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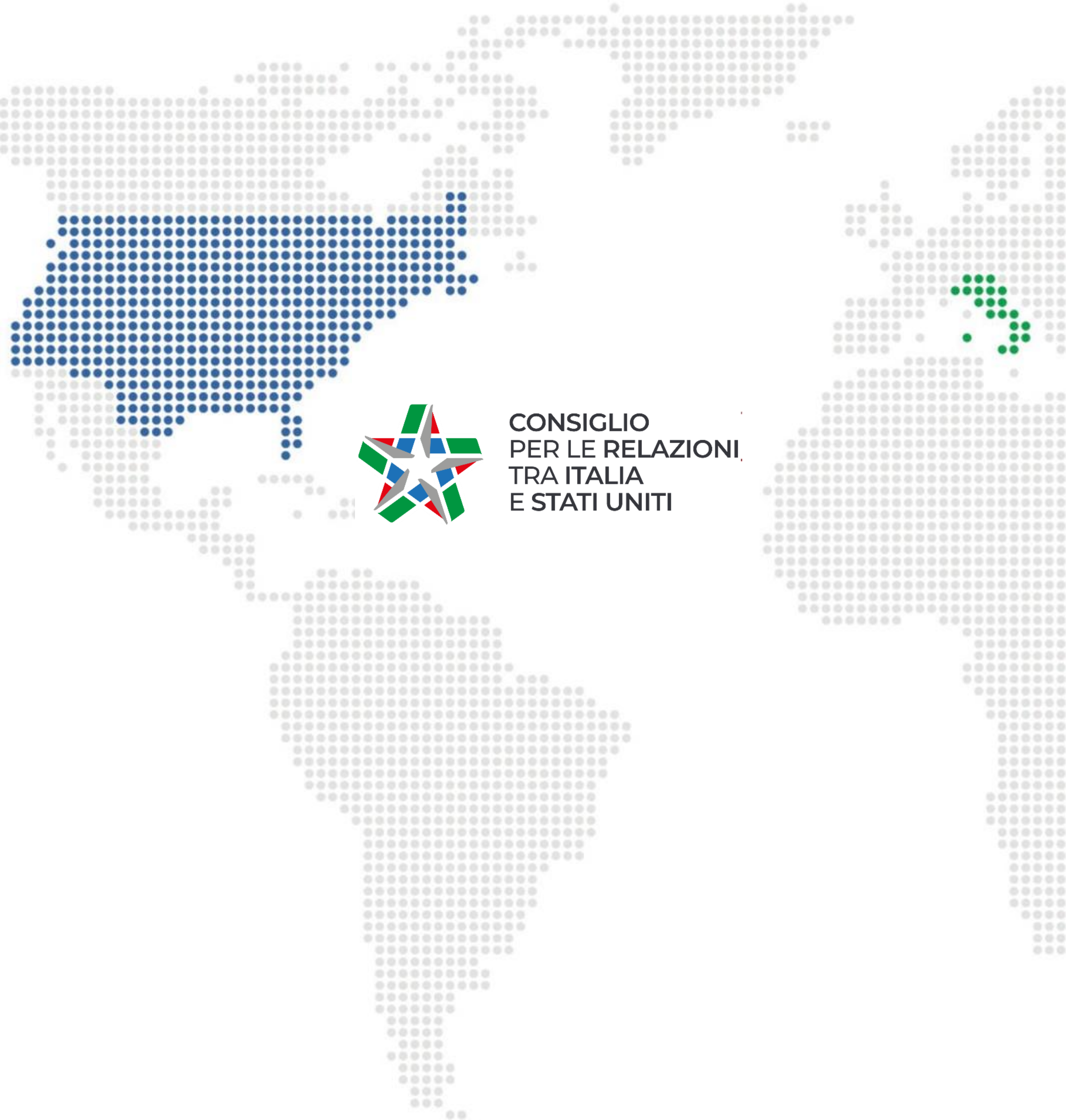

CONSIGLIO PER LE RELAZIONI TRA ITALIA E STATI UNITI

ABOUT THE COUNCIL FOR THE UNITED STATES AND ITALY

The Council for the United States and Italy is a private non-profit organization, founded in Venice in 1983 by Gianni Agnelli and David Rockefeller, who served as honorary presidents until 2003. Marco Tronchetti Provera followed them as Chairman, then Sergio Marchionne until 2018. Domenico Siniscalco is the current Chairman, Gianni Riotta Executive Vice Chairman. The Council for the United States and Italy promotes and creates economic relations between Italy and the United States, linking them to Europe, Asia and Africa through knowledge and free trade. Its members are leaders in the economy, industry, finance, technology, services, consulting, law, and culture - a team in which economic growth is viewed as promoting humanity and wealth as a cultural value to be shared.

This monthly newsletter is prepared jointly by the Council for the United States and Italy and The European House - Ambrosetti.

WEBINAR | From the Twin Towers to Kabul: searching for a new vision | 9th September

Mariangela Zappia *(Ambassador of Italy to the United States)*
Giampaolo Di Paola *(former Minister of Defense & former Military's Chief of Staff, Italy)*
Maurizio Molinari *(Editor-in-Chief, La Repubblica)*

From the Twin Towers to Kabul: it is important to maintain a forward-looking perspective, following the recent events in Afghanistan. Three challenges are ahead for Italy, the United States and NATO: What will happen to the role of the US in the world? What will happen to the system of alliances of a US-centric world? Will there be repercussions on China?

Ambassador Zappia remembers and commemorate the twenty years of NATO commitment in Afghanistan to preserve Western security and its principles. The notion of nation-building is strictly related to the fight of terrorism: you cannot achieve the latter without creating the conditions for stabilization in the country. The West could have done more, could have stayed longer despite the Doha Agreement. A limited military presence on the ground in Afghanistan could have determined a different attitude of Afghan security forces and especially of the Resistance to the Taliban. It could have guaranteed a framework for ensuring the activity of foreign diplomatic corps and NGOs. It could have backed the transition of Afghanistan, supporting the Afghan people. Over the last two decades, Italy has been at the forefront in Afghanistan with 50,000 deployed soldiers and providing an extraordinary contribution to the evacuation of Kabul.
At the same time, a positive change has been brought to Afghanistan in twenty years, planting a seed of freedom especially in the younger generation. Half of the Afghan population is less that twenty years old and they never lived under a Taliban regime. In 2018, youth literacy reached 65%, with enrolment reaching from 1 to 9 million and female enrolment increasing from 0 to 80%. Women became part of the working force and of the Parliament. These numbers confirm that the intervention in Afghanistan was not only military, but it included governance stabilization and human rights' promotion.
Reflecting on the role that we can play in the future, unity at the international level should be key in dealing with Afghanistan, as it proved successful with the evacuation operation. For the European Union, Afghanistan should represent a "wake-up call" with respect to the process towards a common security and a common shared foreign policy, and with respect to migration. The crisis in Afghanistan is generating a new migration crisis, affecting national socio-political balances in Europe. A stronger Europe in the defense domain would not imply a weaker NATO: rather, they can strengthen and benefit each other. Finally, unity in our values remains essential: the US is still the beacon of democracy, and Italy will continue to work together to continue the friendship and the partnership.

On the wake of 9/11 and the invasion of Afghanistan, **Admiral Di Paola** agrees that it was a right decision to take. However, few years later the orientation of the mission shifted towards nation-building, an extremely difficult task that requires enduring commitment in the government approach – this was not the case for NATO allies. Nation-building is not exporting democracy, rather creating the conditions for the people in the country to develop its own way of liberal values and freedom. In the case of Afghanistan, which is a historically divided country, the time required for nation-building is longer than two decades. Furthermore, the time-constrained approach of the Kabul evacuation was a help for the Taliban: even though it was operationally efficient, it was a bad political move.
At the end of the NATO mission, we can identify winners and losers: losers are certainly the Afghan population, especially women. A second loser in the short term is the West, NATO and the US: we were not able to withstand the universal values

of liberal freedom.
In order to strengthen NATO, it is important to rebalance the political power within the Council, thus rebalance the operational tool available, calling the European Union to do more. However, the creation of a Rapid Reaction Force of the EU requires economic and political commitment, which is unfeasible a common foreign policy. Any European force would need to be connected with the US with a strong transatlantic bond.
The winners are the Taliban in the short term, with the recently appointed government having terrorists in its cabinet. Also Iran, Pakistan and Qatar, Russia, China and Turkey are winners in their own way. For the time being, Kabul is in the hands of the Taliban, but windows are still open for Afghanistan. Certainly, the long-run competition between the US and China is still open, with the European Union still in search for its soul and defining the type of geopolitical entity it wants to become.

Finally, **Maurizio Molinari** confirms that the Taliban are the winners after twenty years of war, even if Al-Qaeda and Osama Bin Laden are defeated. The victory is especially important for the Taliban to prove that no matter how powerful the enemy is, God is on their side, and they will ultimately prevail. However, within the Jihadi group there might be internal tensions to determine the prevailing group.
As Ambassador Zappia recommended, the West needs more unity in this dramatic situation: unity might start from thinking about a larger strategy to deal with the global Jihad fight. The key behind the Taliban victory was that the Afghani population, who has been free for twenty years, was not ready to fight. A lesson learned from the recent events is that the only solution that could bring the defeat of the Jihadi group is finding enough will towards modernization and human rights within Muslim countries. A new strategy of the West should include the vision of finding within Muslim societies people that are ready to stand up and protect their rights. They will be the ones suffering the most from the current crisis and from future ones.

WEBINAR | The world economy: challenges and prospects | 29th September

Raghuram G. Rajan *(Professor of Finance at the University of Chicago Booth School of Business)*

With a first-class career both in academia and in civil service, Professor Rajan analyses the global economic outlook.
Industrial countries are experiencing three forces over the last months:

1- The Covid-19 pandemic and the more contagious Delta variant are affecting the pace of the economic rebound, with supply bottlenecks in the manufacturing sector. Mobility is holding up thanks to lower hospitalization rates in vaccinated areas. Countries that were successful during the 1st wave through quarantines and contact tracing have not been as forthcoming on vaccinations e.g., China. As a consequence, lockdowns are being implemented in countries that did not have particular difficulties in the 1st wave e.g., China and Vietnam. This situation affects supply chain across the world, with significant bottlenecks and transportation problems as it happened recently in the UK.
2- The extent of Covid-19 vaccination was particularly efficient in developed countries. Instead, in emerging markets vaccination rollouts are still low, with fear of virus breakouts.
3- The extraordinary fiscal stimulus put in place by central banks in developed world to maintain an accommodating environment.

There is some uncertainty on each of these factors, that play on each other: if a new virus breakout, the pace of vaccination will increase. Overall, growth is expected to be robust throughout the year: the 3rd quarter might be little weaker, with a stronger 4th quarter.
Another complex context is in China: it implemented fairly strong measures to sustain the economy. The government sees its dependence on foreign demand as being potentially problematic. If they aim to decrease foreign dependence together with infrastructure spending, they need to increase domestic consumption, by rising domestic wages and rates of returns of bank deposits. They need to move to high added-value sectors, as planned in the national strategic plan Made in China 2025. In addition, the financial sector would need to be more effective in allocating resources. This is one reason why China moved against the property market, to scale back its high property prices that might bring potential crises. As a result, several developers got into trouble, such as Evergrande.
In an environment aimed at stronger internal demand for common prosperity, the Chinese government aims at spreading economic wealth, by reducing monopoly powers and wealth concentration: it is epitomised by "housing is for living, not for speculation". As a result, the nature of the economy is changing and, in the process, they moved against fintech, food delivery, videogames – anything that seems contrary to a sense of economic prosperity and seems frivolous.

The problem is that China is doing all this at the same time, creating anxiety amongst the private sector and amongst households. So far, the crisis might not spread to the rest of the world through the financial sector, and it might remain contained.
In developing countries, the outlook is even more uncertain also because of the large amount of monetary and fiscal support they received. Most regions will reach their pre-pandemic level this year. However, much more damage has been done considering that fewer people able to work from home and there is less room for economic manoeuvring. In these areas, the malaise might continue with large firms performing well while small firms are in trouble.
Finally, industrial countries have built up substantial debt: countries usually repay their debt through fast growth, austerity, default, or inflation. As of now, we seem to be converging towards inflation for debt management: however, to inflate debt, they need to have long maturity such that the inflation rate is not priced in.
In the US, inflation is at its highest of the last twenty years: because of supply chain shortages, rebounds in service sector (travel and accommodation) and rental housing demand, inflation might remain high for long time.
The key to inflation is the labour market: currently, it is very tight with over 10 million job openings, with a rigid equilibrium that might increase wages. As a result, firms will increase prices to consumers.
With respect to policy attitude, fiscal conservatism is not in place anymore, in the US as well as in Europe: debt constraints are not as rigor thanks to modern monetary theory. Accommodating monetary and fiscal policies brings risks of overheating. In addition, there is a broader support for labour and wages negotiations. Globalization will put less constraint on costs both on corporate and on government side. Finally, central banks have also changed their policy frameworks through for example the average inflation targeting. Overall, we are in a more inflation-friendly environment, but the fiscal environment and the financial market are not ready yet.

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China's Risky Business Crackdown

Raghuram G. Rajan *(Professor of Finance at the University of Chicago Booth School of Business)*

Like the earlier campaign against corruption, Chinese President Xi Jinping's effort to control China's private sector is agreeable in its stated intentions, but questionable in its implementation. Quite possibly, the campaign for "common prosperity" will undermine the economic sectors that China needs to reorient its growth model.

CHICAGO – Is there a larger purpose to the Chinese government’s recent actions against the country’s largest corporations, and does its cleanup of the financial sector fit into its economic strategy?
China has sought for at least 15 years to rebalance its growth from exports and fixed-asset investment to greater domestic consumption – efforts that have assumed a new urgency, owing to conflicts with the United States and other countries. As long as its domestic market expands, China will be able to reduce the strategic vulnerabilities its dependence on exports implies, and foreign firms will become more dependent on the Chinese market, giving China new sources of strategic leverage. But there are serious impediments to this strategy.
For Chinese domestic consumption to increase, both wages and household incomes from invested savings must grow. And for that to happen, China must depart from a growth model that has hitherto relied on significant repression to keep workers’ wages and returns paid to savers low. That means moving toward higher-skill industries that pay workers more, with investment intermediated by a sophisticated financial sector that can generate reasonable returns even without access to cheap capital.
This transition would be difficult under any circumstances, but it is especially challenging today, owing to China’s past actions. Having previously emphasized fixed-asset investment, China now must deal with a massive overhang of unserviceable borrowing by developers and quasi-government vehicles. When restructuring overleveraged entities, Chinese authorities typically force investors to bear the losses, allocating them as they think appropriate. But when there is fear of a generalized loss of confidence, especially among foreign investors, these entities have instead been bailed out. That is why all eyes are

now on the heavily indebted property developer Evergrande.

Similarly, because China's past cavalier treatment of intellectual property rights has made advanced economies increasingly wary of sharing research and know-how, China now must create more of its own IP. And while it has universities and sophisticated private corporations that can do this, the key question is whether these entities will have incentive to innovate freely despite the recent crackdown.

The answer remains unclear, because President Xi Jinping is committed to maintaining the position of the Communist Party of China (CPC) at the apex of Chinese society and business. After launching campaigns to crack down on corruption, he has since moved to bolster the role of state-owned enterprises, even though these tend to be the Chinese economy's least productive players. Despite the central government's favoring of SOEs, the private sector has grown substantially (typically with local government support), and wealthy entrepreneurs like Alibaba co-founder Jack Ma have captured the public's imagination, sometimes even daring to criticize state policy.

The authorities insist that the crackdown on magnates like Ma and their firms is being carried out in the interest of "common prosperity." It is billed as a move against extreme individual wealth (read: billionaires), corporate monopoly (Alibaba and Tencent have allegedly used their platform power to constrain user choice), and exploitation of workers by platforms that until recently boasted about their "996" culture (working from 9 a.m. to 9 p.m., six days per week). And it will strike a blow in favor of data privacy (affording individual data protection against corporations, though not the government), and against cross-border data flows and foreign influence, including foreign listings.

To be sure, as with the anti-corruption campaign, many elements of the new agenda seem attractive. Who could disagree with the slogan "Housing is for living, not for speculation"? The problem lies not with the stated objectives, but rather with the pursuit of them in a system lacking checks and balances.

While the authorities have been careful to emphasize that the campaign is focused on the richest and most prominent entrepreneurs, particularly those who do not seem to be contributing much social value, it is also open-ended enough to target just about anyone. By cracking down on the extremely rich, the government risks discouraging the merely rich from trying to create value.

And who decides what is socially valuable? Bureaucrats and party officials do. It is they who determined that video games and private tutoring are more dispensable than chip manufacturing. And there is little to no avenue for seeking redress if they become overzealous in carrying out what they think Xi wants.

While parallels to Mao's Cultural Revolution are probably overblown, fears that the new crackdown will prove counterproductive are not. Most likely, it will deter innovation and private-sector risk taking, while imposing excessively conservative party preferences on the activities that are being encouraged. Such outcomes are hardly in line with China's need to shift to high-skilled, high-value production.

Moreover, the actions being taken today cannot simply be reversed tomorrow. Once trust in markets or the government is lost, it is not easily restored. This is especially true of confidence in the financial sector, where millions of Chinese have their savings tied up in half-finished houses and in wealth-management products sold by weakly regulated investment firms. Though Chinese authorities have a record of allocating financial losses without precipitating panic, they should not assume that they can continue doing so.

The government's attempt to control the private sector will make it much harder for Chinese corporations to access international markets – an important factor in the country's growth. Consider the government's drive to control data, including requiring that it be stored within China. Chinese service firms like Ant and ByteDance may find it much harder to sell products around the world when potential customers (and their governments) fear that the CPC will have access to their personal data.

The government is also attempting to reduce foreign regulators' leverage by discouraging foreign listings. But the perception that Chinese firms are subject to Western standards of governance is what has allowed them to expand their access to risk capital. With capital currently plentiful and cheap in China, this may not matter much now; but conditions will change.

Although China's business crackdown is broadly consistent with the public mood around the world, it risks going too far, because there are so few checks on the CPC's power, and within the party on its leadership. The slow negotiation on spending bills in Washington, DC, may dismay many observers, but it also speaks to the virtues of the democratic process. Because no single view dominates, there is less chance of a mistaken approach snowballing out of control.