic; and by encouraging an innovative, expanding U.S. private sector that connects Americans and introduces our liberties to others around the world. In sum, we need to rediscover the lost American tradition of integrating economics and security in our foreign policy.

What better place to sound this call than in Philadelphia, where the Founding Fathers created America's first traditions.