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PANEL 1: THE EUROZONE: FROM CRISIS TO CONSOLIDATION?:

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PANEL 3: THE ARAB SPRING IN TRANSATLANTIC PERSPECTIVE:

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P R O C E E D I N G S

MR. VAÏSSE: Why don't we start now? Hi, everybody. I'm Justin Vaïsse. I'm a senior fellow here at Brookings. It's my pleasure to open this 8th Annual Conference of the Center on the U.S. and Europe, which coincides this year with President Obama's trip to Europe. He's indeed in Deauville today at the G-8.

We will have three panels during the day to discuss the situation in Europe and also the situation of Europe in the world and also the transatlantic relationship in general. These three panels were prepared and designed in partnership with our friends at the Heinrich Böll Foundation and we are grateful to them for their help and support.

The first panel, as you know, will focus on the crisis of the euro, including its transatlantic dimension. The second panel will be a discussion between Daniel Cohn-Bendit, the well-known Franco-German politician from the Green Party and our colleague Bob Kagan. It will be about Europe's power in the world. And the third one will explore European reactions to the Arab Spring in the early afternoon, starting at 1:30, and what Europe and America have done and can do together to affect positively developments there.

So, let's start with this first panel and the state of the Eurozone. About exactly a year ago at the 7th CUSE Annual Conference, we had already held a panel on the state of the euro crisis which had begun, as you may remember, with the worsening of the situation -- of the debt situation in Greece in late 2009. The conference was held in very early June of last year just a few weeks after a large bailout package was put together for Greece by the EU and the IMF and rescue mechanism, the EFSF, was put in place to reassure the markets and prevent further contagion from Greece to other countries perceived as weak.

Well, it turns out that the markets were not reassured, not for some time.

As you know, Ireland, and more recently Portugal, have had to be rescued by the EFSF among others. The failure to avoid contagion should not, of course, hide the fact that Europeans in the meantime, in the past year, made considerable progress at reforming the governance of the Eurozone and basically moving towards a closer union.

In March, just three months ago, the so-called comprehensive solution, agreed upon by European governments, included a strengthening of the growth and stability pact, reinforced surveillance mechanisms, national budgets, and a more robust rescue mechanism starting in 2013 as well as a new round of stress tests for European banks. However, trust has not come back or not come back yet.

As you know, the Greek situation seems more intractable than ever and it seems that there's little chance that Athens could get back to the markets, even in a few years from now. European banks still don't inspire confidence. Public opinions are not happy about the measures that have been taken to rein in deficits and reduce debt; especially in Spain in the last few days and weeks, and more importantly we're still far away from getting the strong and resolute political leadership needed to reassure the markets.

So, where is this going exactly and will we have to hold a panel discussion at every CUSE annual conference for the next 5, 10 years?

To answer these questions we have really a first rate group of four distinguished panelists and I'll very briefly introduce them in the order in which I will ask them to do their introductory remarks.

First of all, it's my pleasure to introduce Beatrice Weder Di Mauro. Beatrice holds the chair of international microeconomics in the department of economics at Johannes-Gutenberg University of Mainz. She is one of the five wise men of the German Counsel of Economic Experts. She is actually not a man, and what's more, she's not even German, she's Swiss. However, she is wise, indeed. She's actually so

wise that the German government overlooked these two flaws and she was chosen as the first non-German and non-man for this position where she advises the German government on economic policy with her four colleagues. I should add that, of course, she will be speaking here in her personal capacity only.

I will then ask my neighbor Lucas Papademos to weigh in. Lucas is currently a visiting professor of public policy at the JFK School of Government at Harvard University and a professor of economics at the University of Athens. More importantly, Lucas was previously governor of the Bank of Greece from 1994 to 2002 and then vice president of the ECB, of the European Central Bank, from 2002 to 2010. While he's sometimes (inaudible) the Greek government, he will also speak strictly in his personal capacity here.

Then we have two American observers with us. The next speaker will be Don Kohn, my neighbor here. Don is a senior fellow here at Brookings at the economic studies program. As the former vice chairman of the Fed, Kohn is an expert on monetary policy, financial regulation, and macroeconomics. Prior to his current position, he advised the Chairman, Ben Bernanke, through the crisis in '08 and '09 and also served as a key advisor to the former Fed Chairman Alan Greenspan.

Finally, after the Fed, the Treasury, we will hear from Ted Truman. Ted is senior fellow at the Peterson Institute, just across the street here, where he has been working since 2001 after serving as assistant secretary of the Treasury for International Affairs from 1998 to 2001. Previously -- he's also Fed, actually, because he directed the Division of International Finance of the board of governors of the Federal Reserve System from 1977 to 1998.

So, these are the four panelists to which I will ask to enlighten us on the state of the euro and where this is headed, perhaps starting with you Beatrice and perhaps your general view of the situation and where this is headed.

MS. WEDER DI MAURO: Well, thank you very much, Justin. Thank you for having me here and, you know, related to your question of whether there are going to be panels about euro for the -- you know, for quite a number of years to come, I would think that this is going to be the case.

It is a situation which has not yet been resolved and it's going to be very interesting for a number of years, not only from the policy point of view, but also from the point of view of analyzing what can actually work and what can't work, and that was going to be my introduction because I just happened to teach these days -- actually, the first days of this week, of course, on optimal currency area theory. And for those of you that have been either on the teaching or on the receiving end of this type of theory, that's our workhorse model of what one should do, whether a country should or should not join a common currency area.

And if you look at things from that perspective, you will see very quickly that our -- economics tends to be very quick about, you know, what the benefits are of the common currency, something to do with transactions costs that are lower, and then we focus very much on the costs, about the question of the incidents of asymmetries, about adjustments that -- when isometric developments happen in different regions or countries, how they can be overcome. And, in fact, when you start looking at this you quickly get the impression that there shouldn't be any common currencies anywhere, you know. I mean, you start really wondering why there are rather large currency areas, such as the United States, the more you focus on these costs and the question then is, you know, why -- then you could very quickly conclude that the solution is also quite easy, you know. Countries that are under pressure, such as, for instance, Greece, they should just leave, you know, exit, and in fact there have been some people suggesting Greece should take a holiday from the common currency, depreciate strongly, and then get back in or not get back in. I mean, just stay as a floater.

The problem is that I think what we do miss in this type of quick analysis is the -- enough of a focus on what are actually the alternatives. What are the costs of not having a common currency? Can you do it on your own? What kind of -- let's imagine we could do the transition without any cost, which is not the case, but what are the alternatives? Can you actually be a successful floater? Can you have the type of successful currency crisis and then devaluation and regaining of competitiveness as England had after '92? Or is it -- are you more likely to be in a situation that most emerging markets have been after currency crises in which they have huge balance sheet problems and they do not get back onto private markets for quite a while and they do suffer a large decline in output? And I would suggest that this is more the emerging markets, the alternative is much more what we're talking about and this is why to conclude, very quickly, that exit, or, you know, dismantling a common currency or even -- and, you know, as you may know, there are some sympathies for this kind of solution in Germany saying, well, let's reduce the common currency and let's have just a Nordic and let's let the periphery do it on their own. That the cost of such alternatives are really not thought through enough and that they would be huge, both for the countries concerned, as well as for the ones that stay inside.

So, by -- you know, if I -- by stating this I would say let's exclude the solution that -- one should not opt for the solution of exit for any of the concerned countries and therefore we are left with the types of solutions that are inside.

So, what are those? What are the alternatives that are available right now? Well, one is to continue on the path that is the IMF, EU, and ECB program right now which, of course, is in the case of Greece not faltering, but it's the strategy in general to do what usually the IMF does is to provide some financing and a lot of adjustment.

The problem, I think, clearly the most pressing problem is Greece because their original program of a year ago is now in doubt, whether it's financed and

whether it's credible. And actually markets have concluded that it's not credible. They look at numbers such as 150 or 160 percent of GDP indebtedness, which it's going to be, as programmed at the peak and then starts to slowly move down, which also means that you have a primary surplus, have to have a primary surplus over so many years that you look at the situation and you wonder whether Greece is in any way -- whether one can actually ask from the country to be able to deliver those kinds of surpluses, primary surpluses over many, many years.

Again, I think markets have basically passed verdict on this and have said this is not credible and this is why we see these huge increases in spreads in the -- in whatever number you look at for Greece, be it the CDS or the 10-year bonds, et cetera.

What about governments in Europe? Well, in Germany there is a lot of sympathy for this argument, actually. There is sympathy for two reasons, one, because one actually does also look at the same numbers and says, well, this is something that is going to be in economic and political terms almost unbearable. There should be an alternative and the alternative would be restructuring. So, German, both economists, I mean also us at the Council, but also in governments there is sympathy for doing an earlier, rather than a later, restructuring. And why earlier rather than later restructuring of the debt? Well, in part because as long -- if you wait longer, the restructuring that may happen is going to be made in the official government -- with the official sector because right now, of course, the private sector is being repaid, all loans are being repaid at par. And if you look at the repayment schedule, you'll see that within a few years already the official sector is going to be the main creditor to Greece, and if this continues, then eventually it's going to be the only one.

So, a later restructuring rather than the earlier is automatically also a restructuring with the official sector of other European countries. I am assuming that the

IMF would not be part of the restructuring and, therefore, it actually then would -- if this happened, would express to verify all the fears that Germans tend to have because they have been saying, when the crisis started, well, it's us who is going to be paying for this eventually. It's of course, not true. It's not only Germany, it's all the creditors, but Germany has a third of the pie, and so this is why in government in Germany there is a lot of sympathy for going for a solution restructuring. However, this is not really a majority view within other governments of the euro area, and of course it's not at all the view, as you probably know, inside the ECB.

Why is the ECB so strongly against a restructuring? Well, there are different reasons; the main one certainly being that the question is whether you can control the effects of having a restructuring in one country on the other countries. That is a very, very good reason, which also means that you could not just, you know, restructuring on one end and without having a plan for everything else.

So, if we take this one as a given, we need a plan for everything, then the real comprehensive solution has to have backstops for other countries, it has to have also a plan for other countries which are already on the program possibly. You know, Ireland and Portugal, what do you do with Ireland and Portugal if you start restructuring Greece? How do you backstop if there is further contagion?

And so if we start to think about it in this way, it means that a big solution is quite a complicated thing to organize. You need a lot of coordination. You need to coordinate the IMF, the ECB, the EU, you need to coordinate basically all governments because there has to be a -- almost certainly there would have to be a unanimous vote on this, and you need to -- that's usually the problem you have. You need to coordinate the private sector.

But this coordination problem here is much, much bigger than the usual coordination problem you have when you're thinking about restructuring private debt.

And the problem right now in my view is that this coordination problem is not being solved. There was an attempt to have a secret meeting of finance ministers and it was blown, cover was blown, and so it was no longer secret. It actually resulted in a weekend of speculation that they were talking about the exit of Greece, which was not the case, but it was -- you know, it completely backfired.

There is right now no good mechanism for creating the coordination that would be necessary to coordinate on such a solution because too many things would have to be in place at the same time.

In my view what is needed right now would be one player that can take over this coordination. This could be the EFSF and the way it could be done is through a debt exchange between the private sector and the EFSF in the first place, and then a second step in renegotiating the program with Greece, I think that could be a feasible solution. The other thing is, you know, where is the IMF on this? Is the IMF -- the IMF, in many ways, is now a pivotal player because it depends on whether the program goes on, whether the next tranche is released or not. The IMF could also be this player that sort of forces the coordination, but the question is, can it do it right now and will it.

And finally there is the -- I'm done -- and finally there is the ECB. The ECB has to be part of any solution. It can't be done without the ECB because although the bonds that the ECB is right now holding in its balance sheet straight -- that it bought on the secondary market, that's not the main issue. The main issue is that the refinancing and the liquidity provision of Greece, but also of some other countries of the banks of these countries, is almost exclusively through the ECB. So, the ECB holds the card on whether the banking system is floating or is not, and if the ECB is not on board with a restructuring, it can't happen.

So, right now we are in a block situation. That would be my analysis. We need a pivotal player that can provide a solution. IMF could be one -- could have

been, maybe.

MS. VAÏSSE: Thanks, Beatrice. I was hoping you would cheer us up for the introduction and then we would face some skepticism from the American side, but I didn't get it. So, Lucas, I'll try with you.

MR. PAPADEMOS: I'm not sure I'm going to cheer you up but let me first say that I'm very happy to be here. Thanks for the invitation. I think the topic of this session is becoming increasingly topical, unfortunately for the wrong reason, but I would agree with both of you that some more conferences on this topic are likely to be held in the coming years. I would hope, however, that it's not going to be very long string of conferences.

In my opening remarks I would like to say a few things on three issues that also Justin touched in his introduction, first of all, the general issue, where do we stand with the euro crisis and how is it likely to evolve? Secondly, I would like to focus on the policy challenges that are being faced in Greece in its efforts to resolve the sovereign debt crisis, and whether, despite the worsening of conditions, there is light at the end of the tunnel or, as some people think, maybe there is a train coming in the opposite direction.

And third, if I have a little bit of time -- otherwise I will do it in the discussion -- to say a few words on how the crisis management arrangements under construction in the euro area can contribute to the resolution of the crisis.

Now, where do we stand with regard to the crisis? Definitely the crisis is not standing, it is evolving very rapidly. It is evolving in an environment, which is collateralized by two opposing, rather contradictory developments. On the one hand -- and I think this is important to emphasize -- appropriate and bold action has been taken in all countries under market pressure over the last year, and also at the European level in terms of creating a new policy framework, strengthening, as we say, the "E" in the

EMU, and also establishing crisis management arrangements. But at the same time there is increased uncertainty in the markets about the capacity and the willingness of countries to take the additional steps needed to reduce the fiscal imbalances and address the competitiveness problems.

And one issue that has been very extensively and intensively debated over the past few months and especially the last few weeks is exactly the issue of debt restructuring that, as I will try to say in a moment, has actually played a role in terms of intensifying the market tensions.

Now, over the past six months, as we know, the conditions have not improved, they have actually deteriorated in the markets as being judged both by the bond yield spreads and the CDS premium despite implementation and the continuous implementation, as I said earlier, of bold and important measures to reduce fiscal imbalances and improve the competitiveness of the economies. So, markets are not reassured, they have not been convinced that the debt dynamics will be sustainable in the long term, and also that the funding pressures will be addressed over the medium term.

Now, the key question in my mind is what policy actions, given these unfavorable developments, can be taken at the national level as well as the euro area level, in order to change the market sentiment? This is sometimes what has been called game changing actions, so as to enhance confidence in the markets, in the sustainability of public finances, and in the resolution of the crisis.

Now, let me make now a few remarks on the Greek case trying to address this question -- actually, two questions -- what are the factors that explain the deterioration of the market sentiment? And what can be done to address the situation? And then say a few words about actions that can be taken at the European level.

Now, it's almost exactly one year after the agreement of the financial

support to be provided to Greece and the adoption of an ambitious economic adjustment program, and one year later the Greek economy and Greek policymakers are facing, again, I would say, extraordinary policy challenges.

Now, market conditions, especially over the last two months, have really deteriorated, and it's interesting to know that this deterioration, while market sentiment has taken place against the background over other impressive, but it seems also forgotten, reduction in the budget deficit in 2010 by 5 percentage points of GDP, as well as the implementation of a number of important structural reforms, particularly reforms relating to the pension system and labor markets that should help improve the sustainability -- the fiscal sustainability in the longer term, and strengthen the competitiveness of the economy.

So, what factors account for the unfavorable developments? Now, of course markets, appropriately, are forward looking. So, they acknowledge the progress that has been made in the past, but they are also concerned on a number of things. First of all, they are concerned about implementation, slippages, and delays that have taken -- that have been observed over the past six months.

Second, they worry about the so-called adjustment fatigue, political uncertainty, and social tensions that may make it difficult to effectively reduce further the deficit and control the debt dynamics in the long run. And concerns have been expressed, in particular, that an efficient public administration and the lack of political consensus on the adjustment program will hinder the attainment of fiscal targets and the implementation of the reform agenda over the long term. The implementation of the reform agenda is particularly important in order to boost economic growth, which is an important condition that will affect the sustainability of debt dynamics.

So, as a result, I think these concerns have led some to suggest that a vicious circle between lower than expected growth, than expected in the adjustment

program, and higher than planned deficits is going to take hold and this will make the resolution of the crisis very difficult.

Now, I think some of these concerns are based on facts and they have to be addressed very carefully if further progress is going to be made and market tensions to ease, but I think also some of the concerns that have been expressed are based either on exaggerated assessment of the social and political -- the social situation in particular, or certain misperceptions of reality. But before coming to this point, let me say that over the past two months there have been two factors that have actually contributed to increase the market pressures. The first has been the debate on the desirability, necessity, or inevitability of restructuring and second, the speculation about what I would call the absurd and purely hypothetical scenario of Greece abandoning the euro area.

Let me make a few remarks about these issues. By the way, if you look very carefully at the evolution of bond yield spreads and CDS premium, you can see how particular events, debates, discussions, have played quite an important role, other things equal, understandably in enhancing uncertainty, fueling adverse expectations, and effecting market conditions.

Now, the option of Greece of exiting the euro area I think has already been dismissed as an absurdity by all responsible authorities, both in the European Union and in Greece. It is not legally feasible and I think it's self evident, and you said it yourself, that if one assesses very carefully the implications of this hypothetical scenario, you come to the conclusion that it would have serious adverse consequences, both for Greece as well as for the European Monetary Union.

It's therefore a non-option. Theoretical exercises and discussions that have taken place during the period of crisis merely contribute to increasing uncertainty and increasing public confusion, and I think this is not particularly helpful.

Now, the debate on debt restructuring has been extensive and intensive

over the past few weeks. Now, the proponents of debt restructuring advance arguments that seemingly can help -- the debt restructuring can seemingly help address the countries debt burden and facilitate the fiscal adjustment process. Some consider it as desirable and necessary and in order to relieve the country's debt burden and address the medium-term funding changes -- challenges. Others consider it as inevitable given the size of the public debt and the perceived uncertainty about the sustainability.

Now, what I believe is that these arguments fail to take into account -- and I think this may explain also the ECB position -- I'm expressing my view, but it's not very different -- that the participation of Greece or any country in the monetary union and in the case of Greece also the composition of its debt by holder, imply that debt restructuring which entails haircut losses for the investors, for the holders of government securities, will have very serious adverse effects, adverse consequences, for the Greek banking system and the Greek economy and should also be avoided for many other reasons. And an important reason is the systemic implications of such a restructuring that the consequences it will help for market conditions and debt dynamics for other countries under pressure.

So, overall, I think debt restructuring is undesirable both for Greece and for the euro area as it will entail real costs and potential risks that are far greater than any perceived financial benefits. Perhaps during the discussion I can elaborate a little bit more because you advanced a number of interesting arguments and one would like to discuss them more, but I wanted to take the opportunity to say a couple more things if I can.

MR. VAÏSSE: Just one minute.

MR. PAPADEMOS: Okay. Then on the Greek case. I will skip over why restructuring is a necessary although it is undesirable, and let me say first of all on the Greek case that I believe that if the adjustment program, including the implementation of

a new very ambitious privatization program that can help address directly the debt problem, if it's implemented fully, effectively, and consistently over time, and if also over the coming months there is a reduced uncertainty concerning the political support of this program over the long term, something which is quite difficult as recent events have shown, then this will play a very important roll in progressively improving market conditions because it will minimize -- it will actually reassure markets about the commitment and the capacity of the authorities and the Greek people to achieve the fiscal objectives and the structural reforms which are necessary to improve the country's competitiveness.

If you allow me 30 seconds just to mention the topic, and I'll come back to this later. Having said that, I think it has to be agreed -- we have to be realistic -- that it may not be possible that the improvement in the market conditions will be rapid enough in order to make feasible the funding of the borrowing requirements of the Greek state over the medium term, that is in 2012 and 2013, at a reasonable cost.

So, certain actions and arrangements could contribute toward facilitating this and what I have in mind, which I will elaborate later on, is two things, first that the scope of activities of the EFSF and the new to be established EFSM, can be expanded as to allow interventions in the secondary market in order to improve market functioning, not to have debt buy backs because these markets are illiquid and dysfunctional during a period of crisis and allowing this intervention can really facilitate both the adjustment process of the countries and also speed up the resolution of the crisis. And the other point has to do with the provision, which is at present incorporated in the framework of the EFSM, related to the private sector involvement in the case of potential insolvency. I believe that this provision is appropriate in principle, and it's an important way in order to minimize the moral hazard in the longer term, but we have to think very carefully how the introduction of this provision during the period of crisis and increased uncertainty,

whether it will have undesirable and unintended, I believe, consequences for market conditions and can hinder the resolution of the problem.

So, I'm not against having it, but we have to think how to have it in a way that minimizes unintended consequences in the short term. Thank you.

MR. VIASSE: Thanks, Lucas. Without further ado, I'll turn to my American colleagues and ask Don first for his view on the European situation.

MR. KOHN: Thank you, Justin, and thank you for the opportunity to participate in this panel. It's funny, the state of the Eurozone, I kind of -- there are different perspectives here. If I look from 30,000 feet -- if I can get away from the ash cloud anyhow and look from 30,000 feet, the Eurozone macro economy is not doing that badly, right? It's growing; it's expanding, pushed forward by the France and Germany, in particular. They have an inflation problem but it's not significantly different from a lot of other inflation problems being faced today, but of course when you look down -- when you drop below the ash cloud and look down closer, there are all these tensions that we've been talking about within the euro area, and if they're not resolved in a prompt and thorough way, they could undermine economic progress, not only in Europe, but here as well.

So, I think the U.S., we can't kid ourselves in the U.S. We have a very strong interest in how Europe resolves these issues. Our economies are tightly integrated. We saw over 2007 and '08 and '09 how closely integrated our financial markets are. We have banks operating both in the U.S. and in Europe, both U.S. banks and European banks. We saw the effects of the dollar shortage and demand for dollars in Europe on U.S. markets in the early part of the crisis. U.S. money market funds have lent a lot of money to European banks. Our economies and financial markets are very closely integrated and we have every interest in helping you guys work this problem out.

I think there are also lessons from Europe for the United States, lessons

in living beyond our means, both on a fiscal level -- certainly the U.S. has been doing that and is projected to continue to do that for some time -- and the lesson I think we can draw from Europe is that you can go for a long time without market discipline. And those markets can turn very, very quickly and you're forced into situations that force you to take actions that are not in your long-run best interests because they're forced by the markets. They happen very suddenly. They're very, very costly. But I think there's also lessons, not only on the fiscal side, but on the broader national side. The current account deficit that the U.S. ran for so long, there also market sentiment can turn. In order to borrow the money to run the current account deficit, you have to have the confidence of the markets and the other countries, and I think there's -- we need to pay careful attention to how we're emerging from the recession. We need to be much less dependent on foreign borrowing. We need to have a much smaller current account deficit.

Having said that, the U.S. has a substantial interest in what happens in Europe. I think we're limited in what we can do directly to help. The Federal Reserve has made swap agreements available to Europeans to help with dollar funding if that becomes a problem. Certainly, the U.S. has and should support sensible solutions that involve international organizations like the IMF so that the U.S. is contributing through its participation in international organizations, but there's, I think, not much else -- maybe Ted has some ideas -- of what we can do to help you guys through this crisis.

Looking at this from the U.S. perspective and having lived through the financial crisis over here, I think what's particularly striking -- and this has been emphasized by the previously two panelists -- are the political difficulties one sees in Europe greatly complicates the crisis management and longer-term reforms. In the U.S., crisis management was closely coordinated among the central bank and the Treasury. There was broad agreement on the diagnosis, the approach, and the forcefulness of that approach, the need to come in with a lot of support and action to stabilize the situation.

There was also broad diagnosis on what needed to be done to reform the situation in the banking -- U.S. banking and financial markets to create a more stable environment going forward. It wasn't always easy to sell this to the public. It took, I think, joint visits by both Paulson and Bernanke and Geithner and Bernanke, to do this, but it's striking that it was this coordinated action by the fiscal and the monetary authorities that stabilized the situation and that's obviously missing in Europe today, the lack of a large fiscal authority in the Eurozone is hurting both crisis management and the approach to longer-term corrections.

I think in this environment the ECB strikes me as probably the only institution that can take a kind of a zone wide perspective and then act forcefully -- has the tools to act forcefully on that perspective, and they've done that. There's a lot to applaud in what the ECB has done, but they are naturally reluctant, and I'm completely sympathetic with this, to be a sort of a stealth fiscal redistribution system by taking losses on what they have in their portfolio. And they are very, very conscious, as Lucas emphasized, of the contagion risk of having problems in one area spill over to the other areas. Once you start knocking over those dominos it's very hard to know where they're going to hold.

In this kind of environment we've had very strong liquidity support and not very strong sovereignty capital support for solving the problems and the tension between sovereignty and the individual countries, and the need for forceful coordinated actions with a fiscal character is evident, the sort of coordinated approach that Beatrice was talking about. And they've been trying to get by, by just doing enough and that obviously has reached its limits. It's not happening. They need a much more forceful approach.

I never liked that bicycle analogy that people use for the European Union, you have to keep riding forward or the thing falls over. But I think we're kind of

there now, actually, that monetary union, euro area is at a very critical point in its history and there needs to be much more the sort of coordinated actions that Beatrice and Lucas were talking about in the euro area, not only from the ECB, but from fiscal authorities.

And I would say that thinking by analogy to how we handled the banking crisis, more forceful kinds of things than are currently, at least, publicly in train.

In the banking crisis we had to stabilize the system by providing liquidity and providing capital while making the intermediate -- the medium- and longer-term reforms to stabilize the system over the longer run. To me, this implies that we need -- Europe needs the continued liquidity support, they need to stabilize the situation through liquidity support. The ECB has got to be part of this thing as well as EFSM. The contagion, one important channel for contagion, is the banking system in Europe, so I think, very critical to strengthen the banking system, to force those banks to raise capital, either from the governments, or better, from the markets. So, I think a substantial strengthening of the banking -- the outcome of the stress test that we'll get later in June is a very critical point here.

Concerns about the banking system are constraining the authorities as they look at what to do about sovereign debt, and a very high priority should be to strengthen the banking system to raise capital in that banking system much more than it is now.

And I think the other point is there's a lot of emphasis on what the Greece and the other weaker countries need to do but also a lot of concern about the political will and the patience of the people of these countries to take the needed reforms. And those reforms certainly are needed, both in the fiscal area and on the competitiveness side as well. Even if the government wasn't borrowing, countries with current account deficits, the private sector, would need to be borrowing. They need to become more competitive. In an environment in which you don't and can't devalue your

currency relative to your major trading partners, this can be a very difficult internal process of discipline on wages and prices within the country. It could take a long time. To me this implies -- but it's absolutely necessary, but this implies not only all this emphasis on pain in the -- and reforms in the periphery countries, in the countries that are troubled, but it also implies that the other countries of Europe are going to have to step forward and support those countries as they undertake those reforms. Otherwise the reforms and the increase in competitiveness would be so difficult and so painful, it won't be carried out.

So, more emphasis, on my mind, on the coordinated approach Beatrice was taking, was talking about, will have to include help from the center, from the stronger countries as well as sacrifice by the others.

MR. VAÏSSE: Thanks very much, Don. Ted?

MR. TRUMAN: Well, it's a pleasure to be here. Yes, I worked at both the Federal Reserve and the Treasury and it used to be that I used to say it was easier to be -- respectable to be a former central banker, but it so happens that the balance has switched a little bit, Don, over the last two or three years. It's not quite as respectable to be a former central banker as a former Treasury official.

I was --

MR. KOHN: We'll talk about this later, Ted.

MR. TRUMAN: Well, okay. I was very glad that Don mentioned the lessons for the United States because I don't want my comments to say that we're perfect, by the way, here. I don't think there's any sense in that regard.

On the question -- issue of the years to come, I'm going to start out my remarks by saying I participated in a panel at the IMF in March of 1998 on the EMU and the International Monetary System, so we've been going for 14 years, and I noted that the EMU would create a stateless currency, which was pretty unique. Europe would be

living in a halfway house where economic decision-making would be done in an uncertain manner. And the effects of that decision-making would be important for the continued stability and prosperity of the global economy.

Certainly the single currency of the EU is a unique experience. One can say it's like the Gold Standard, but I think it actually is very much not like the Gold Standard.

And as far as the halfway house is concerned, my comments at the time in 1997 are relatively mild. You have these two strands, a debate, it seems to me. One was between the -- which was largely European -- between what I think has been called the economists school and the monetarists school. And the economist's school said, economic integration comes first and then you have central decision-making, and the monetarist school said, we build the Central Bank and everything falls back into place, and smooth integration follows from the institution building.

Then you have the second debate, which involved those who were worried about whether Europe was an optimum currency area. This was largely a U.S. debate, but as we just heard it still resonates in Europe, and worrying about so-called asymmetric shocks. Now, in the first strand, my view is that the politics of -- and I think this is broadly consistent with what we've heard -- the politics of European institution-building was ahead and now is behind the economics of convergence with unfortunate results. The establishment of the Eurozone with a single currency was not enough. It facilitated the emergence of intra-European, Eurozone imbalances, and policies and the political narrative have not kept up.

For example, in Germany, the advent of the euro was good for business, better than expected, as my colleagues across the street have written in the *Financial Times* this morning. This is a coincidence. Germany's real effective exchange rate is now 10 percent below where it was in December 1998. Between 2005 and 2010, its

current account surplus, scaled by GDP, was 6 percent of GDP, more than 60 percent, larger than the average between '85 and '90, before German unification when it was a big problem for the world economy, the German surplus.

However, the German political elite -- this is where the political narrative comes in -- failed to explain to the general public -- this is not just Germany, but I'm picking on Germany. I'm glad you're from Switzerland so I can pick on you -- Germany with some impunity -- failed to explain to the general public that these benefits might not be permanent and that they might involve a cost that might have to be paid later.

And on the optimum currency area and asymmetric shocks, what we have learned is the asymmetric shock, which economists actually had trouble generating examples of, turned out to be largely internal in nature. Europe participated in a global credit boom, it benefitted the exporters in Germany, the consumers increased, the homebuyers in Ireland and elsewhere, and the credit boom facilitated the build up imbalances that have now -- in the Eurozone itself, which is now bust.

So, the halfway house has not served the Eurozone well.

Now for the rest of the world, for the last 18 months, non Eurozone countries have been adversely affected by the European/Eurozone crisis. The euro has been weaker than otherwise. European growth, on average, has been slower, notwithstanding the fact that it's been better maybe than expected, slower. Financial volatility has been higher, and countries outside of Europe have shouldered some of the financial costs of dealing with the crisis.

I don't want to be misunderstood. The economic case for IMF and Federal Reserve -- I wrote this before maybe knowing that Don was there -- to assist Europe in general and the Eurozone in particular is very strong.

At the same time the -- and I would have to use this word -- smugness from the European economic policy elites blinded them to the emerging crisis and that

smugness has also exacerbated the normal political difficulties associated with selling such assistance to Europe to a skeptical public in the United States and their representatives in Congress. I think this applies to the rest of the world as well.

There are economic, financial and political limits to the amount and nature of outside support provided to Europe, notwithstanding what Don said. Taxpayers in Europe are skeptical about the wisdom of continuing on the current plan trajectory, but most European -- Eurozone politicians and policymakers appear to be determined to press ahead.

On the other hand, in the United States, Asia, Latin America, and Africa, taxpayers and their political representatives understandably are more skeptical because they are less likely to be directly affected by the fallout from a true Plan B, which would involve a significant write-down of sovereign debts of Greece and potentially of other countries if and when that becomes necessary.

Taxpayers and politicians outside of Europe are also likely to become increasingly less tolerant of the European halfway house. Either Europe should move forward towards greater economic and financial and political union, and as these recent moves, I think, as you said, Justin, are less than convincing and are still on paper, by the way, maybe why they're less convincing, they've been there before -- or Europe should move back towards a closer form of economic and financial confederation including the reintroduction of exchange rates ability.

Now, let me be clear. I worked with -- under Bob Triffin, right. I favor the first option. But those are the options.

More immediately, however, the leadership of the International Monetary Fund should not be held hostage to the parochial interests of Europe and the Eurozone. The next managing director of the Fund must represent the system as a whole. European argues that she or he should come from Europe because half of the IMF's

percent of the exposure is to Europe. Quite frankly, as many people have written, including myself, that argument does not pass the smell test.

The interests of the international monetary system require that decisions about the terms and scale of support for economic and financial programs in the crisis countries of the Eurozone not be made in Berlin, Brussels, Frankfurt, Helsinki, or Paris. In an open selection process for the new managing director, any candidate from Europe must receive the broad support of other members of the Fund. Those members must be convinced that the new leader of the IMF will analyze the pros and cons of moving to Plan B from the perspective of the system as a whole. Thank you.

MR. VAÏSSE: Thanks, Ted. You know, I'd like to get back to Beatrice and ask her about this halfway house. You know, a year ago, when we did this panel on the Eurozone crisis, people were, you know, already startled that Europe had been able to put that package together to rescue Greece, et cetera. And since then we had the comprehensive solution, and I won't repeat all the things -- I mean, many of the things are already in place, like the stress tests are going on right now and we'll have the results in a few weeks. The European parliament in a few weeks from now will approve the comprehensive solution, which is a leap forward in terms of integration and --

MR. TRUMAN: On paper.

MR. VAÏSSE: So, why on paper only?

MR. TRUMAN: We saw the stability growth pack, right, the first time it was confronted it was ducked, right, and weakened. So, there's no -- there is good reason for the markets to be distrustful of paper documents.

MR. VAÏSSE: Precisely. So, what's your reaction on this and how do you assess the comprehensive solution and the halfway house? Are we still at a halfway house in terms of currency zone or currency unit or have we moved forward, if perhaps insufficiently? And how do you see the next steps, towards more federalism or to use

that word, what are the necessary steps taken, and do you agree with Ted's position?

MS. WEDER DI MAURO: Sorry, no, I do not agree with Ted's position on most things, but on some I do.

I would say, yes, first on what I agree. We are not there yet, but I would not agree with basically just saying everything is just on paper.

The EFSF is not on paper. It's there. It is workable, it is functional, it is actually already lending to Portugal and Ireland. The ESM is decided. You know, its fine-tuning is still on the way but the ESM is going to be a European monetary fund and the Europeans have chosen to still have the International Monetary Fund in there, well, for several reasons. I don't think the main one is to have some co-financing. I think the main one is actually that the IMF can play a certain role of independent third party, which actually helps this coordination problem.

The Europeans have a lot of experience with this coordination problem, and in fact, you know, this has led to several solutions. I mean, many of the policies in Europe are already, to some extent, delegated to a European level. This is something that is just not in existence in any other place or any other area of the world, and nobody else has experience with this. This is why it's very hard to understand that European decision -- the European decision-making in general.

At the level of this new European monetary fund, for instance, what happens is governments set the rules for now having programs if it came again to be necessary, but they also at the same time said, okay, we want to have a very high level of control. So, in many of the stages you actually need unanimity. This of course leads automatically to a lot of bargaining and a lot of this common decision-making and need for discussions among governments.

This, in turn -- and that one I would agree with you that this leads to effect that in Europe we cannot expect in the short run the fiscal and the monetary

authority to act together in the same forceful way as we've observed in the U.S. In fact, right now, one could argue that they are almost playing a game of chicken because the monetary authority has said, you know, enough is enough. We are not going to go further with the fiscal -- quasi-fiscal roles we have taken on, and this is, again, different from the U.S. I mean, the Fed never said, you know, this is our line in the sand. The ECB has stated to draw clear lines in the sand and staking its credibility on that too. That's quite a strong move.

It has, for instance, said that if the fiscal authorities go ahead with insisting on restructuring we will not accept -- and rating authority agencies -- not authorities yet -- go ahead with their threats to then put these bonds into default, selective default statutes, then the ECB would no longer accept them for refinancing. That, of course, you know, is a very, very strong -- it's, you know, what somebody called kind of the nuclear type of threat.

So, right now we have -- we do not have the two authorities acting in concert, but -- and this is part of the problem for getting to a real comprehensive solution, that was my initial speech. But let's also realize where we were one year ago. There was nothing in place whatsoever. Everybody was -- you know, had to -- everything had to be built from -- really from scratch. And this concerns both the crisis management institutions as well as the long run institutions which are meant to stabilize the system in the future, and now there is in fact an important interaction between what you would want to have in the long run and what this may imply for the short run. This is when we get to the question of, you know, what is the role of bail in in the future? In my view, somebody mentioned it, market discipline always -- at the moment -- always comes too late and too much. Too much, too late, because it's not market discipline. The markets cannot function under the circumstances as we have worldwide. There is no type of insolvency law or institution or something that simulates the losses that would happen when a

country is actually insolvent. It's just not in existence. The SDRM was not accepted worldwide and Europe is actually trying to implement some type of SDRM for the long run. And that's right, that's a right solution because it is real reinforced market discipline in the long run.

But the question is, how this interacts with the short run, and that's where your concern was mainly that, you know, right now the countries that are in trouble now may actually have a problem if we are talking about bail in in the future, because then people will expect the bail in right now also.

So, I do agree with the fact that we are not there yet, but I completely disagree with the fact, you know, this is not going in the right direction overall. At the European level I really think the decisions that have been taken in only one year, the institutions that have been put in place in only one year, and they are not only in paper, I really want to address this, because it has required all this coordination and the coordination did work to put in place, for instance, an ESM. This is the way forward, it's not there yet, and why is Europe going to continuously keep building these institutions, because, you know, if you are serious, you can criticize. You can criticize a lot, but seriously, what is the alternative? You have to also think seriously about -- through the alternatives and come up with a better alternative. And I don't think just saying, you know, then you break up is an alternative. That's certainly not a good one.

MR. VAÏSSE: Lucas?

MR. PAPADEMOS: I want to comment on something concerning the future. I think the important steps that were taken at the European level over the past year do not only concern the establishment or relate to the establishment of the EFSF and the ESM, which are mechanisms for crisis management and crisis resolution. These are very important, of course, because this is the immediate objective, how to resolve the crisis, but I think what is very important for the future of the EMU are the decisions that

have been taken to reinforce the economic policy framework in the euro area, both by reinforcing, by strengthening the stability and growth pact and also by broadening the framework to have better economic surveillance that would also focus on competitiveness developments and balance of payments developments.

What I think is very important is to ensure that in the future crises like this one will not be repeated. And why does this crisis occur? I think first of all -- in two sentences, really, because countries made very big policy mistakes, they pressured some of them, very responsible fiscal policies or inappropriate labor market policies that were not compatible with the single monetary policy of the ECB, and at the same time, markets did not exert sufficient discipline in the new EMU framework.

Now, at the same time -- so, one important cause of the crisis, and perhaps the most important one, had a national origin, but at the same time, the stability and growth pact, and more generally, the economic policy framework that was aiming at aligning fiscal policies toward sustainability and coordinate them in the direction so as to make them compatible with a monetary union, that framework simply failed. It turned out to be both ineffective in preventing crisis, in correcting mistakes, and also it was incomplete in that it ignored in any systematic way the development of other macroeconomic imbalances, the losses in competitiveness, which are large and persistent, and the associated current account imbalances.

I think the new framework, and also in the light of the very painful experience over the last few years, is going to make a big difference in order to strengthen the functioning of the EMU, even if there is no considerable progress in the direction of a political unit and federals.

MR. VAÏSSE: I have a question for Don. You know, as (inaudible) sometimes points out, the U.S. fundamentals are worse than the EU if you take the two zones generally. Standard and Poor's recently downgraded the outlook for the U.S. You

could say that, yes, Europe as a monetary zone is a halfway house and political leadership is lacking, but here in the U.S. political leadership is also lacking as we've seen with the debates on the debt ceiling.

So, what exactly is the difference and why -- so, we were just talking of market discipline and the fact that basically lenders were lending to Greece up until December 2009 on par with Germany. So it's not market discipline. It was a blindness or just suddenly realized something, and now they seem to be treating the U.S. and Europe very differently. So, could you address the different -- Ted was saying earlier, you know, we're not perfect, et cetera. So, could you address the differences and point out why -- and then I'll ask the question to Ted, and then why is the U.S. treated differently than Europe.

MR. KOHN: So, I think, one difference is the components of overall relative total. So, I agree with you that the U.S. political system is not, so far, very good at coming to grips with our intermediate and longer-term problem. It might even not be very good with coming to grips with our immediate problems, the debt ceiling, in early August. We'll see. I think that will -- they'll work that out, but the tougher problems are the intermediate and long-term fiscal trajectory, which is not sustainable, very serious problem in the United States. And our political system has only actually begun the conversation about that late last year. It's encouraging the conversation has begun, it's -- the tone of the conversation, however, is not very encouraging, but at least they're talking about it.

So, I think -- I don't think people are making comparisons of U.S. and Europe and saying somehow the U.S. is better off, doing a better job than Europe in general. I think Europe has a different set of issues when the sovereign components are having problems. So, the U.S. debt is treated not any differently than German debt or French debt. It is treated differently than Greek debt and Portuguese debt and Irish debt,

just as U.S. debt is treated differently than California debt and New York debt and that sort of thing.

So, the U.S. has its components that are having issues and are suffering in credit markets as a consequence, just as Europe is. I don't think one is being treated significantly different from the other.

MR. VAISSE: So, Ted, is one of the reasons for the difference, the absence of a transfer union in Europe -- Don was mentioning different states and some of them are in a dire situation, indeed, but we know they won't fail or they won't fail for long or for real, whereas in Europe, some countries have had to be rescued, really, and we've seen in the past for some cities or some states -- New York City in the '70s, obviously -- situations like this. So, is that one of the critical points of difference?

MR. TRUMAN: Well, it's an interesting -- look, Don and I see Europe, understandably, through U.S. eyes. In fact, I participated in an exercise run by the British about thinking about the European Monetary Union when they did their examination of joining and forced me to learn a lot more about U.S. monetary history than I knew before. I think the one advantage is we have one structure, so we actually have solved, as best you can, the coordination problem, and I think that's the point. We don't -- a simple example of that, we may have our political problems, but we've settled that actually you only need 60 percent of the Senate plus 50 percent of the House to get -- that's the vote, 60 percent of the Senate, 50 percent of the House, that is a small majority relative to -- well, it's a super majority, but small relative to European decision-making at this time, and that's a big advantage, right, that we have.

So, we have -- even though it's clumsy, right, it is well trod -- the paths are well trod, when we know how we go about doing these things, and it will be ugly, and we will get there. The issue of the states, I think, is more complicated, right? We don't actually have a -- we don't have a mechanism for bankruptcy in states. That's part of --

actually, we have rejected that in the U.S. system, and that's one of the reasons why maybe I'm skeptical about the CACs in the ESM because they're only discretionary. I think it'll never happen. So, it will be even just confusing, quite frankly, and I think the important issue -- one of the important differences and why I'm -- look, I'm in favor of moving forward and I understand you can't do a great leap forward even to the messiness of the United States -- I can put it that way -- is the politics. I think the decision-making in Europe, right, is way ahead of the domestic policy -- the politics, the people of Europe, right, whether it's in Greece or in Germany or in Finland or wherever, right, leaving aside the fact that you have this problem that you have 10 countries that are outside the Eurozone, which is a big problem too. So, Europe, what is Europe, right? Is it 17 or is it 10?

But the politics, it seems to me, and there is much less buy into the system and where the system is headed -- and of course I'm an economist so I can pontificate about politics but I don't know anything about it, but we're all economists, so we share that weakness -- but I think that's the real problem, right, that how the political narrative is being sold and is it bought. That's why I made my point about Germany. The German public doesn't believe that they're part of the problem in Greece, and they were.

MR. VAISEE: Precisely. One last question before we get to the room. To you, Lucas. Focusing more on public opinions, public opinions in the South, especially in Greece, will have to bear the brunt of the adjustment within Portugal, in Spain, right now, even though Spain has not had the major problems that Greece and Portugal have had. In Greece, obviously, and we've seen a demonstration, we've seen demonstrations in Spain, but also in Northern Europe where taxpayers are getting fed up with the impression that they are subsidizing southern countries. In Germany, this idea of transfer union, of having a sort of *Mezzogiorno* problem or sort of replicating the help that was given to East Germany after reunification, and doing it again but in a context which is

not national, but Europeans, and where they feel less solidarity or less natural empathy for people they perceive as having mismanaged their economy. So, how do you think -- how worried are you that southern public opinions on the one hand and -- just to sort of character -- Ireland is in the north, of course -- but southern public opinions and then northern public opinions will bear the -- will support the continued necessity for adjustment?

MR. PAPADEMOS: Well, let me respond, first of all, by focusing on the public opinion in the countries under market pressure, Greece and others as well. In Greece, in particular, I have been impressed by the fact that over one year, with a few exceptions, most of the time surveys indicate that a large majority of the public ranging between 60 percent, sometimes to 70 percent, are either supporting or at least accepting, the adjustment program as something which is necessary to address, first of all, the fiscal imbalances, that everybody understands now could not persist longer, but also address persistent and longstanding structural weaknesses in the economy.

Second point; and I think I have a feeling that in other countries, although I'm not as well informed about the outcomes of service, the general, let's say, sentiment of the public is not likely to be different. Second point -- I will make two positive points and one more cautious point -- is that public demonstrations, although they have received a lot of attention, both in the newspapers and on the TV, they've been relatively contained, I would say actually, very contained, both in terms of size and intensity, considering the magnitude of the adjustment. Many demonstrations, including some of the more intense ones the last few months, did not involve more than 10- to 30,000 people in a city of 4.5 million. Of course, I'm not underemphasizing the importance of 10- or 30,000 people, and one cannot exclude that in such demonstrations certain extreme events can take place that can destabilize the social environment. But I think one has to see this in a certain perspective, that is, during a period when over a 3-year period the

real GDP has contracted by 10 percent and the real disposable income of civil servants declined in 2010 by 20 percent. Twenty percent. I think this is something that is not, I think, understood. It's a fact. It's in all the reports that have been written. Within an environment involving such a huge adjustment, that the market reaction is like this, I think it's rather remarkable.

However, now, let me give a word of caution. The adjustment process is reaching a critical stage where the reductions in real incomes becomes more widespread from the public sector to the private sector. And what is critical for public opinion, as well as social cohesion, is whether they can see down the road the so-called light at the end of the tunnel, because it has always been argued that labor market practices, bad labor market -- inappropriate labor market practices, and irresponsible fiscal policies would have to be reversed, and this would be good, both for stability and for sustained growth.

Now, if the recovery does not come at the expected pace, then I think one can expect certain tensions. And in order, however, to address these tensions, I think it's especially important -- I wouldn't be -- the way, really, to address them in my view is to implement fully the program. Because part of the problems that are being encountered relate to the fact that certain aspects of the programs have not been fully implemented and these are the aspects that can help further support economic activity like the liberalization of markets, particularly the service sector, as well as the implementation of other reforms, which through increased competition and greater market adaptability, will help support growth.

Now, so, I'm on the whole, of course, cautious because the adjustment process, as I said, goes to a crucial phase, but on the whole I think we have to see that the public reaction has been -- I would say, encouraging, if I may use this word. Now, perhaps, Beatrice, you may say something about the public opinion in Germany and other --

MR. VAÏSSE: Is there going to be a rescue fatigue in Germany that you -- I mean, we saw populist movements in different places, Finland and elsewhere. In Germany, apart from the press, we've not seen a mass change in the political spectrum.

MS. WEDER DI MAURO: Well, you know, I think there is a latent potential in Germany for somebody to pick up this discourse and it has not happened. All the political parties so far have behaved very responsibly and nobody has gone for this populist course. But there are of course many people in Germany on the conservative side who think -- who basically go, oh, I told you so. We always knew it; one should never have done this, never with the -- there are so many prejudices about Greece, about -- I mean, Italy used to be actually the prime case where everybody -- even the textbooks I'm using, you know, they always have Germany and Italy as the two cases. They still do use Germany and Italy. I'm also Italian, by the way, so, you know, I can speak for Italy.

So, but Germany is learning very, very fast. It had to learn -- you have to imagine that nobody in the German parliament, in the German political system, not even the press, had or had any knowledge one year ago about what a stabilization program is. I mean, those were things that happened in emerging markets, not at home. Most of these people are not economists, they are lawyers, they are -- you know, they have liberal arts background. Now everybody is all of the sudden very much into macroeconomics. And actually last week it happened, you know, every evening when I got home I turned on the TV; there is a talk show about the euro every evening in Germany now. So lots of experts have actually emerged in a short time and you can imagine that these experts are, you know, a little bit all over the place.

So, the optimistic view is that this is a learning process. You know, in Latin America even the taxi drivers knew about hyperinflation at some stage because they've lived through it. So, this may be a learning process and in a way a fast track course in international macro that these people have to go through -- the peoples of

Europe have to go through, and understanding, actually, how these things work, but there is, of course, also a more pessimistic side which is that this is also the breeding grounds for populism. Again, so far it has not happened and I am quite optimistic for Germany that it will not happen. This is partly to do because this kind of populist approach is always also very much a nationalistic type -- it goes together, so these tend to be nationalist parties that go for this populism. And in Germany, for historical reasons, there is a very strong reluctance to be branded anything that has to do with nationalist.

So, it's not so much of a winning proposition for existing political party, but there is the possibility of something new emerging and the breeding ground is actually there. So, in that sense I do agree with what you said, Ted, about the political narrative. It's not only a political narrative; it's also the economic narrative. It's very hard -- you, as an economist, you go try and explain to people, even in the U.S., try and explain what is the benefit of having a dollar and not having several currencies. The economic narrative of the benefits of common currency and the research behind it, by the way, is -- it pales compared with the cost. I would guess about 5 percent of research is about benefits. And it's very hard also in Germany. You said, well, German is one of the winners. You know, even if you talk to German entrepreneurs who are exporting all over Europe and you tell them, well, you, of course, are one of the winners from the euro, then most of them will agree with you, but some will say, well, you know, we already did it before. We were already exporting, we were already successful before, and we're also exporting into countries that do not have the euro.

So, the whole narrative of the benefits is under developed.

MR. VAÏSSE: Thanks. Let's go to the room now. We have about 10 minutes and I suggest we take one round of three or four questions, so please identify yourself and make sure you ask a question. Thanks.

MR. RASHISH: Peter Rashish, U.S. Chamber of Commerce. To follow

up on that particular issue of the understanding of the German public on the issue, can we be optimistic that when the stress test results come, out which are likely to show that a number of German banks hold not only bonds from the peripheral countries, but also have a lot of loans in the private sector in those countries -- can we hope that then it will be seen, you know, to borrow Christine Lagarde's phrase, it takes two to tango? These German banks made these loans out of free will to these countries and because of the recycling of all the surpluses which were fueled by the benefits from being in the Eurozone. I mean, can we hope that that will lead to a more balanced view of the causes of the crisis and thus, I think, a more reluctant -- less of a risk that that populism arises and more willingness to be part of the solution in Germany?

MR. VAÏSSE: Interesting. No other question? Yeah, there's one here.

MS. FRANKS: Sarah Franks, and I'm an independent researcher with Absolute Strategy Research. I guess our question is kind of similar, to carry on with the idea about Germany. I guess I'm most curious about, how does the German -- has Germany been given the wrong cost of capital? How is that going to play out? You know, we talk about the imbalances and the risk to that, what's the endgame there? I mean, you know, it seems like we're entering a time where current account imbalances are beginning to reopen. So, I'm just wondering what you guys sort of foresee for that over the next few years.

MR. VAÏSSE: In the back of the room -- sir, here, then in the back.

MR. DURANI: Yes, this is (inaudible) Durani. I'm a retired urban planning professor. I have a question for Dr. Papademos.

The questions that I have requesting your comment on those, is that really based on the difficulty in translating the broad view policy at the higher level, and the narrow view of a household itself. So, taking the Greek situation from two viewpoints, I would like your comment first on the general public viewpoint, for example, at the level

of a small business in downtown Athens, and the unions, or in outlying villages or towns across the country, when the general population perception is that daily living has become very expensive because of the EU membership. And now they are being asked to bear even a greater burden of austerity.

The second question is, what is the government's response in convincing its own citizens that its policies will get them out of the hole that they dug themselves into? So, especially when tax evasion is so widespread among the Greek citizenship, that's what we hear.

On the lighter side, I want to ask Dr. Papademos that having intellectually wandered from physics to engineering -- electrical engineering -- and finally to the economics field, do you think that you are now firmly anchored into this economics field?

MR. VAÏSSE: Thanks for the question. Last two questions in the back.

MR. BACHMANN: Thanks. Thank you. Danny Bachmann, IHS Global Insight. If we went back to the 1980s, I have the feeling we could have had the same discussions substituting Latin America for Europe. If we were in the 1990s, the discussion would have sounded similar but we would have substituted Asia for Europe. So, does Europe have anything to learn from previous sovereign financial crises, and when do we stop having the same discussions?

MR. VAÏSSE: There was one last question here, Dieter, and then we'll stop and ask the panelists to pick up the questions they want.

MR. DETKA: Thank you very much. Dieter Detka, Georgetown University. I would like to come back to the issue of debt restructuring. I think that's key because nobody likes to talk about it and it's difficult to accept that, that this might be the issue. There are nicer words now being used, not default and not restructuring, but re-profiling as the newest concept. But isn't it true that if we continue to treat this crisis as a

liquidity issue, we somehow might end up in a Ponzi scheme of piling debt, new debt upon old debt, and the question is, of course, how long can this go? And then you might argue against populism and all of that, but it will come, it's unavoidable.

So, can you please take that issue up and maybe consider, you know, a little more seriously that the need for some sort of re-profiling -- I want to use the newest word here -- might be necessary in order to be convincing as an economic solution to Europe's crisis.

MR. VAISSE: Thanks, since our time is up, I suggest each panelist takes two minutes to pick the questions that either they have been asked or that they want to address.

Maybe we could start with you, Ted, and the reverse order.

MR. TRUMAN: Let me deal with the last two questions, since I have spent a lot of my career, for better, for worse, dealing with external financial crises, including Latin America and Asia.

The lessons, I think, are -- one lesson is -- which was actually echoed by Beatrice and Lucas -- is you have to move with force in terms of policy. When markets react, as (inaudible) said, policy has to overreact. And that lesson -- and the successful cases are ones where policy has gotten out in front and turned the markets around.

A second lesson is, if you're going to go the restructuring route, don't wait until you've no money left in the till. That includes no money left in the till for the international financial community to help the country who is going through the restructuring, so you don't want to drain -- absolutely drain public opinion -- I'm thinking about Argentina in 2001, a willingness to help the country meet the inevitable financing needs after you go through the restructuring.

But I don't think, at this point -- this should be clear -- that anything is inevitable. I think it's possible.

I will cite the example of Brazil in 2002. When the spreads on Brazil were at 24 percent, right, everybody insisted there would be a restructuring. By the way, the German government wanted a restructuring of Brazilian debt in 1998 too. Everybody thought there would be a restructuring of Brazilian debt, right, following the election of Lula. It didn't happen. So, the spreads on the market do not tell you that restructuring is inevitable.

Everybody writing papers, including across the street, my colleague Morris Goldstein, saying the debt dynamics does not add up. Right? It turned out because Brazil politically was able to put it together and increase the force of their economic policies that they were able to turn things around and it is now -- it may have its problems now, but it recently has been a pretty powerhouse, at least by Latin American standards.

MR. KOHN: I'll pick up that last point. I think not only is restructuring not inevitable, but before it happens, the contagion risks have to be much better contained than they are now. So, as I tried to stress in my opening remarks, I think the banks -- and this goes to the first question to some extent too -- the banks need -- the European banks need to be much stronger than they are. They need a lot more capital. They need to be forced to raise capital in the markets. In order to get it from the government with all the strings that come tied to that and not -- and to retain earnings, I think, increase in the capital banks will help tremendously to contain the potential contagion and would give the governments the option, perhaps, of re-profiling at some point. But right now I think it would be very dangerous.

The second point is the current account imbalances. I agree that if -- certainly if Greece and the other countries that are running deficits, or the United States, running current account deficits, are to run smaller current account deficits because they're more competitive in one way or another, then Germany will run a smaller current

account surplus. So the Germans are going to have to think about how to generate domestic demand and not have such export, dependent export led growth, and that's got to be part of the formulation. It's very difficult when you're also constricting fiscal policy at the same time.

So, it's challenging but necessary. You can't have Greece, Ireland, Portugal, constantly in restraint, constantly constraining their domestic demand without something happening in Germany. And the fatigue on the periphery is going to -- is already -- I mean, Lucas may be right that a majority of the Greek population supports what's going on, but we saw problems in Spain, Portugal, and Ireland on the political side. And I wonder whether what's happening in Greece isn't a little bit like what's happening in the U.S. where the population sees the problem fiscally but doesn't like any of the specific suggestions about how to fix it.

MR. VAÏSSE: Lucas?

MR. PAPADEMOS: Well, let me also say a few words, first of all, on restructuring and then try to respond to the specific questions.

Now, the argument against restructuring -- first of all, you said piling up the debts and where will this end. Well, of course the idea here, and this is part of the adjustment program, is that when significant primary deficits are being established, then the debt will continue to go up for a while, it will start to steadily go down. So, the baseline scenario associated with implementation, not only of the Greek, but also of the Irish and the Portuguese program, imply that sustainability has been attained provided the appropriate policies are being effectively implemented.

Now, the other arguments against restructuring, on one hand they're the systemic and I think these are very important. One thing to keep in mind is that if there is a restructuring of debt in one country, even if it does not lead to, let's say, expectation that this will follow in another country under market pressure, the implications on market

valuations, particularly if confidence is eroded, can be substantial, and the implications on bank balance sheets will be significant because the base is much bigger and is not limited only to their exposures to Greece, Ireland, or Portugal.

But let me add something more specific relating to the “potential benefits,” either for the country that may restructure its debt or for the creditors. And I think this very much relates, as I said very quickly during my remarks, on the composition of the debt by holder, and also very much related to the fact that the country is a member of the monetary union.

If we take the Greek example, just to give two numbers, one-third of the public debt is held by Greek financial institutions and Greek pension funds. Any restructuring entailing haircuts could not be absorbed by these institutions or the pension funds and would have to result into additional expenditure by the state in order to recapitalize them or support the pension funds. More than one-third of the debt is held by official holders, either the IMF or there are guarantees of the European governments or the ECB. Any restructuring that will imply any haircuts, will essentially entail a direct cost on governments and ultimately on taxpayers.

So, the cost will have to be directly absorbed by the taxpayers. And it seems to me this is both unacceptable in a monetary union of partners, that the actions of one will have implications for the taxpayers of the other, but also politically, if it happens, it's going to be problematic.

So, what is left is the remaining part where one could conceive of potential benefits, although I don't see how you can address only part of the debt in one way and not in the other, but if this happens, how will a country be able to access the markets again in a short period of time?

So, I'm just giving you a few arguments that it seems to me raise serious questions about the benefits of this exercise.

As far as the re-profiling, I would very much agree with what Don said, that under present conditions, the so-called concept of re-profiling, based on voluntary and market friendly arrangements is not a feasible one, and it's not fundamentally different from a restructuring. Now, under certain conditions it may be able to implement such an idea, but I think at present is also not feasible and desirable.

MR. VAÏSSE: Thanks. Beatrice? You have the last word.

MR. PAPADEMOS: I will have to answer more bilaterally the questions for the other gentleman.

MR. VAISEE: Thanks.

MS. WEDER DI MAURO: Yeah, let me also start out with the restructuring question. I'm more sympathetic to restructuring earlier than later solution, although I have clearly said that it's very hard to be done in the right way because it would have to be truly comprehensive and taken into account the systemic effects.

Re-profiling, as a substitute, I think is not going to do much. You know, it started with the fact that, as you said it's only going to be affecting a small part -- an increasingly smaller part of the Greek debt, which is actually held abroad by financial institutions. You know, when people say, oh, it's the German banks that hold all this, it's not true. It's increasingly less true because they have also -- you know, any private institution that has been observing this crisis as it unfolds, has of course had its strategies of coping with it. And, you know, some of them have sold the Greek debt at secondary market prices, some of them have bought at secondary market prices hoping to eventually maybe profit from the fact there is going to be no restructuring.

So, my expectation, on your question in terms of the stress test is, that we're going to see actually quite little of these bonds still being held in the balance sheet and where they are still being held it's mainly in the public sector banks. So, those losses -- potential losses -- belong to the public sector anyway or they have been, in the case of

the bad banks, previously private bank in Germany that was a very big one that was taken over by the public sector and they split off into a bad bank, that's where all these potentially toxic assets -- the old U.S. and other toxic assets and the new, possibly problematic ones, are being held.

So, the private sector, you know, immediate balance sheet impact, I think, is smaller than people think and it's becoming smaller all the time because more and more is being held by the public sector and it's being held by the ECB and, therefore, the problem becomes larger, which would be my argument as to why you have to do something earlier, rather than later, but other people will argue, well, that's why you can't do anything already now.

If you were to do something big, what could be a game changer? You said, Lucas, earlier that EFSF could be given an expanded role of the ESM in the future to also intervene in secondary markets. In my view, the lessons from Latin America is that it's not enough to lengthen maturities, to intervene in the markets, you do actually have to have some kind of debt exchange which involves really also a relief for the country in (inaudible) terms. And such a debt exchange could be organized to an ESM.

So in my view, that would be a game-changing solution, which could be implemented within the next year, and it would, of course, then also be -- at the same time have a solution for Greece and we also would have to say what you do with debt in Ireland and possibly in Portugal.

So, in terms of the stress tests, I really, again, as I already said so, the immediate direct impact of holdings of bonds in the peripheral countries, I don't think is the major issue and it's becoming smaller as we go along.

And finally the current account imbalance, I think here there is some misunderstanding. You know, people are talking about Germany two years ago. Last year the growth of Germany was mainly driven from the domestic economy and this year

it is all, according to our projection, is going to be 70 to 80 percent. This is no longer an economy that is growing mostly as an export-led economy. That's not -- it's just not right.

So, this rebalancing, the internal rebalance, and of course the countries that are having to adjust very strongly internally now, they are not running the kind of deficits they used to run, so the current account imbalances inside the euro area, those are already adjusting, so the narrative and the discussion about Germany seems to have been lagging behind the fact that this is already happening.

MR. VAISSE: Good news at last. Well, please, join me in thanking the four panelists for a great session and we'll reconvene at 11:00 with Daniel Cohn-Bendit and Bob Kagan. Thanks.

(Recess)

MS. HILL: Ladies and gentlemen, we're just getting ready here. I'm asking my fellow panelists to make sure that their Blackberries are switched off. For any of you who were at the first panel, our Greek colleague got a call immediately after he had spoken. Clearly there was a bit of concern in the Greek markets about his comments, and he had to dash off stage. So I'm wanting to ensure that we don't create any more political controversies across Europe. I think that's the last thing we need.

I'm Fiona Hill, the Director for the Center on the U.S. and Europe. I'm very delighted to see that so many people are here for our second panel of our day-long annual conference on issues related to Europe and the EU and the consequences to the United States. This panel is focusing on the issue of European power. And we have with us two speakers today who know a thing or two about this issue, and I'm sure that's why so many of you have turned out.

On my right we have probably the most famous representative of the European Green movement, Daniel Cohn-Bendit, who is here as a guest of the Heinrich Böll Foundation who are our partners in crime, so to speak, for this conference today. I

don't think for anybody who has been following European politics actually for several decades, although he looks as youthful as he did in those early days when he was Danny, and I used to be as a young person watching him on the barricades in so many different places. He looks pretty much the same as far as I can tell. He doesn't really need much introduction. And, of course, the German Greens have just had so much success recently in politics that whoever wrote off the Green movement early on in its incarnation is now I think having to turnaround and wonder whether the Greens are the next party of power in Europe. So there is the power dimension here.

And on my left or on your right from the audience -- we were joking about what's left and what's right these days in politics and Daniel said it dependent on where you're sitting and from whose perspective. So he's ironically on my right and on your left. We have here on my left and on your right, Bob Kagan, who doesn't also need much introduction for this audience but who is newly joined Brookings. After years we've stolen him away from Carnegie, but as everybody knows, Bob Kagan, just like Daniel Cohn-Bendit, is very much an institution in his own rights and one of our foremost commentators here in the United States on issues of U.S. foreign policy and the issues of power.

And we're having this panel against the background, of course, of President Obama's most recent trip to Europe. Today the conference of the G-8 in Deauville has just wrapped up and if the volcanic ash has continued to drift northwards and hasn't crept south, I believe the President is on his way to Poland. But then he could always take a train anywhere; it isn't too far away. But in any case, he's heading off to Poland which is soon going to be having the rotating presidency of the EU, having just finished at the G-8 conference and, of course, having had meetings in London and before that back to his ancestral home in Ireland.

So in the G-8, of course, the big four of the EU -- the U.K., France, Germany, and Italy -- were very represented and, of course, in declaring the fact that European countries are still big players in global affairs. But the question that we're here to address today is Europe, is the EU itself, particularly considered a power in its own right.

So I wanted an initial question to Daniel Cohn-Bendit about this issue of the EU. We just had the last panel on the crisis in the Eurozone, and with the Lisbon Treaty in place in the last year, there's so much expectation that the EU coming into its own rights as a major, unified, player and then the euro crisis hit. As we heard in the last panel, we may be talking about the crisis in the Eurozone for some time to come. And this has really cast into doubt in many courses the ability of the EU, if it doesn't have a strong fiscal underpinning, to be able to project itself as an effective unitary actor, especially as so much informed policy these days requires some kind of financial backing. And, of course, the big debate about now with the Middle East is will the EU be able to step up with a major assistance package.

I've just come back from a week in Turkey where I took part in a number of conferences where the EU project was pretty much flatly declared as finished. Now, obviously, this kind of plays into Turkish politics somewhat, but is it indeed finished as some of the naysayers would have us believe? Where is European integration going to go from here or is this just a difficult period?

MR. COHN-BENDIT: Well, it is a difficult period. This is true. I mean, the complicated thing in this debate is that we don't discuss in our mind historical project. We just say, oh, this year's bad so it's over. I mean, I always said, take the Europe of 50 years ago. And then you say what we have today is incredible, impossible. If 45 one would have said you will have this Europe in 50 years, nobody would say it would never get there. Then you add all the crises, the French refusing the United Army, et cetera, so

I think it's a normal crisis in building something anew. It's not the state, but it's something completely new. The European Union is something that didn't exist before nowhere. It's not the federal state. It's not the nation state. It's not putting state only together. So this has difficulties. And, of course, in crises like today with the euro, they suddenly have to defend? It's not a nation state, but they have to defend common money and it's complicated. Now they create new structure.

But look, you have a federal state in the United States, okay? Is the politics to defend the dollar much better in a federal state than the politics of the European Union defending the euro? I think it's a good argument to compare to see if it's true. I would say the euro is in difficulty because now, and you are right, everybody sees that you can't only make one country to the other; you need a real European budget. And this put the government in problems because do you continue with this budget which is part -- the national budget, give something to Europe, or you take all resources? You have completely new debate on own resource in Europe, own budget, so as a base of a possibility of politics to adjust now the different countries. And at the end, in economy and finance, this is a most difficult thing to bring together. You know, the German are not nationalists. The French are not nationalists. But the Germans want that all Europe thinks like the Germans. And the French want that all Europe think like the French. And in the economy, in finance, it's a problem because the cultures are different. And I think there we are. We are not at every country -- Germany is suddenly to think we have a responsibility if we like it or not for Greece or for Portugal. And the Greek and the Portuguese have a responsibility to say we are not acting alone. We are in a framework, so our way of doing things must completely change.

And to finish, we have also this big problem of wrong financial economic politics. Take Ireland; Ireland was really the example of the neoliberal, get low taxes for enterprise, and the world is beautiful. And it was beautiful. And suddenly you had a

crash and now Ireland is where Greece is. Completely different, but you see also there suddenly the Europeans have to think do we need a conversion of taxes for enterprise? Do we need -- suddenly a conversion of things is on the agenda, but this takes time. But I would say so we have difficulties. We have difficulties of economic financial culture to bring together, but all the people who say the euro has failed are wrong. In the United States the majority didn't believe in the euro. They didn't believe at the beginning that Europe could do it. Then they say well, they will do it, but it will fail. So every year they say, you see? It failed. I mean it's a thing that you can forget. The euro will continue. Based on this, there are difficulties and we can discuss the difficulties. But forget the idea that you will have a Franc or a D-Mark again. This is over.

MS. HILL: Well, that's very good to hear, although we will continue, of course, to keep debating this as we go on.

Bob, we've heard from Daniel that this really was an enormous historical project, and he's absolutely right. If we were all sitting here 50 years ago in the Brookings Institution, we would never have envisaged what we've seen today. And exactly this point, this is a new creation. It isn't a federal state, per se. It's certainly not a nation state by any stretch. And it's not an attempt really to become the United States in some kind of European form. But how should we look at Europe from the outside because in many respects the EU, the European Union, has been trying to exert itself as an independent power in the international context and has requested, of course, a representation for itself in key multilateral institutions. So how should we think about this issue of the EU as a power in the international context, and also how much does that really matter for the United States? Don Kohn on the last panel, for example, said we shouldn't be at all sanguine or take any joy in these crises in the Eurozone because they will have a big impact on American markets. And clearly the perceptions of EU power,

with Europe being the traditional longstanding ally, individual set of allies, will have a reflection on our own abilities to conduct foreign policy.

MR. KAGAN: Yes, well --

MS. HILL: I shouldn't have tried to answer the question --

MR. KAGAN: No, no, that's fine, it's great. I'll see if I can deal with the question and the answer. First of all, let me just say I agree with Daniel about the state of the euro and the Eurozone. I think it will ultimately come out of this crisis, and I don't see it -- I've not been one of those, by the way, who's been predicting the imminent demise. I've always said that what Europe has created was a kind of a miracle and something to be grateful for. And as Americans I think we should be grateful for the European Union.

I guess the question we're addressing, though, is what is Europe's power in the world? And I would have to say, unfortunately, the fact that you spent your time discussing whether the European Union will in fact hold together, I'm with you on that. But that's a long way from Europe will run the 21st century, which is what --

MR. COHN-BENDIT: I agree with you. I agree.

MR. KAGAN: And it's almost as if we in the United States said don't worry, the United States is going to hold together. So don't worry, we're not breaking up. That's not progress, especially not progress compared to what we were talking about maybe even 8 years ago about the European Union and its project and what would happen in terms of its influence in the world.

And I think there are two things that need to be said about the European Union because we tend to pull them together but they need to be viewed separately. The European Union is a project primarily about the past. It is primarily about preventing recurrence of the horrors of Europe in the 20th century. That is the motive force behind the creation of the European Union, and that is why in my view Europeans will not allow the European Union to fail. It is about -- the past is too horrible to return to. Everybody in

Europe understands that. And, therefore, Europe, despite all the obstacles and there are obstacles, will keep plodding if not forward, but certainly to hold onto what there is.

But there's a separate question, which sometimes people elide into that, which is will Europe be a great power on the international stage? The fact that Europe will succeed in preventing a return to its past does not necessarily mean it will take on this new function effectively. And I think that's what's in real doubt, and I've always thought it was in real doubt, that the European Union would come to stand in the international system -- well at one point I think people thought it would basically learn how to run the international system, but even at this point, standing along the other great powers in the international system as a great power of equal influence. I think that's, unfortunately, what's in doubt right now. Because setting aside the crisis, and even before the crisis, I think there were real doubts about whether Europe had the capacity to play a role as a great power in the international system as it's currently configured.

And the first problem in that regard is a theoretical one. The Europeans made a bet -- now again, they did this for historical reasons. But as they were looking forward in terms of power and influence in the world, they made a bet that the world had moved into the end-of-history phase, that it was all going to be about geo-economics and not geopolitics, that it was all going to be about soft power and not hard power. And in a world that is about soft power and not power, that's about geo-economics and globalization, not geopolitics and competition, Europe seemed to be poised to be the exemplar of success in that new international system. Unfortunately, insofar as that was a bet, it's proving to be the wrong bet. The truth is we are not at the end of history. The truth is that we have not replaced geopolitics with geo-economics. The truth is hard power still matters. The truth is we are back to global competition of a recognizable variety, constrained I would say only by nuclear weapons, not by any natural evolution of mankind, and I hope it's constrained by nuclear weapons. And in that environment

Europe is now not necessarily configured to act, and it's not configured in two ways: One, it's not configured as an institution capable of enough unitary action to compete with strong unitary actors in other states. It's why Russia is able to pick the Europeans apart on energy. It's why China is able to play one European off of another. It's why the United States was able to play Europeans off against one another during the Iraq crisis. I'm not saying it's a good thing. I'm saying it's a vulnerability that Europe has.

And the other is, again, the question of hard power, which I think, unfortunately, we have not moved into a new era. It's still important. And Europe's hard power capabilities, despite the very encouraging actions of France and Britain on the Libya episode, Europeans' hard power capabilities in relative terms are declining and declining and declining. And so whether Europe is going to be able to compete as a great power -- and I don't, by the way, suggest that that's all there is. Europe has a massive economy. It will wield influence. It wields a lot of moral influence, which I think is important. But I'm not sure it's going to be able to compete effectively in an unfortunately competitive great-power world as it's currently configured.

MR. COHN-BENDIT: Can I --

MS. HILL: Yes, please, and I was actually going to ask you, what about this moral level that Bob has mentioned? One thing just quickly to mention today -- I mean, most people may have read about this that we've finally, or the Serbians, have finally tracked down Mladic.

MR. COHN-BENDIT: Wonderful, and this was the pressure of Europe.

MS. HILL: And mentioned, and that's what I was going to ask you.

MR. COHN-BENDIT: Because this was the thing. You come in if you give us Mladic. So it's not only a moral, so it was also a real power to change a little bit. But I come back to this.

Now look, look, first we have to discuss what will be a power of tomorrow. And I agree with you, it's not only soft power. But you must agree with me that Europe can only be a power if it is both, if it is an economic power putting forward a new form of growth, putting forward ecological and social responsibility in the economy. This is one, a moral power where exactly the lesson of history is a lesson of human rights. Europe failed.

And then I come to the hard power. Europe failed at the beginning in Bosnia for the first time completely. It was because they were afraid of the real moral stand. They put moral stand aside, not to take the consequences of the moral stand. So there you are absolutely right. And there Europe started a lesson, or the European Union -- I always say the European Union, but Europe is bigger than the European Union -- that European foreign policy is not to add 26 now, 27, or 14 foreign policies, but is to find a common ground of European interests who is not the French interest, plus the English, plus the German. You saw it in Bosnia; it failed because the German went to the Croats. The English went to the Serbs. The French went to the Serbs and to Bosnia and neither or both and nobody knows whatever until -- this was the reality until it's true. A part of the European and the American is end of the game.

But there the lesson was on its way and then you have another behavior of Europe in either of some European countries. In Kosovo you must accept that this was a dramatic evolution. You have now -- I would say the problem of Europe now is, you're absolutely right, lesson of the past. But the lesson of the past is not what is now a European interpretation of behavior in now and the future of this. Not only getting together, not only making war between France and Germany. And there you see that the Europeans are not at the level of the treaties. In the treaties it's written, if you are in an international institution, U.N., the European countries that are in must coordinate their action before they act there. Did you see it in Libya in the Security Council? No. So the

European today and now we are in an historically interesting phase, namely that the nation state has to understand, start to understand, that to give civil liberty to Europe is to add internationally completely differently. And this is a contradiction, and now you took the example of Libya. The intent of Libya is interesting because it was a French and an English reaction. They didn't believe. They didn't want. Sarkozy didn't want because Sarkozy had to pay very hard his hard friendship with el-Qaddafi two years before. So it was in his own interest for the next election that Sarkozy could come out of this. But in there it was not European. The problem is, and if you take Libya and if you take Libya as an example, you'll see the French started with four planes. Wonderful. And it was important because it was a first stop in Benghazi. I don't want to play it down. But then you needed the American Tomahawks. And after a week when the Americans went back, they were needed for the second phase, also the American Tomahawks. So you had now the demonstration that the hard power of France, neither the hard power of Britain, was there. And now you have the interesting debate, and it's my position. If Europe wants to take responsibility, not as a power like the American power, not because they want to lead the world, but to play because they have to give answers of crises in the world, then the European countries much go and say we need a European army. We have more than two million European soldiers if you take the 27 together. To do what? For what? So we are now in a very interesting 20 years that the nation state will say our existence in the world is not through our capacity as French, English, Luxemburg, Andorra, I don't know what, but as a common existence. And there you will see that Europe can -- and this is the political fight -- can be in future of power, but it will be a different power with a different way of doing things than the American one.

MR. KAGAN: Look, I don't rule this out. I just think you've got to -- the track record is an unfortunate one because we've had this conversation as you said. We had this conversation at the end of the 1990s, 20 years ago. Was it 20 years ago? How

many years is that? In 1999 because of Kosovo, wasn't there the great Anglo-French meeting and coming together of Blair and Chirac? What was it? St. Merlot? And that was when they decided, you know this was not acceptable. We had this European conflict. We couldn't do anything until the Americans came. The Americans did everything, unacceptable. The Europeans need to have their own force, 1999. And I'm personally -- I, not a lot of people on my side of the argument, but I felt all through the next ten years, good, do it. I don't care whether you do it part of NATO. I don't care whether you call it a European army. I don't care what you call it. Just do it. Create the independent capacity. And what's happened since then? What's happened since then is you've now repeated every single one of the problems that everybody identified in 1999: The French and the Germans can't agree, the British are this, the Americans are doing everything, and here we are starting all over again.

MR. COHN-BENDIT: Bob, can I tell you something?

MR. KAGAN: It's okay.

MR. COHN-BENDIT: You're right, you're right, you're right, but now take back the debate in Europe of common money; 73 --

MR. KAGAN: Okay, wake us up when you figure this out because 50 years are going to go by --

MR. COHN-BENDIT: No, no, no -- the problem --

MR. KAGAN: 50 years will go by. I heard this, by the way, in 1999. They said wait 25 years. So I think 25 years is coming up. The world is not going to stand by while Europe gets it act together.

MR. COHN-BENDIT: But the world is not going to stand by with the wrong position of the United States who has everything, but now they see they can't do it.

MR. KAGAN: Which is why I want Europe to get its act together.

MR. COHN-BENDIT: I know you want Europe -- I just want --

MR. KAGAN: I'm begging Europe to pull itself together.

MR. COHN-BENDIT: But it's much easier to make it this year in a discussion of how to do it with the 27 European states where -- and this is the difficulty of Europe -- you are always arguing if there is a leading country in Europe who could push it, and this doesn't exist and it is against the European construction.

MR. KAGAN: Right.

MR. COHN-BENDIT: It's a construction, and it's why it will grow through crises. I'm optimistic knowing that in crises you make state forward, and I think this Libyan crisis puts Germany as a kindergarten. Yes, well, it was a reality. It was a childish foreign minister who plays now a very hard -- this in his party, but this was -- Germany decided no politics. And this was one of the problems that Europe had in this Libyan conflict. At the same time, you see the German -- and the Europeans need the Germans in the financial or economic crisis. So we are slowly building this common institution. Now I agree with you. The problem of the European army is one of the most difficult. Why? Because if you have this European army, it means it's a national sovereignty. It's completely been redefined by the Europeans. And this -- you need 500 years to create European sovereignty and now you come, Bob, and saw come on Danny, do it in ten years.

MR. KAGAN: No, I'm not.

MR. COHN-BENDIT: Be strong, be strong.

MS. HILL: Well, look, I'll be the barricade here. This is a really big debate about the formation of a European army. Of course, in Germany it's also a major debate about the feature of the German forces, the defense forces. And it's probably not something that we can resolve right now, but it's certainly a big issue that I think in moving forward is going to be on the table. And as both of you said, perhaps Libya is going to be the test case, but maybe not.

But there are some other examples of Europe exerting some kind of coercive power. And we just mentioned about Mladic, and you said yourself that this is the influence of the EU. Now, the Serbian President today said, no, no, it's only by chance that we managed to capture him today. But just a few days ago, Barroso, who was on a visit to the region, actually did read them the riot act about making progress on these issues. So clearly there was some coercive element in there that was the impetus.

We've also got another test with Belarus right now. There was a piece in the *New York Times* there today, another classic line from President Lukashenko talking about the fit of the political prisoners in Belarus and saying that he may probably now consider releasing them because he needs a \$3 billion at least bailout from the West because the anticipated Russian financial assistance is not coming through. Now this will be another test here. The EU, like the United States, has put sanctions on the Belarus leadership. We've possibly got them on a whole host of different players right now, also with Assad and the Syrians. I mean, how effective are these kinds of coercive instruments do you think in the European context? It is a different prospective than Serbia while there's the carrot at the end of that of EU membership. It doesn't seem to be likely of that for Belarus. But I mean, how much can the EU play with other forms of coercive power if a military is not on the table right now?

MR. COHN-BENDIT: Well, I think with Lukashenko you talked the problem. The problem -- he needs the real European power at the moment, the economic power, and he knows that there are limits. And this limits his dictatorship. I don't say it's not a detractor, but we have a tool, much more than we had in the '80s with Poland in a certain situation, a tool to limit if he uses it really strongly. Now this is a debate in the European institution, how strong do we want to be? But I think if we are strong, we can force Lukashenko to make a step backwards. I don't say you change because you can change only from the -- if the people restart the movement. But this is

the power and the partnership politics of Europe must be based on human rights and democratic arguments. And this is a lesson what we have with Libya because you take me -- Lukashenko I say the horrible thing is of Libya is not only the military. It is one. But all our refugee politics was based on an agreement with a dictator. We push you back all our refugees. You put them in a camp, whatever you do, we don't care. We don't look. So we get rid of this and we accept your dictatorship. This was the relation between European countries and the European Union with Libya. And you can make the same argument on Tunisia, the same argument on Mubarak. Now if we get the lesson of Lukashenko that Europeans' idea of a politics-based also of argument of human rights and democracy is the tool to try not to change the world, but to press the world or to press this region.

MS. HILL: Well, what about this issue, Bob? And this is something that you've spent a lot of time thinking about here, and obviously it's something that we have difficulty in the United States as well in being consistent with them. How much prospect do you really think that the EU has for realistically pushing forward on this kind of approach that Daniel is outlining?

MR. KAGAN: Well, I think it's possible, and I think people like Daniel and the European Parliament, which I hope gets stronger actually in terms of its influence because there's a lot of concern about human rights there, more than you find in most of the national governments. I think that is an evolution that Europe can take. This is what I meant by Europe being a moral force. I don't mean that lightly. Europe does stand in a way that nobody else does. The United States is its own peculiar self, but Europe is a whole group of countries founded around a common set of values and principles and that is potentially a great force. And so I'm even willing to say, you know, Europe, okay, it's not going to be a great military power, but it can do other things.

Now the problem is there were two ways that Europe can be influential, and we've now mentioned both of them. One is having a common human rights policy. Now I think it's easier in the case of Belarus than it is in the case of say China or Russia. And what we find, of course, is -- again, and I say this as an American who's critical of our own policies toward some of these countries, so this is not a relative discussion -- but look, it's obvious that Europeans have a differentiated policy and certain governments are perfectly delighted to take advantage of relationships to sell weapons, to do business. So you want to have a common human rights policy toward China except that you're constantly -- everybody is competing for the trade, competing against each other in fact. And so that's going to obviously be a problem in terms of that. Belarus may be slightly easier. Whether that can take place --

MR. COHN-BENDIT: Because it's smaller.

MR. KAGAN: It's smaller. It's not as big a deal. And I would say, look, the great test -- forget about China, China is a long ways away. The great test for Europe is Russia. Russia is becoming a more and more authoritarian dictatorship. Every single day there are elections. This year, which one could pretend might be taken seriously, Russia has signed up to the European agreements on what elections are. Will there be concerted European pressure on Russia to live up to its own stated commitments on democracy? That'll be a very interesting question. I'm skeptical because France can't wait to sell Mistral ships, and they don't want business getting away. So that's one test.

Now, that's one issue for Europe's moral. The other was the issue of European enlargement, which was what played in Serbia. And I remember Robert Cooper wrote, I don't know, maybe a decade ago, and I thought this might be true. That Europe may not have a traditional kind of foreign policy impact on the world as a great power operating, but it could through the process of enlargement play a very powerful role, especially since where Europe could conceivably enlarge, is one of the most

important strategic theaters in the world. If it's enlarging to the Ukraine, if it's enlarging to Turkey, et cetera, I thought fine. That's a role for Europe. That's an excellent role for Europe where they bring these countries into the liberal European order of peace and security and prosperity. The problem, of course, is that that has stopped.

MS. HILL: Right.

MR. KAGAN: Now you'll say -- I can hear you say it in a minute -- it's a temporary stop. In 10 years, et cetera --

MR. COHN-BENDIT: No, no, I don't --

MR. KAGAN: Look, the price paid -- and by the way, the United States is responsible partly for the direction that Turkey has gone in. Turkey is responsible for the direction that Turkey has gone in, but Europe plays a big part in the direction that Turkey has gone in by the way it treated Turkish accession. And if it comes to Ukraine, I mean, Europe has indigestion so Europe is no longer -- that's a great power that Europe has and Serbia may be the last place it's going to get played.

MS. HILL: And, Daniel, can you pick up on this issue of Turkey as well.

MR. COHN-BENDIT: Yes, yes.

MS. HILL: Of course, it's a critical issue inside of Germany.

MR. COHN-BENDIT: First we have to make one clear. Europe is not a political unity. You have within Europe different political forces. So, for instance, the force that I am in, we fight for now I don't know how many years, for Turkey, for the entrance of Turkey, in the European Union. You can say we lost politically. Sometime, you know, you're not the majority. And you're absolutely right, one of the reasons why Turkey has finished the European project. Erdogan has another project. One of the reasons of it is how Europe -- but massively Germany and France -- handled the Turkish question. And why? Because it was an ideological internal discussion. You couldn't discuss with the French government, take Sarkozy, take Metal, the strategic importance

of Turkey. I don't want to say they didn't understand; they didn't care. It was an internal politics and when migration or this type of thing is internal, you're out. You can see it here in the state.

So you're absolutely right that the force of attraction of Europe is the force of its prospective of joining the club, because joining the club is a better life. This is easy to say. Now I would say that this debate -- I have an idea how to reopen this debate and where then the national opinion will have a big, big problem to say no. And it's two minutes, but it's -- I think if you take the Middle East and if you take the debate and you see this incredible theater of the Congress with Netanyahu where it was the end of politics. He could have read the last part magazine in every two sentences. They will all get up and say yes, Chicago will win, yes, Chicago will win. Now it's Dallas, yes, it's Dallas. So this was a political level of what happened, but you have behind to say if Europe and if the states, Europe, U.N., wants to have an influence in the Middle East, you have to propose something. You can't only say -- you can't say to the Palestinians forget the return of the refugees. If you want an agreement, forget it. To Israeli, you want security? Forget it that it will be Israel. NATO, Russian, whatever, we put the soldiers there, but not Israeli soldiers in a Palestinian state. It seems obvious. So we have this proposition to say we can fix something, but what is the future of this region? And then I said to the Israelis, if you go to a really two-state solution, the prospective of Israel will be a member of NATO. Come on, stop -- this is a prospective to Palestinian state and Israeli state, say okay. You go to really two states, your prospective join the EU. We will change a lot of things. We have to change because it must be countries in Europe we have to change this phrase to make -- I don't know why -- but if you say in Europe today, we have the possibility to give to this region an incredible future by saying, if you go to the two states, the two states will have a prospective in the European Union. It will change the lives of your children for the next 50 years. This is a prospective, and you

think one German who would say no to this because of the responsibility of history? You see one Frenchman who would say no? We will do everything to do it possible if this is a possibility to make a strong peace. So I think there you have the example that Europe has an incredible potential of conflict resolution that neither have for them for this because the attraction, what it means to join the club, is something still. Of course, you could tell me both would prefer to join the United States. Okay, I agree with this argument. It's too far. It's too far.

MR. KAGAN: Okay, if you do that, you're going to have 10 million Palestinians, right?

MR. COHN-BENDIT: Yes.

MR. KAGAN: Won't everybody claim -- I just want to make sure that you understand the minute you declare Palestine one of the European Union, you're going to have the entire --

MS. HILL: It also suggests that we'll have it to solve the problem of Turkey --

MR. KAGAN: Well, you skipped right over Turkey, which I think was a population issue, right?

MR. COHN-BENDIT: No, no. The problem of Turkey is now. We must understand that Erdogan now has another agenda. He has also -- we really defended Turkey's accession and also we say a modernization of this country. That's a social democrat with a nationalistic view, didn't dare to do. Now we are in a completely complicated situation because Erdogan suddenly had a great power agenda. And he sees his political agenda is to reunify the east Mediterranean. He sees this prospective to Syria, to this, and so the debate that we need for Turkey is also in the Turkish society. If you want, I write a paper -- I wrote a paper years ago. Turkey is in between in their -- and now the problem of Europe, and there is where you're right, is Europe must start also

to have a definition of their interest in the definition and Turkey is a good answer to the problem in energy, the error that we made with Poland. I mean, this was a -- we have a lot of things to resolve in Europe. If you imagine that the former German Chancellor is on the payroll, then you're right with your Russian argument. You're completely right. And that Europe has a difficulty to make a definition of economic relations with Russia, fair enough, and it will. And the political relations, and there I agree with you. I could tell you hundreds of stories why Europe is incapable, is fascinated, by the growth of China. And, of course, they say the dissident, the poor people, and it's horrible, but it's for Sunday morning when you go into church. But the real days all the week, you always forgot with this, so the human rights power of Europe is something that we put on the center of the debate, how we really use it or not.

MS. HILL: Well, one of the questions -- this addresses the institutional capacity here because we heard on the last panel, for example, Beatrice Weder Di Mauro was calling for the need for coordination among all of the various economic, fiscal, and financial institutions that Europe has created along with the larger international institutions. And this kind of gets down to the question of keeping these on the daily agenda, this struggle that Europe is currently having, of creating the institutions for a common foreign policy. Every day we read in the press about poor Catherine Ashton -- and I'm saying poor Catherine Ashton because every day she seems to be under fire from a different quarter -- and then occasionally she gets a little bit of praise. Where all of this institutional back-and-forth has been put on at least the head of one person, but we still have this problem of where Europe hasn't quite got its act together on which institution is going to take the lead on foreign policy. In Deauville Barroso was there while Catherine Ashton I think has rushed off to Serbia to take control of Mladic. So we have this problem here. Does this institutional crisis suggest the end for common foreign policy, Bob, or do you think that we can still get out of this?

MR. KAGAN: Well, I don't think the institutional issues are so critical because that's where I agree with Daniel. I mean, yeah, over time you can have a stronger and stronger institution. And look, let's face it, everybody in Europe would admit if they are -- off the record anyway -- that they deliberately picked two people to run this institution --

MR. COHN-BENDIT: Exactly, exactly, and we voted against. We voted against for both.

MR. KAGAN: -- That would not compete -- right. There were all kinds of dashing international figures that they could have put in, Joschka Fischer or anybody like that.

MR. COHN-BENDIT: Exactly, exactly, you are right.

MR. KAGAN: And the European leaders all said absolutely not, that's not what we want. So fine. I don't think that's the big question, but again, getting back to our earlier discussion, this isn't just a give us time and eventually question. There is also a theoretical question whether this can actually be done. And I would say right now, based on the track record, which is not so short anymore, the powers, the capitals do not want to give up power. And whether the day may come that they will want to, I don't dispute it. Anything can happen. The European Union's a miracle. That could be the second miracle. But right now, I would say --

MR. COHN-BENDIT: The third one.

MR. KAGAN: The third miracle.

MR. COHN-BENDIT: The euro is the second.

MR. KAGAN: The euro is the second, okay. So miracles come in threes presumably. But I would say that foreign policy is the last horizon for all the reasons you say because what does foreign policy mean? Ultimately, foreign policy means deploying

your citizens and potentially getting them killed. That's what foreign policy means, and that's --

MR. COHN-BENDIT: One part of.

MR. KAGAN: No, but I'm saying at the end of the day, that's why people don't give it up lightly. The United States wouldn't join the League of Nations because they didn't want any other country ever telling them where they had to send their troops ultimately. And there are other reasons, too, and I think that's a problem for Europe. And also then there are egos involved, right? So we understand that. But I don't see any progress in that direction, and so whether you can get there or not at some point I believe it.

And the other question -- let me just raise -- ask you about Germany. Sure you can say you have a crazy foreign minister, you have politics, et cetera, et cetera, but I think that the Germans have been pretty clear about how they view these kinds of issues. Yes, there was Kosovo, and Kosovo was this great moment when everybody thought okay, here's Germany coming back in to play this kind of global role. But I think that as a result of various things, including Iraq, including other things that have happened, I think Germans don't want to play that kind of role. And I mean, here was a situation where if you had said to me, you will have U.N. authorization, you will have EU authorization, and you will have NATO authorization, and the Germans will still refuse to play, I would have said that's impossible. I can't even imagine that.

MR. COHN-BENDIT: Arab League, add Arab League.

MR. KAGAN: And Arab League, most importantly, Arab League. So that I thought -- now to me that raises a real question as to where is Germany? Where does Germany want to go? Because you know as well as I do, there is no European foreign policy without Germany.

MR. COHN-BENDIT: I agree. First, this is a real battle. Now if you take the little history -- you're right if you see Germany and when westerners say abstention, I don't know if you really wanted to vote against, but it doesn't matter. It's the same abstention, you know. Then first one of the leaders of the Greens said I agree with him. Then you had a revolt in the Parliamentary group and in two hours they changed this and condemned and said you can't because of all -- you had the Arab League, you had the United Nations, and then to German look, it's not we, we are not there, you know. So this is the debate that started. It reminded me of '93 Kosovo. In '93 it was exactly the same situation we were at the beginning exactly the same few who said you can't continue like this. But what is now interesting is that for the next year when there will be the election, I think whoever will on foreign policy on this, learn the election now everybody's clear. We must go to a European position, and Germany will have learned the lesson. You can't continue to argue only with your own history because the result of this argument is Europe. So you find a solution. You find a solution to come out of the prison of your history. What I can't understand is it's a prison. And it's for this -- I'm optimistic that we can win the battle, but I'm not -- I agree with you that it's a very difficult thing.

Now on the institution, look at the finance crisis. You have more and more creation of European regulation to control the banks. It's the European going the European way. At the beginning all the countries said no, no, no. It's a nation. We do it nationwide. The Germans were the last to refuse a European -- now they make a stab at European control and coordination, I don't know, but you see that everybody is forced in this crisis to understand that to control the economic or the financial crisis, the nation control can't work.

So I'm not -- and you talk the debate now about the defense reform. Now the Germans will have 170,000 soldiers. They have a big massive financial problem. You can't -- if you say what we need for the world -- if you want -- and if you are

Defense Minister, you are obliged to see the world. And then you will see the only solution is to coordinate this in the European way, that we can take part of this, with others we take all. So I'm optimistic that the world, the reality of the world, forces also Europe to go a step forward. Now, I agree with you. My big problem is I'm not sure that the end of the tunnel will be in my lifetime. This is a little problem, you know? But I think they are all force, even -- and Germany is forced to understand that their foreign policy is not linked anymore to their history. It's impossible. You can't do a league like this. And it was really funny because you had this argument on Libya, and you had two big persons -- not big -- persons important or not an important person to argue for an intervention. The Germans argue we can't. Rommel came again. Now you have always the same history, Rommel, and then you have a very known Jewish pacifist -- no, no, no, he's not a pacifist -- in Israel -- who really didn't -- he say you can't let Benghazi take over by -- and it was me -- two Jews who said to the German now stop it with your Jewish reminders. We know, now look at the reality. And I think it's for -- so I think Germany slowly, too slow, but come out of this.

MR. KAGAN: It's not just Germany either. I mean, there really is --

MR. COHN-BENDIT: You asked me the question of Germany.

MR. KAGAN: No, no, I know, but I'm saying -- I just don't know and I don't want to, you know -- but I think -- I really do think all of Europe is living with its history. It's not just Germany. All of Europe is living with the history of the 20th century, and it may take a very long time. But, by the way, maybe --

MR. COHN-BENDIT: The states are. United States are.

MR. KAGAN: Maybe it's wonderful, maybe it's wonderful that -- well, the United States has a totally different lesson from World War II. That's the thing. This is what's different --

MR. COHN-BENDIT: Yes, that's what's different between their memories.

MR. KAGAN: This is what's different between us. You know, there's this great -- do you read the transatlantic survey that the GMF sponsors? *Transatlantic Trends*. My favorite question on that survey, which nobody pays any attention to except me -- it's my question. The question -- I didn't ask it, but I love it -- the question is would you agree with the following segment? Under certain circumstances, war is necessary to achieve justice. Would you agree with that statement? In the United States -- and this was from 2003 when the Iraq war had dipped a little bit -- but the consistent answer is 80 percent of Americans agree with that statement, 80 percent -- 50 percent agree with it strongly. In France 16 percent agree with that, 16 percent. Europe as a whole is roughly 25 percent, but only because the British are 61 percent. Continental Europe is roughly 20 percent, so it's like 23 percent. Americans, 80 percent. Europeans, 20 percent. And this isn't about do you want to bomb Iran? Do you want to bomb Korea? Do you want to bomb anybody? This is a philosophical question.

SPEAKER: And the Germans?

MR. KAGAN: The Germans are better than the French -- aren't better, excuse me -- the Germans have a higher number and I don't want to make any value judgments -- the Germans are higher than the French, interestingly, because the French pulled the trigger in Libya and Germans didn't.

MR. COHN-BENDIT: But when Sarkozy decide to go to Libya, 70 percent of the French say it's okay.

MR. KAGAN: Right, no, I know, right.

MR. COHN-BENDIT: So you have also to say this part of the story.

MR. KAGAN: I'm just saying there is something in Europe that is real, and it is -- in a way, it's a wonderful thing, okay? But it doesn't lend one to think that this

is a Europe bent ultimately on mixing hard power with soft power and becoming a great power in the international system. But let me tell you something. I so hope you're right, and I wish you luck in Germany. I don't even -- I'm not even being sarcastic. I really wish you luck because you're right, that's what Germany needs to escape. And if Germany escapes it, Europe will be healthy.

MS. HILL: Well, I would like in the next 25 minutes to put the audience in the hot seat as well here. We've already had a good bit of backwards and forwards, but I'm kind of getting a bit of neck strain here. It's a bit like being in the David Cameron and President Obama ping pong match that we saw and were trying to watch.

MR. COHN-BENDIT: And they didn't play a game.

MS. HILL: No, they didn't. Well, that's the special relationship. Another obsession that we've just gone through and thank God they've moved on to France and Poland now.

So while our two speakers are getting a water break here -- oh, and I'm getting one, too, thank you very much -- let's collect some questions and comments. We've already had a few from the audience, and let's get them provoked again. This gentleman here, and then --

MR. KAGAN: We don't require a lot of provoking.

MS. HILL: No, you don't, so --

SPEAKER: My question is basically to both of them, but mainly to Daniel. Unfortunately, you seem to continue to be a dreamer in spite of the 30 years or so, which is not necessarily a bad thing, but what you said about the possible idea of expanding Europe to Israel and Palestine when you know that Europe already was against even opening up to Mediterranean union. And Germany, in particular, was against it, strongly against it, even the idea of a Mediterranean union. And you know also in the past when Morocco claimed to be the closest to Europe, Morocco was shunned by

mostly all Europeans. So this is basically a project, a dreaming project, to open up Europe to other countries when, in fact, you know that the real European country, Turkey, is being rejected. The Mediterranean as a whole is being rejected. Just 20,000 Tunisians, immigrants to Europe, were rejected totally. A population of 500 million could not absorb 20,000 Tunisians. Europe is in a mess politically speaking.

MS. HILL: Okay, great question. Dieter Detka?

MR. DETKA: Thank you very much. Dieter Detka, Georgetown University. Well, first I'm glad that Daniel Cohn-Bendit defends Europe so much and remains optimistic, and I think that's great. But let's look a little bit at the reality. Europe has wonderful instruments. We have the southern neighborhood, the Mediterranean union, and we have the eastern partnership, and we mentioned Libya and we mentioned Lukashenko. And now, look at the reality and your hope and optimism I would like to share. I mean, this is not a question to provoke you in any way, but I would like to share it with you. You know, what doesn't exist on the national level first in terms of defense and capabilities, will never exist on the European level. So that's what we have to achieve. If you want to be effective in a case like Libya, you have to have capabilities. You have to build capabilities. And again, the problem is on the national level. And look at the German new defense plans, the reform plans.

MR. COHN-BENDIT: But it was a fake.

MR. DETKA: So here we go. So how do you bridge this? Europe takes on the eastern partnership and talks about human rights and democracy, and then comes Lukashenko and puts down everything that's decent and that looks like human rights. And what does Europe do? Nothing. Libya? Europe had a decision-making process on Libya. Germany pulled out of even the NATO commitment at that time. Europe, the European Council, got together and made a decision, we're going to deliver humanitarian assistance, and we will even protect it to some degree militarily. But look at the reality?

How does it look? It gives Qaddafi a free pass. There's nothing that would change and transform its own plans. The European neighborhood in the south, the Mediterranean union; there was a commitment and Germany, remember, was adamant in making this a European project. Sarkozy was trying to do this more as a southern European project. And then you have this enormous failure to act when the hour of acting comes. And there is nothing more important for the hour of Europe than to stand up for its own plans in the southern neighborhood and in the eastern partnership, and it's not there, and that's --

MS. HILL: Well, we're getting a lot of differences of unified Germans here on the hope that -- and Dieter will. We'll also have a panel after this on the neighborhood policy, so I hope you'll stay and be able to put some of the questions to some of the people who will be on that panel as well. Does anybody else want to pile on at this moment? We've had a number of -- yes, the lady here in the shirt. Thank you.

SPEAKER: This is addressed to Mr. Cohn-Bendit. If you comment, please, whether or not you think the U.S. is trapped in its Cold War history and discuss EU-Russian relations. I think we tend to demonize Putin more than he deserves, and I would like to have some of your feedback.

MS. HILL: Okay, right. We've covered a lot of territory here. Daniel, and then I will give Bob a chance to weigh in.

MR. COHN-BENDIT: Well, first I talked about Turkey in my -- I know that my proposition on the Middle East is unrealistic. I know this and you're right to say and I think the future of Morocco is in the union of the southern Mediterranean and not integration. I could give you a lot of argument. We had the argument on Turkey. Why Turkey is so important for Europe is because for the first 50 years we hold Turkey to say you have a perspective of Europe. It was the European Christian democrats who start with this. It was not the leftists, it was the Christians. The prospective is -- so to be clear

on this. And I think that in the time where the world are fighting terrorism, to show that fighting terrorism is not fighting Muslim, was an incredible, would have been incredible why Turkey became so important and then strategically important.

The difference was Israel and Palestine that emotionally nobody would argue against in Europe. This is because this is linked in a positive trap of history. You have negative trap and you have positive. And I can promise you, everybody will tell me it's not realistic, you can't do it, but emotionally it's very sympathetic. When you discuss Turkey, nobody said emotionally it's sympathetic. No, we don't want them and it's impossible and 18 million people and whatever you can have. So this is the difference. And, you know, dreamer, dreamer. Yes, if there would not have been dream -- it's an easy answer and I take it back again -- but without dreamer you would never have had a Europe because at the beginning it was an absolutely crazy dream.

So now all the argument now about capability. You know, when we had the financial crisis, nobody dared to think that the solution we came that the central bank will bail out, as a central bank, taking debt from the Greeks, from the -- impossible. Capability is forbidden. It's even forbidden, and they did it, they did it. They did it for millions, billions, billions. So Europe is building some capability. Now you're absolutely right on the military, but then continue your argument. You have this reform. I talked before, military reform of Germany. You have the problem of France. France is fighting now or discussing now a second atomic big navy, and they don't have the money. Nobody has the money. And, of course, now this debate on the real situation of the state, the money brings one of the solutions. I don't say it must be, it is mathematic, but one of the solutions is rethink all this defense. Look, I will tell you, 150,000, half 70,000, German soldiers. You don't need them. We need 350,000 European soldiers. If you have 350,000 -- how many you have? You have big specialists in America everywhere in the world. How many Americans you have?

MR. KAGAN: 1.2, thank you.

MR. COHN-BENDIT: 1.2.

MR. KAGAN: He's a better specialist than I am.

MR. COHN-BENDIT: 1.2, okay. I think because Europe will be a mixture of soft and hard power, you can go out with 400,000, okay, 400,000 modernized? Come on. If you have 400,000 modernized capabilities, you will be also in Georgetown very happy. Leave it there, but it's of course -- if the duty what you have to do in the world, if you reduce it always in this nature, it would mean -- can you imagine the necessity of the world of today only thought by California? No, if California has to put an army on, they would say which capability they can build. Nothing. They have no money. So, no, I mean -- I want to tell you this is a lesson of the times for the European. Now I don't think this will come. It must come. I think we have to defend this idea to fight for it, and then in 10 years I will come to Georgetown and you will tell me, Danny, half of this was you said is reality and the other half is not. Well, it's progress, you know?

MS. HILL: Bob, do you want to take on any of these issues? The lady also asked about Putin --

MR. COHN-BENDIT: Oh, yes, Putin.

MR. KAGAN: Well, she asked him. She knows what I think about Putin. I don't think she wants --

MR. COHN-BENDIT: Well, no, no. I mean, we don't demonize him. I think Putin is a terrible dictator. Now you can say which type of politics we do with a dictatorship like Russia. It's an open question, but come on. A man who is responsible for so much killing of journalists, of people and that, you can't say we demonized him. And all this politics was, you know, was an incredible massacre and provoked the most bloody Muslim revolt -- it was provoked by the Russians for years. And I don't want to talk with you about Khodorkovsky and the trial and what happened there. I mean, it is out

of the rule of law, out of the rule of law, and then I think -- and it's very dangerous that Russia today in a very intelligent way, said look, come on. We are a democracy. And one of the men who was most responsible for this is the former German Chancellor, saying that Putin is a perfect democrat. Of course, we can go along like this. Russia is a perfect democracy. I will tell you something. In this democracy, I don't want to live. I don't say that we have to make war to beat Russia. I don't say -- we have to describe the things like they are. And, of course, you can beat Putin. Is Putin worse than Yeltsin? Yeltsin was corrupt. Putin gave a nation sense to the Russians. Okay, but he's as corrupt, is as corrupt, and all the system is corrupt, so quite difficult.

MS. HILL: Bob, on some of the other issues that were raised, do you want to make any further comment or shall we --

MR. KAGAN: Look, I just think -- let me just say a time of economic crisis is not a time to make eternal judgments about what's possible and what's not possible. So this is the wrong time to be asking the Europeans, you know, unfortunately, now's the time to really beef up your military capacity because the problem is that the trend predates the crisis. And the general trend in European military capacity, not only in relative terms, but in absolute terms, has been downward. And there's a simple reason for it I think -- and this is the only thing I want to add, and I wanted to ask you about this so I don't want to get in the way of the audience. The average European citizen does not feel the need for a great military capacity. The average German does not feel threatened by anything that a military capacity can solve for them. They feel threatened by immigration. They feel threatened by forces of the economy. They do not feel threatened by an external threat. And I asked a very senior official, very senior official, when you go to the German people and say this is why we need a military, what do you say to them? And he actually didn't have an answer to that. And if they're saying -- but he said the one thing you can't say to them because the German people aren't ready to

listen to it yet is what you said, which is that we need a tool for international policy. We need to be able to deal with the human rights problem, a responsibility to protect. He says the German people don't want to hear that. Now I don't whether that's true and you're going to change it personally. But I think also not just in Germany, but looking around Europe, there isn't a driver for military capacity at the public level which -- let me just segue then into the second question -- what is the European public mood about Europe now? Because -- and I don't want to say that, again, we're in difficult economic times, but you do have the rise of nationalist parties in almost every single European country. I don't know whether Alapat is about to win or not --

MR. COHN-BENDIT: No, no, never.

MR. KAGAN: Never, okay, fine, good -- but you have --

MR. COHN-BENDIT: Like the Tea Party is never going to win in the United States? Come on.

MR. KAGAN: We'll have to talk about that in two years. Anyway, I just wonder whether the European public is going in the same direction on Europe as you're going on Europe.

MR. COHN-BENDIT: Look, you're right with the populous. You're right with the populous. You have the true Finn, the true German, the true French, the true -- but okay, it's 20 percent of the population that in a crisis -- and this was the error of all the Marxists that in the crisis the people go in the right direction. No, history shows us that the people go in the wrong direction in a crisis. So this is true. I think that where you're wrong is you can argue in Germany or in France which situation where you need military capability. And this has named Bosnia, Libya, and others you can argue there we need. And we can't say we shut our eyes and let the people rant and it doesn't matter. And there nobody in Germany will tell you that we cheat with you or that we don't need, we

need only police. Then they will start to cheat with you, but not because they want to say it's not necessary. They are afraid of the consequences. So this is the difference.

MR. KAGAN: Okay.

MS. HILL: We have a sir here in the audience with the blue tie. Sorry, sir, the gentleman behind you and then you. Yes, the one with the blue tie.

SPEAKER: I'm wondering what you think will be the willingness or lack of willingness on the part of NATO to play a role in future situations given what in Germany or Libya will the alliance hold on, or will it just shrink into a shell of its former self?

MS. HILL: It's a good question. Sir, can you guys come back down?

SPEAKER: I was wondering, I have really enjoyed the back-and-forth, but the question of is the modern force taking over the military force? What is actually your agreement on that? Which one is more powerful, the modern force or the military power? We see personally that it's the modern force, which is taking over the military force. So what's the future for the same kind of policy for Europe?

MS. HILL: You were saying modern force?

SPEAKER: The moral force.

MS. HILL: Oh, the moral force.

SPEAKER: I mean, the human rights and other things demanded by the population, which was oppressed and suppressed for generations, but it took over.

MS. HILL: Yeah, these two questions pretty much related as well. I mean, one thing that I wanted to add was when the NATO question came up because I was thinking about this when the two of you were in the last exchange. It was about Afghanistan. I mean obviously Afghanistan has not been popular in any European countries, but European militaries have been very active within the NATO framework and have taken considerable losses. And although that has resulted in some blowback

obviously, it hasn't necessarily led to a complete rejection of the necessity that people saw in the first place of being involved in Afghanistan. But Afghanistan has been a real test for the NATO alliance and also a big question more broadly for Europe. So, I mean, how to tie these two issues together, this emphasis on moral force. Obviously, if there's a withdrawal of or a reduction of the forces in Afghanistan, there's still going to be a large European involvement in Afghanistan in policing and some of these issues that you were pointing out that Europeans always point to. And there seem to be a very strong moral obligation for people to continue to be there. I mean, how much is NATO playing now in these debates within Europe on this very issue of which takes the precedence, the moral force, the soft power, or the things that Europe does very well against the military power?

MR. KAGAN: I don't feel confident about what the effect of Afghanistan has been on NATO, but partly I think it's been on the negative because I think that European publics have become very disenchanted with the involvement. The governments have held relatively firm because they're part of the alliance. I think the reason Europeans went into Afghanistan in the first place was out of -- not because they were particularly interested in Afghanistan. It was an act of solidarity. It was this kind of thing we do like, that one we didn't like, et cetera. And then they've been stuck ever since. But I would say that if anything, in Britain for instance, the taste left in their mouths of the British public is not a good one. And so -- and I personally feel that the United States made too much of the U.S.-European relationship about are you giving us troops for Afghanistan and neglected other things and focused on the things that the Europeans were least interested in doing actually. So I'm a little bit concerned about that, and I am concerned on Libya. It's such a mixed picture that I don't know how to feel about it. On the one hand, yes, you had the United States and Europe working together, but within NATO councils, it was very difficult with not only Germany, but with Turkey as well. And I don't know what -- I know they have given the issue of what is NATO with a Turkey that's

going in the direction that you're talking about in? I don't know. Maybe it will be fine or maybe it won't be fine. Turkey was enough of a problem when all they cared about was Cyprus.

MR. COHN-BENDIT: But Cyprus is a problem about the Greeks at the moment.

MR. KAGAN: I'm just saying, within the --

MR. COHN-BENDIT: Don't put this on the --

MR. KAGAN: Okay, I apologize.

MR. COHN-BENDIT: Okay.

MR. KAGAN: And my wife would shoot me for saying that, but --

MR. COHN-BENDIT: No, no. I'm a pacifist.

MR. KAGAN: But in any case, suffice it to say that I'm worried, I'm a little bit worried about, the future of NATO and especially as European capacity is declining. Look, British capacity is declining, and the British were such a big pillar in terms of the transatlantic military capacity.

MS. HILL: But this is why Turkey has a very important role in terms of the size of its country.

MR. KAGAN: Well, they have a lot of capability, but I don't know what they want to do with it anymore. And they were willing to use some of their force in Libya, by the way, as it turns out.

MR. COHN-BENDIT: Exactly, more than the Germans.

MR. KAGAN: More than the Germans, right.

MR. COHN-BENDIT: More than the Germans, okay.

MR. KAGAN: And on the morality versus military power, I don't see what the trade-off -- there's not a trade-off. You can only make good on your morality sometimes if you have military capacity. It's fine to say -- I'm not 100 percent sure I

understand what the nature of the question is -- but the moral force as we've seen throughout history does need to have some capacity to back it up. It isn't enough to feel the right things. And I think in the world today, unfortunately, military power is going to continue to be a critical element.

MS. HILL: I see a transatlantic trends question.

MR. KAGAN: Well, right -- well, that raises the question. Is morality something to be achieved by war? That's a good question. I think Americans and Europeans tend to --

MR. COHN-BENDIT: You gave the wrong answer in Iraq.

MR. KAGAN: You think I gave the wrong answer about Iraq? You could say we gave the wrong answer in Vietnam. I'm not saying that military force is always right, and I'm not saying the United States is always right.

MR. COHN-BENDIT: It's always a question.

MR. KAGAN: It's always a question, but I guess I would say the forces that agree with the things that we agree with have to have capacity.

MR. COHN-BENDIT: Was NATO in Afghanistan, too? I mean, the problem with Afghanistan today is the moral base why it started after 9/11 I think was strong. Now what we learn -- and I don't want to say whose fold it is -- but we learn in Afghanistan that wanting to do the good, if you do a lot of error from the beginning, then it became a nightmare. And I think the problem of Afghanistan is not to condemn it, to say let's be clear the error. Why we did things -- the Americans thought arming the tribes -- and now we can start all the debate on Afghanistan -- I think it's -- we have really to be clear that if there was a lot of error, that at the end of the day, it's very difficult to handle. So I would say for NATO, I mean, you're right with all the capacities, but I think the answers of Europe and capacity can only be given by the idea of the European army because they have no money the British. Poor Cameron, he would like to have much

more capacity. He would like to be, but he can't. And the German, it's the same. So I think this financial argument is for me a political one. Okay, let's think how to do it without coming back with a nation capability. It's -- I always come back to this, the end of the story of NATO. What I want not today, but I want to discuss is, isn't it the time to make a definition to take something like NATO and to think which is the army capability, capacity, that you end needs as you end. Because I think the world of today is a completely different world, and I think we saw of Libya and we saw everywhere that if you have a U.N. resolution, that what is the capacity and you see the problem that you end with in Nigeria. You see the problem -- I can tell you all the U.N. resolutions where the capability was none and then it was also a nightmare. So I would like once to have a discussion on the future of NATO's need and the armed forces of the united --

MR. KAGAN: That would put a great burden on Europeans if they have to create a European force and contribute to a U.N. force. You've got a real -- this is going to be a powerhouse of a Europe let me tell you.

MR. COHN-BENDIT: But I think first we have to learn to think a little bit bigger.

MR. KAGAN: What was the rapid-reaction force size supposed to be, the European rapid-reaction force? That was supposed to be 60,000 -- 30,000 deployable forces, and they haven't been able to do that.

MR. COHN-BENDIT: Yes, but you're --

MS. HILL: Give him time, and I'm sure he'll --

MR. KAGAN: I'm sure we'll get to 30,000 --

MR. COHN-BENDIT: I have no problem with you because the rapid-reaction force that we talk about, when starting in Bosnia there were none. You ask the Americans, I agree with them. I don't have the problem. I say yes, this is the argument why we have to think. And I can only say if you want to touch Europe and say the

German have to do their intervention force or the French will never get it. They will never get it.

MS. HILL: Well, we need to wrap up so that everyone can go out and grab some lunch before it all disappears like our coffee cake this morning. In the blink of an eye, the Brookings interns will get it before anyone gets out of here. I'm joking, of course. But I wanted to ask Bob and Daniel if you have any last thoughts on this. Let's try to leave everyone on a positive note because we would like -- as you said, it's always very difficult doing things in a crisis. And this is an unusual confluence of crises that we have now, not to mention volcanoes that keep erupting just when it's safe to fly again.

MR. COHN-BENDIT: Then I can go back.

MS. HILL: Exactly. So Bob, do you have any closing thoughts before we break?

MR. KAGAN: Well, the thought is -- and this gets back to the most basic point -- is that we really do need both of us to be strong in all the various dimensions of strength together because in my view, we have an increasingly competitive world geopolitically and, unfortunately, some of those major competitors like China and Russia are profoundly not where we are in terms of human values. And they are shaping the international system because it's inevitable that great power shapes the international system. And so this relationship is actually critical, and I'm -- we didn't even have a debate. I mean, there's almost nothing to debate except our optimism about the future. And I would love to be as optimistic as you are, but things are different than they were in 2003, the last time we debated, and I'm delighted to be on your side.

MS. HILL: Daniel?

MR. COHN-BENDIT: Well, I just want to say to Bob, look, I agree with you, your sentence what you love, that sometime in the world you need war. And I would

give you to say, but before you say yes, think three times. Because if you had thought three times before Iraq, perhaps you would have said at this time, this should be wrong.

MR. KAGAN: Did you think three times before Libya?

MR. COHN-BENDIT: No.

MR. KAGAN: Okay. Good. Thank you.

MR. COHN-BENDIT: No, no, but Libya was a big difference. Libya there were fighting for their freedom and there were millions. It was a city who has freed themselves. If in Baghdad there would be a free city and then Hussein --

MR. KAGAN: Oh, why was there no free city in Baghdad? Because Saddam had killed hundreds of thousands of people over 10 years.

MR. COHN-BENDIT: Yes, but there's a difference --

MR. KAGAN: But it wasn't happening, you see?

Now we've started the Iraq debate, and we're never going to have lunch.

(Recess)

MS. LAURENCE: Well, welcome back. Thank you all for returning to the afternoon session of the CUSE annual conference. My name is Jonathan Laurence. I'm a fellow here at the CUSE and a professor of political science at Boston College.

We're meeting at a very eventful moment. And for that reason, I'm especially grateful to our panel for agreeing to be here. As intellectuals and as policy makers, the members of this panel are faced with a deluge of developments every day. Each of them is contributing to decision making processes that are influencing the course of history and the lives of millions.

And during the extraordinarily eventful last 20 weeks or so, we've witnessed great displays of courage and personal sacrifice by the peoples of Tunisia, Egypt, Libya, Syria, Bahrain, among others. And we've seen the governments of the

United States and Europe adapt. First cautiously, and later with great alacrity to the changing circumstances on the ground.

And as President Obama said yesterday at Westminster, "These are early days. It will be years before these revolutions reach their conclusion." And in terms of the revolutionary calendar, it's fair to say that we are rapidly approaching the critical month of Brumaire. And as one rather influential German theorist might have put it, how do we avoid having these outcomes of the volatile situations before us descend into either tragedy or farce?

As we speak, right now, G-8 leaders are meeting in Calvados, near Deauville, to discuss their support for uprisings in the Arab world. And it is expected that they will announce large aid packages in response to the requests by Egypt and Tunisia for roughly \$25 billion and \$12 billion, respectively.

The European Union inaugurated an office in Benghazi last week, and the Commission recently increased its humanitarian aid budget for Libya and updated its neighborhood policy for the region. The State and Treasury departments here have recently announced a debt swap arrangement that will permit Egyptians to invest in job creation and entrepreneurship.

So, the situation and the U.S. and European responses are evolving by the day. And here to offer some reflection on developments to date, and to speak about how the United States and Europe can continue to accompany their Arab partners during this crucial and rather molten phase, is a panel of very distinguished guests. And I am grateful to each of them for taking the time to be here today.

To my immediate right is Tamara Wittes, deputy assistant secretary of state for Near Eastern Affairs, and formerly a senior fellow in Foreign Policy Studies here at Brookings. She is the author of the very influential book, *Freedom's Unsteady March: The American Role in Building Arab Democracy*.

To my right also is Mr. Hugues Mingarelli, managing director for the Middle East and Southern Neighborhood of the European External Action Service. He was previously deputy director general of the Commission's External Relations Directorate, and was also the founding director of the European Agency for Reconstruction.

And to my left is Madame Ana Palacio, former foreign minister of the Kingdom of Spain and founding partner of Palacio y Asociados, and who has also served in a number of key positions in both the Spanish and European Parliaments, in European and American think tanks, as well as a number of international organizations.

I've asked each of them to speak for about seven minutes, beginning with Tamara and following the order of introduction. After which I will ask a few questions and then open it up to the audience. So, please, Tamara. Thank you.

MS. WITTES: Well, thanks very much. And I'll just say first what a pleasure it is to be back in my former home here at Brookings and to join you for this wonderful annual event.

You know, I think that there are a lot of myths and stories about the Middle East and about external relations with the Middle East that have been blown apart by the events of the last months. And those of us who have been working on these issues are faced with these events -- with a sense of humility going forward, because so many preconceptions have been dismantled.

But I think that there are a number of ways in which that dismantlement has been highly constructive. Of course -- and as both Secretary of State Clinton and the President have noted certain myths about the region: that Arabs are somehow demobilized or politically passive; that they're not interested in the rights and freedoms that the rest of us enjoy and that are yearned for universally around the world. These myths -- to dismantle these is certainly worthwhile.

But I think that it's also been useful, recent events, to help us examine

some preconceptions about the role of external actors in the Middle East. I think that in many ways, we've been able to move in the last several months past some old and somewhat tired debates about the role of external actors, especially the U.S. and Europe, you know, old notions that external involvement is always somehow unwelcome interference, a violation of sovereignty, a new form of imperialism.

But also, the notion that external engagement on the set of issues is -- must always be either wholly altruistic or wholly self-interested. And I think also there's been a bit of deconstruction of the notion that, well, if only Western governments expounded clearly and resoundingly on democracy and human rights, the dictators would fall. So, I think that we're in a much more constructive place as we deal with these events.

Now, there's no question that the people of the Arab world have made their views clear. That they see political change as the best way for them to address all of the concerns that they face about their communities and their futures. Their economic concerns and their security concerns, as well as their political concerns.

Our role, therefore, is to welcome that development and to recognize it for what it is: that it provides us with an opportunity in many ways to strengthen and expand the foundations for a sustainable, long-term U.S.-Arab partnership, a partnership that President Obama has envisioned and worked toward really since he entered office; the notion that our relationships in the region should not simply be government to government, but that we must engage more broadly with citizens of the region and be responsive to their concerns.

What the events of the last months have highlighted is the extent to which the status quo at the governmental level, and the relationship between government and citizens in the region, is not stable. And it's not sustainable, and the President spoke about that at length last week. And that as a result of that, that status quo is no longer an

environment in which we can reliably pursue all of our interests in the region.

And our interests in the region, I think both ours and the -- and European interests remain very much the same: to prevent terrorism and prevent the proliferation of weapons of mass destruction, to protect global commerce, to ensure the security of our partners in the region, and defend against aggression. All of these interests remain. All of them -- the achievement of these interests demand stability. And I think what's become crystal clear -- if there was any doubt in some minds in the past -- is that stability in the region today demands democratic change.

So, as I said, from the beginning of the administration we've really sought to broaden our relationships in the region beyond governments, to reach out to people to find common ground, to work on the basis of mutual respect and mutual interest, and create greater reciprocity. And I think part of that common ground that the President spoke about in Cairo two years ago has been a shared commitment to freedom and dignity and opportunity. A shared commitment with people in the region to democratic values.

And we've worked hard in my bureau and the work that I do supervising the Middle East Partnership Initiative to build more and stronger partnerships on that basis. So that today, half of the projects that the Middle East Partnership Initiative has in the Middle East are direct partnerships with indigenous NGOs, as opposed to large projects run by organizations here inside the beltway. And I think that's just one example of the kind of change that we've tried to introduce from the beginning of the administration.

Now, going forward as the President laid out last week, our approach to supporting political and economic reform across the region -- our approach to supporting these indigenous demands for democratic change -- will rest on three pillars: political, economic, and security.

In terms of political change, as the President mentioned, we need to start with

Egypt and Tunisia and ensure that we sustain a strong commitment diplomatically, programmatically, and in a variety of different ways for the transitions that are underway in those countries, because they will take a long time to come to fruition. But we also need to continue our support for democratic change in other places. And to support activists and civil society organizations who are working in their own communities on behalf of the agendas that they have set for their countries and their local communities. And to make clear our readiness to engage with all peaceful groups, even those with whom we may disagree on policy issues.

I want to talk a little bit more about the economic tools that we have to support democratic change in the region. Because I think it's important that we understand the role of those economic tools. And this is something that on which there's been intensive engagement between the U.S. and Europe in these last months.

There's no question that economic conditions in the region contributed to the events that we've seen underway, but I think it's important to emphasize that the drivers of these events are not simply economic. It's not just about economic deprivation; it's not just about unemployment. What's been going on in the region is about dignity and opportunity, which has economic elements but it's actually much broader than that. It's about equity, it's about fairness, it's about access to opportunities.

So, it's important as we work to create a supportive economic environment for political change that we keep our eye on those fundamental demands coming from citizens in the region. But it's also important for us to recognize that economic challenges in Egypt, in Tunisia, and elsewhere -- if they're not addressed effectively and urgently, can compromise the process of political transition. Not only in the short-term in terms of stabilization, which I think is a lot of the goal that we're seeing manifested in the decisions announced by the President last week in terms of debt relief for Egypt and loan guarantees. And also what's coming out of Deauville. But also, in the

longer-term, to ensure that as these countries move down the democratic path that we are helping create an environment in which they can deliver for their citizens, and that that is an important element of creating the conditions for successful democratic consolidation.

So, economic stability is important, but so is a long-term commitment to expanding individual opportunity combating corruption, supporting private sector development and entrepreneurship. These are the things that will truly deliver on the promise of these changes for individuals on the ground in a way that they can see and feel. And those are long-term efforts, but they're important.

So, I could go on to talk a bit more about the specifics in each place and time, but I'll stop there and perhaps we can get into that in the discussion. Thanks.

MR. LAURENCE: Yeah, we'll get back to that. Thank you very much, Tami. Mr. Mingarelli?

MR. MINGARELLI: Many thanks. It's a pleasure, obviously, to be here to exchange views on what the European Union and a few other actors have been trying to do in what you call the Middle East, or the Near East. What we call the Maghreb and Mashreq Regions.

As you all know, Europeans have been present in these regions for good and bad reasons for centuries. And over the last two decades we have conducted our policies toward these countries.

And there are two policy frameworks. In 1995 we launched the Euro-Mediterranean Partnership, better known as the Barcelona Process. And in 2005, in the wake of the latest EU enlargement and the European Neighborhood Policy.

We have been developing our relations with these countries since -- over the last five years, and other neighborhood policy. And we decided a few months ago to carry out an assessment of the impact of this policy on our neighbors. And we got a very

mixed picture of what we have been doing. On the one hand, there are a few achievements. On the other hand, a lot of shortcomings.

The few achievements. First of all, there is no doubt that since 2005 we have been able to intensify in a considerable way our bilateral relationship with each of our countries in Eastern Europe, in the South Caucasus, in the Maghreb, and in the Mashreq Regions. These mean, obviously, that we have been able to better understand each other, to deepen our political dialogue, to enhance our economic and trade links, and to better understand the regional conflicts which still exist in these countries.

We have been able as well to support the democratic processes that some of these countries have known. And I have in mind in particular the revolutions which took place in Ukraine, in Georgia, and the democratic transformation in Moldova.

Some of our neighbors have conducted, as well, useful and necessary economic reforms. And the EU, thanks to our trade and economic links, have contributed to these. And I have in mind the reforms carried out in Morocco, in Jordan, in Ukraine, in Georgia.

Finally, the joint action plan that we have drawn up with our neighbors in the framework of this neighborhood policy have become reference documents for the authorities of our neighbors when they shape their domestic reform programs.

But obviously, the shortcomings are more numerous than the achievements. First of all, we have not been able to promote democratic reforms in the vast majority of these countries. In countries like Azerbaijan or Belarus, the situation has deteriorated. And in most of the Arab countries, there has not been any democratic progress, to say the least.

Weak governance and poverty remain serious challenges in most of our neighboring countries. In some countries, as I said, economic reform not being conducted. But overall, the living conditions of the population remain very difficult.

And finally, regional conflicts remain there and continue to hamper the

development of these countries. You all know what these regional conflicts are about. On our Eastern borders, we have Transnistria, Abkhazia, South Ossetia, Nagorno-Karabakh. In the South, we have Western Sahara, and obviously the Arab-Israeli conflict.

There has been, as well, a few developments over the last two years in the EU which lead us to think that we should review the way we develop our policy toward these neighbors. And these developments are well-known. Basically, the entry and to enforce the Lisbon Treaty in 2009 -- at the end of 2009 -- created a new situation. First of all, we have a provision in the Lisbon Treaty which provides for a special relationship between the EU and its neighbors. And it's a novelty.

So on point, we have now a representative for foreign policy with, at the same time, a vice president of the European Commission. And are that -- their disposal the European External Action Service. And all these should allow us to bring together all EU instruments which, up to a few months ago, were different heads.

So, we decided to review this policy and to try to draw the lessons of what had been wrong over the last years. And at the same time, to draw the conclusion of the Arab uprising. So, the popular uprising in the Arab countries taught us that, first of all, -- it has already been said but I want to re-insist on that -- stability without democracy is not sustainable. And here, I think that we have all collectively, at least in the EU, committed a mistake.

Second point, we have a confirmation that human rights and basic democratic principles are not Western values, but universal ones. And finally, we have to recognize that change has to come from within. There is only so much that outsiders can do.

The EU response to these events came in two steps. In early March, the Commission and the high representative issued a communication entitled "Partnership for

Democracy and Shared Prosperity" to react to the events in North Africa and in the Middle East. And yesterday the Commission and the high representative issued a communication which embraces the rule of our neighborhood. Namely, our neighbors in Maghreb and Mashreq, but in our neighbors in the South Caucasus and Eastern Europe as well.

The key principles of the new approach that we intend to develop can be summarized as follows. First of all, in our policies towards these countries, more emphasis should be placed, obviously, on democratic reforms. Democratic reforms start with free and fair elections, but we have to go beyond. We have to redouble efforts to create in these countries freedom of expression, assembly, to establish independent judiciaries, to make sure that the law enforcement agencies are really and under democratic control. Basically, we have to ensure that in these countries, democracy does not stop at the election. But that we create, really, the institution which will allow a real and deep democracy to take root.

Second point, we have to put a stronger focus on the civil society. Up to now, we have tended to favor, to privilege, the government-to-government relationship. Now we will have really to put more focus on the civil society and the media. And in this regard, one of the main lessons of the Arab uprisings is that women and young people are central to the democratic progress, because they have played both in Tunisia and Egypt a key role -- a major role in the uprisings.

We will have as well to better differentiate between countries. Namely, we will have to make sure that the EU offer and this policy is tailored to the specific needs of each partner country. We were aware, obviously, that a one size fits all approach would not do the trick. But we are now more aware than ever that our policies have to be tailored to the specific situation and aspiration of each of our partner countries.

And finally, we would like to place at the center of our policy what the

high representative, Cathy Ashton, has called "mutual accountability." Namely, we have to monitor very closely the reforms undertaken by our partner countries in the political and economic areas. But, they should be allowed as well to monitor that the EU deliver on its promises.

So, these are basically the key principles and outlying our policy. Now, obviously, our policy will be credible if we are able to put on the table a credible offer. And we have to recognize that up to now, we have not done enough for our neighbors. And we would like, in this regard -- and I will stop in one minute -- to beef up our EU offer, mainly in the following areas.

First of all, in order to establish a real partnership with civil societies, we will set up two new vehicles. We will set up a civil society facility, which will allow us to be more efficient in boosting NGOs. And second point, we will set up -- and this is a proposal which was put forward by the Polish foreign minister, Sikorski, and backed by numerous members of the European Parliament. We want to set up a European endowment for democracy, in order for us to be able to back -- to support political parties and non-registered NGOs and trade unions.

Second point. We want to intensify our political and security cooperation with neighbors. This means, in one sentence, that the EU should be more involved in all the regional conflicts that I have just mentioned.

Third point. In order to better support sustainable economic and social development, we have to strengthen our industrial cooperation and support the improvement of the business environment. And obviously, we have to coordinate with our American friends.

We have to promote the direct investment of European small businesses in this country, and put in place a credit line and micro-credit to favor the development of small businesses. We would like, as well, to develop pilot regional development

programs, because as you know, there are huge development disparities between regions in one single country.

If, for instance, you take the case of Tunisia, one of the main things that our Tunisian friends told us after January is that there is a huge disparity between the literal -- the Riparian Regions and the Continental Regions, in terms of economic development. And this is a source of major economic imbalance in their country.

We would like, as well, to enhance our dialogue on social and employment policies, and make our macroeconomic policy develop more effective. There is an area as well where the EU should do far more, it is trade. In trade, we have a very clear objective. We would like to develop with all our partner countries, when the conditions are ripe, what we call deep and comprehensive free trade agreements. This means that in addition to removing the remaining customs tariff barriers, we would like to get rid of all non-tariff barriers. Which means that we should assist our partner countries to take over our regulation norms and standards, so that they can really export their products without any remaining difficulty.

We should, as well, in a number of key sectors enhance our cooperation. And we have particularly in mind energy, where we would like to integrate all our neighbors in our electricity and gas sectors. This is important for them, but this is important, above all, to consolidate the independence and sovereignty of a number of them.

In this regard, we would like to favor the participation of these countries and in EU agencies and programs. All the sectors where we would like to redouble our efforts; climate change, environment, and transport. Because it is clear that in all these sectors we have no borders.

And finally, there is an area where all our neighbors expect more from the EU, but it is a particularly sensitive one for our member state. It is the area of mobility

of people. In two words, what we would like to do is pursue visa facilitation with a selected number of neighbors, to pursue visa liberalization with the most advanced of them, and to develop with all of them mobility partnerships to reach a better management of migratory flows between these countries and the EU.

And my last word, obviously, will be about money. We will increase our funding, and the community instrument. We will get more funding, more loans, from the European Investment Bank. And we are struggling to extend the mandate of the European Bank for reconstruction and development to the countries of the Maghreb and Mashreq regions.

This is in few words how I can present our intention.

MR. LAURENCE: Thank you very much. We'll definitely come back to many of those points. And I'm sure I'm not alone in remarking -- the degree of convergence that exists, actually, that exists between American and European goals at this point. And perhaps our next panelist will show us where some of the daylight exists between the United States and Europe. You who do not have the burden of government at the moment. Please share your insights.

MS. PALACIO: Thank you. First of all, I must begin by saying (inaudible) that it's a great honor to be here, to be in Washington, to be at Brookings. And Brookings, it's a reference. It's a reference, as you know, for certain times. Especially we Europeans, we forgot that there was a Pacific coast to the United States. But now, often, we feel that Americans forget -- right or wrong -- but forget that there is an Atlantic coast to the United States. So, this is important for us.

This is my second comment after my gratitude. It's just methodological. In seven minutes you have to proceed by big brush strokes. So I will be provocative, and of course no nuances. Maybe in the questions and answers, there will be time for nuances.

Well, the first thing is that from a European perspective, yes of course there are differences. And Hugues Mingarelli has made a really perfect presentation of the neighborhood policy. But of course there is Yemen. There are the Gulf Cooperation countries. And these are important for Europe -- as important for Europe, or even more important, if I may say so, than for the United States.

And frankly, there is the elephant in the room, Iran. There -- I mean, somewhere we have to mention that Iran is there. It's a big elephant in the room.

Now, second idea. This difference is not just about countries. And there are differences. The tensions in some countries -- these tensions between Shia and Sunnis, tribal force. It's also that our tools to address -- and through this, I join what Hugues Mingarelli has said -- our tools are different. We have the Neighborhood Policy.

On the Neighborhood Policy, just to complete what -- as I said, I fully agree with what he has said. But I would add two things. The first is that, yes, the (inaudible) process from '95 to 2004, 2005 just did not live up to the expectation.

If you take the Barcelona Declaration, you will see that out of -- if I remember correctly -- out of 18 paragraphs, 11 refer to reforms, democratization, et cetera. Reforms, in a sense. Five or six to security. But of course, in '95, we did not have the immigration pressure and we did not have the security pressure. So, after the Barcelona Process changed -- and in the end, it was not these goals that were behind the policy -- the -- you made Iranian policy. But this policy was driven reactively by immigration and by security. This is the first thing that I think we have to remember.

The second thing is that, yes. In 2004, we included the Southern border -- what we understood -- and in those days, I participated actively from government. We have to have a similar approach to the south and to the east. To the east, European Union was very tough -- or insistent on reforms to the east. To the south, as I say, we didn't live up to the Barcelona Declaration that was -- really stress this, but we didn't live

to this expectations because of, you know, reality. Reality on the floor. We have to understand that we cannot just forget about the interests. Values are important but interests are everyday bread and butter. That's when you are there.

But what Mr. Mingarelli hasn't mentioned is the last, the (Spanish), where there, honestly, all idea of reform disappears. And all these goals of reforms are replaced by the idea of de-polluting the Mediterranean, which is, frankly, a very important task to do, but far from what was the Barcelona Declaration.

So, unfortunately, we tried to equate European policy to the South -- European policy to the East. And just a clear example, the EBRD was not extended to the South. The EBRD, in its charter -- in its constitutional charter, has an idea of reform promotion, of democracy promotion, which was not extended because of all these issues that I have mentioned.

So, this last updating of our Neighborhood Policy, I hope will be now the moment where really our -- we look to the east the same way we look to the south.

Now, I think that we have mentioned the timeline. And we also have to mention the realities on the ground. Many people try to equate the Arab Spring with the fall of the Berlin Wall. There are many differences, and maybe we can discuss this. But there are two major ones. We have no money -- really, the crisis means that there is issue.

And as European Union, we do not have the magnet of enlargement. Frankly, we have been extremely successful. The European Union is the most successful project in stabilizing, in bringing prosperity. But honestly, behind this was the magnet of belonging to the European Union which, frankly, it's not the case. Just as a telegram. Let's think of innovative approaches, like the European Economic Area, for instance, which is a clear possibility.

Now, having said all this, what are the challenges? With differences,

with all that. I have put them under five headlines. The first is security. And of course, I fully agree with what Samantha White has said. And I will only add that security is also important for our neighbors. We have seen how much money Tunisia and Egypt are losing because of the lack of security. Because of tourism, because if there is no security there will not be investment, et cetera. So, security.

The second is institutions. The second heading. And of course, when we speak about the institution, I have to say we say, well, there was a hunger for democracy. As Tamara Wittes has said, it was a hunger or cry for dignity for just -- not exactly for democracy as we understand it. So, in all honesty, we have to ask ourselves, what democracy? What democracy? By this I mean a formal democracy? Just election? No. We need to reinforce institutions.

And I will just add there that at the same time, we cannot be Euro-Atlantic centered. And we have to understand that the legitimacy in these countries in general, but in certain countries -- I will think of Jordan and Morocco -- the legitimacy of the king being the descendant from the prophet, being the commander of the faithful, is something that we have to put into this puzzle. I'm not saying by this at all that we have to give up or taint or diminish our stand for the universality of human rights. But this idea that legitimacy in those countries, we have to take into account this historical, traditional legitimacy that for us brings us to (inaudible). But it's not -- our reality is something that we have to do.

What I think that we have to understand is that what is asked for is sharing power, more -- empowering the Parliament truthfully. Having institutions that really just share the power. There is a shift of power. Not -- and this, I think that the word is reform. Wherever -- I mean, there are places where reform is -- it's a bit too late for it, reform. But anyway, in those where reform -- reform is -- it's okay.

In this idea of security, of course, there is another immense area. Which

is, legal security and bringing to the rule of law. Because of course, the rule of law we cannot expect those countries to have the rule of law from one day to the next. But yes, we have to address corruption, to address all these issues. And this idea of legal security that has a lot to do with the possibilities of investment, of prosperity.

And with this, I -- my third heading will be market economy. Honestly, for us in the U.S. and in Europe, it's (speaking in a foreign language). Well, it doesn't -- it's not on the ground there. What we read so often that socialist approach to economy is disappearing, it's not true. If you listen to the voices on the ground, in many cases -- I'm not generalizing -- but in many cases, because they are asking for dignity, they are asking much more for equality. And not just for equal opportunities, for equality. And in many cases, free market economy is seen as the source of many evils. As a system that has privileged few, and that has gone against the majority.

And I think that there, we have a lot to do in pedagogy, in explaining what is really market economy. That market economy is not corruption. Market economy is legal security for everyone.

In relation, between these two headings, I think that we have a big challenge with parties there. And this is not for governments; this is for the IRIs, the NDIs, all these institutions, the EPPs, the socialists, internationalists. We need to be there to be in this area of citizenship, but, frankly, as political party.

My fourth heading is education. We haven't mentioned that. But frankly, when you see that the Pew Attitude Report of 2010 tells you that 84 percent of respondents in Egypt favor lapidation of adulterous women, that 76 favor cutting the hand of the thief, and that 82 -- it's a little bit less -- of the respondents favor just death penalty for the apostate, well, you know, this idea of democracy and human rights and just this longing for democracy and human rights, we have to reinterpret it. Because as I said, these are the Pew Report figures.

So, what I think that in all these countries, there has been an effort in education. But frankly, the quality of the education is not there. And I think that as Europeans, as Americans, we can at least have an influence on just bringing a more inquisitive-oriented education. Not repetitive education. And I'm paraphrasing something written by Marwan Wasser in his book on how this is still -- this repetition and this ideas of religion, et cetera, are part of it.

And my last heading is we need to strengthen the middle classes. Because I would say that this is a summary of all the above. Strengthening the middle classes is the big challenge in all these countries. Even with all the differences. Strengthening the middle classes.

Because the middle classes ask for better services. For a Moroccan stability just are better armed to combat corruption, are better armed to organize themselves in political parties.

But of course -- this is my last remark -- you cannot just strengthen -- not create, because they exist -- create a middle class from one day to the other.

And my last, last remark is linked to this one, is that in countries where demography is so young, I think that what the -- our expectations can be high, and we can be optimistic. Because, I mean, I'm not Egyptian, I'm not Tunisian. But what I feel is that even the most illiterate young man or woman in the last village in the Nile or somewhere in the desert just feels more empathy and feels closer to this middle class model that he has seen in all these revolutions than to other classical models. And because he or she will appeal to this model, we have -- I mean, we have a real possibility for the future.

Is it going to be easy? No. Is it going to be messy? Yes. But that's the name of the game. So, thank you.

MR. LAURENCE: Thank you very much. Well, let me take one of

Madame Palacio's points and put it to my two speakers on my right. Since she raises the point that we are in a time of budgetary austerity, money is not as plentiful as it was, perhaps, 20 years ago after the fall of the Berlin Wall.

Tami, you've written in the past that the United States faces a choice of being either a midwife or a spectator for Arab democracy. Does the amount of money that we have available buy us a seat in the operating room? Is there, moreover, a chance to create the kind of positive conditionality that you've mentioned? And I know that the European Neighborhood Policy also speaks of the formula of more for more, in the same sense.

Would either of you be willing to comment on that, please?

MS. WITTES: Sure. Well, look. I think this is a very important question, because as Ana noted, we're in a different circumstance today than we were in 1989. And that requires us to be creative.

But I also think it's important to recognize that beyond the sort of urgent needs of economic stabilization, the real path to growth and development and a kind of development that reaches all people in this region is not going to be thorough assistance, primarily. Assistance is important in targeted sectors to help facilitate certain types of reforms, certainly to support civil society, because there isn't a really good mechanism for philanthropy for civil society in this region yet.

But what we really need to work on is what you were just talking about, which is the need to create a magnet for this region to keep countries and interest groups within countries pointed down the path of democratic reform. And that's about assistance money, primarily. It is about the issues that my colleague from the EU has been explaining are a challenge, and something we have to struggle with: trade, market access, and migration and mobility.

So these are really important issues for us to work on together. The

President spoke about a trade and investment partnership initiative that we envisioned. But I think in order for it to be at its most effective, it's something that we will need to do together to really make that magnet as powerful as possible.

MR. LAURENCE: Thank you.

MR. MINGARELLI: No, I can just support what has just been said.

Assistance is not the main vehicle we should use to support economic development. We should put a strong emphasis on trade; there is no doubt about that. Market access is important, but the removal of non-tariff barriers as far as the EU is concerned is even more important. Because the main obstacle of the exports of products from North Africa to the EU market is not customs duties, but regulation norms and standards. And therefore, we have to assist them in taking over what we call (French), namely the body of (inaudible) which make our regulation norms and standards.

Second point, we have to work to make sure that these countries can attract the investments they need. The foreign investment they need. And therefore, we have to provide technical assistance, which is not extremely expensive, to ensure that they will create an environment -- a legal and regulatory framework, legal certainty -- which will allow foreign investors to go to these countries.

Finally, we have as well to better manage our limited resources in two ways. First of all, we have to be more cost-effective in the way we manage our assistance budget. And second point, we have to ensure that our limited resources go where we have our political priorities. And this is something, again, where in the EU we can do a lot. We have started by redirecting part of the resources of the region towards our neighborhood.

MR. LAURENCE: Now, if I could just -- if I could just follow up a little bit. In the second panel of today's conference there was very little agreement on the notion of the EU as a unitary actor. And you've been speaking of it in these terms. And if we can

just drill down a little bit on the external action service and its competencies and its responsibilities, to what extent does it enjoy the consensus of its members? And to what extent can we accuse it of having competence creep, or whatever British politicians sometimes refer to it as?

MR. MINGARELLI: In certain areas, we have exclusive competencies. This is the case of trade, for instance. In other areas, obviously, we have to work on the basis of consensus that we have to forge among 27 member states. But this is what the EU is about. We have to live with that.

MR. LAURENCE: Thank you.

MS. PALACIO: Just one sentence. Do we need money? Honestly, yes. Let's not fool ourselves. Why? Because at -- I mean, one of the issues that we need to address is the regional integration. And we need to understand that there will -- there is a need of investment in infrastructures. And this is a must. I think that another of the changes from the Barcelona Process to the Neighborhood Policies -- that the Barcelona Process had a regional approach. Integration of the region approach.

The Neighborhood Policy is just radial. It's just European Union, which is -- with each of the countries. Which is, by the way, the American approach as well. But we need to integrate this region. We need to vertebrate this region. These economies are absolutely enclaved. The regional exchange in many of them -- the commerce. The regional commerce is less than 10 percent, which is not really -- it's not realistic.

And investing in infrastructure, we will need to address this. And this is why I think it's so important that the European Union and the United States coordinate its effort and make sure that the money that the World Bank and other institutions invest there just goes to the priorities. I fully agree. We need to prioritize.

But among these priorities, we will need to vertebrate this region so this region just integrates physically. And not just physically, social. Which, by the way, has a footnote

on what you mentioned about -- no, Hugues mentioned on the frozen or not frozen conflicts, especially the Western Sahara. The frontier between Morocco and Algeria is closed.

MR. MINGARELLI: Closed.

MS. PALACIO: We need to make these frontiers reopen. And that there is an exchange of electricity, of goods, of people. This is something that we have to address.

MR. LAURENCE: Thank you. And Tami, if we think about the announcement of charges against former president Mubarak, what is the effect of that on the U.S. Government's attempt to engage other governments in the region to go down the path of reform? Does it have a chilling effect? Or is it something that you simply have to work with?

MS. WITTES: Look, I think that, obviously, that's a question that's a subject of intensive debate inside Egypt, as transitional justice always is in such situations. And every country finds its own resolution to these challenges.

But I think the important point here and the point that we've worked hard to make to partners across the region is the importance of getting out ahead of these developments and of listening to people before things get to the crisis point, to initiate a process of real dialogue between government and opposition to bring in civil society who can help come up with solutions that can move a country forward in terms of legal reforms and institutional reforms that are necessary.

And so if you have that process ongoing, then you don't -- you know, it's not a question of revolutions across the region. And our hope is that we'll see a more inclusive kind of politics taking place everywhere.

MR. LAURENCE: Thank you. Well, I'd like to open up to the audience. I'm going to be gathering three questions at a time. And I would just ask you to state

your name and your affiliation, and put a question mark at the end of your question.

I'll start with this gentleman here.

MR. ISLA: Thank you. My name is Ron Isla from the American Institute for Contemporary German Studies. I have two questions to Mr. Mingarelli.

So, you are saying that the European Union now tries to be a stronger actor in security politics, trying to establish a strategic dialogue with its neighborhood. And I'm wondering if this really brings an added value, especially against the backdrop that even in former times, the EU already tried to be an actor in foreign policy and security policy.

I well remember the inauguration of the Union for the Mediterranean in 2008, when Mr. Sarkozy gave a warm welcome on a red carpet to one of the biggest slaughterers of our time. And there are also loads of references in the action plans of the Neighborhood Policy referring to security politics.

So I'm wondering -- and to be provocative, as a European, I would say, we don't need any more new buzzwords like "governance facility" or "endowment for democracy." We need the will and the determination of the Europeans because all the instruments are already at hand, I would say.

And secondly, just quickly, against the backdrop of the Syrian crisis. And I know of the sanctions the European Union took. I'm just wondering, is there any action also going on behind closed doors? So, what are the possibilities now for the European Union to seize influence on the Damascus Region?

Thank you.

MR. LAURENCE: There's the question mark I was looking for. Okay, next please.

MR. BEARY: Brian Beary, U.S. correspondent for *Europolitics*. I think my question is more directed towards Hugues and Tamara. Both of you used the same

sentence; the status quo is not sustainable. And I find it kind of fascinating because I think if we were here six months ago, neither of you would have used that sentence.

MS. WITTES: Actually, I think I published it in 2008.

MR. BEARY: Oh, really? Okay. Well, which leads to my question, which is, did you in any extent see this coming? And if not, why not? Why wasn't it on your radar?

MR. LAURENCE: Let me take one more. From the back, the gentleman with his hand up. Yes.

SPEAKER: Thank you. My name is Yaya Fanusie. I'm the lead person for the Special Operations Division of the United States of Africa 2017 project.

I enjoy your recitation of what's going on in that area. What I'm specifically looking at -- North Africa. Can you tell me all the predictions focused in or recommendations you're making? Who are the people that you've been talking to? The new movement or representatives of the dying ruling class, political class?

MR. LAURENCE: Thank you, sir. Let me allow the panelists to respond.

MR. MINGARELLI: Okay. First question, the EU has already been an actor in foreign security policy. Yes, I just said that we should be more present in the regional conflicts in our neighborhood. Ana Palacio reminded that the Western Sahara conflict basically prevents any kind of regional cooperation in the Maghreb. The coast of the non-Maghreb is enormous for the four countries of the Maghreb Region. So, five -- if we are the Mauritania. And the EU is not present -- as such, is not present at all. You know, we are just supporting the efforts employed by the envoy of the UN secretary general. But the U.S. as such does not intervene in this conflict.

And we are not entirely absent of the Israeli-Arab conflict. We are not totally absent in what is going on in Transnistria. But above all, we do not place a role that we should play in these conflicts. If you want, I could elaborate. I don't know what

more we could do, basically, to be full-fledged members of the format in which we are seeking political solution. And when there is a need for peacekeeping forces, we should be there as well.

Second point, the political will is more important than new instruments, new gadgets. You are right. Without a political will, there is very little we can achieve. But even when you have the political will, if you don't have the appropriate instruments you are in a predicament.

I said that we will set up a new endowment for democracy to fund political parties. I have been struggling for more than 10 years to try to assist the civil society in Belarus without an impact, just because in Belarus NGOs cannot be registered. And we, with our current EU instruments, we cannot assist non-registered NGOs. I hope that tomorrow we will be more effective with this new instrument.

Syria, we have the sanctions. But at the same time we continue in various ways to try to convince President Assad that the best way forward and the only way forward for him is to stop the violence and to start to engage a national dialogue with the demonstrators.

I want to leave my friends answer as well a number of questions.

MS. WITTES: Sure. Let me perhaps start with the gentleman's question in the back about to whom are we speaking as we develop our response. And I think it's important to emphasize that there's an incredible diversity of groups on the ground in Tunisia and in Egypt. And indeed, since these revolutions the diversity has grown, so that in Tunisia today, for example, you have over 70 political parties, most of whom didn't exist a few months ago.

So it's absolutely imperative as we go about this work that we engage very broadly. And that's what we've been working to do through our embassies and in a variety of other ways. And I think again, that this type of broader engagement and expansion of the

range of views to which we expose ourselves and which we integrate into our thinking is part and parcel of the broader engagement strategy that President Obama has brought to his approach to the region from the beginning.

To the provocative question, did you see this coming? And if not, why not? You know, I think if you poll Middle East experts and -- for better or worse, I guess after 15 years I would put myself in that category -- I think you'll find very, very few who, if any, who predicted these events. Why? Because revolutions are always unpredictable.

But I think what a number of people did recognize -- and I'll include among this my secretary of state -- is that pressures have been building in this region for some time. Ana referred to the demographic balance, and the trend in the region has been quite visible. And the rise of this young generation has placed new pressures on governments, pressures that they had a difficult time accommodating. The rise of satellite broadcasting and new media tools and the way that this changed organizational capacities outside of government.

And, you know, the sense -- the ability had to access information and become more aware of the disparities between their aspirations and the realities that they faced. Their aspirations and what they saw elsewhere in the world, and what they had available to them at home. I think all of these trends have been building in the region for at least a decade. And while the approximate causes, I think, are inevitably unpredictable, the ingredients were there.

And finally, I'll just say on regional security issues -- because it has kept coming up. And I want to emphasize that this is absolutely an essential piece of how we do things going forward. And that we do need to recognize the interplay between regional conflicts and the other things that are going on. And I think that we've found in these last months very close cooperation between the U.S. and Europe on the broad range of security challenges in the region in a way that's been very constructive.

MS. PALACIO: Well, three very -- one sentence on each.

On the European Union, yes, of course you need political will. But, you know, bashing the foreign policy or the European Union as an actor is so easy. You know what? What -- I mean, it's a process. It's working in progress. And yes, it's not perfect and yes, there are many flaws. But I think that I would tend to see all, you know, the glass half full.

I will add a footnote on this idea that we have to -- we need to engage broadly with everyone. And just link this with the role of big formations of -- political formations. I mean, in Spain the first democratic elections there were more than 130 parties. And from 130 parties, well, this was filtered. And in great part was filtered through the big families -- the big political families. So these would be my footnotes there.

MR. LAURENCE: Thank you very much. Let me gather the next three questions. I have one in the back?

MR. DANZIG: Thank you. Two questions to Tami Wittes. Number one, could you also --

MR. LAURENCE: What is your name, please?

MR. DANZIG: Sorry. I'm Rafi Danzig with APEC. First question is could you also talk about Syria, specifically? What the policy is vis-à-vis Syria?

MS. WITTES: Sure.

MR. DANZIG: And number two, you said that we are engaging both with those groups with which we agree and those we disagree -- with which we disagree. I suppose you mean like the Muslim Brotherhood, groups like that. And my question is is it possible to engage with all of them equally or to favor those groups with which we agree over those with which we disagree?

MR. DETKA: Dieter Detka, Georgetown University. I'd like to come back

to the notion of regional integration and the concept that Ana Palacio mentioned, use regional integration in Europe's neighborhood.

And what I see happening now is that Europe uses too much a kind of hop and spokes approach without really furthering corporations in these neighborhoods. And that's essential, because millions and billions of dollars went into the Southern neighborhood -- into individual states -- without almost zero effect, to be honest.

And in that context, I think you need a regional approach plus a better and smarter approach to what is called usually conditionality. You know, there is a way of killing the good part with a conditionality trap. But Europe has power and has enormous economic power in trade, investment, many other things. And that needs to be on the table more than it has been before. And I want to hear you talk about it.

Thank you.

MR. LAURENCE: Okay, I'm going to gather two more questions so that we have three. Yes.

MR. ILLIG: Fazil Illig, WPI. I'm wondering if our policies in the region is going to mirror our spectacular successes in Afghanistan? And to return to that brilliant formulation by the affirmation to ratition (?). It said everything happens twice in history. First time as a tragedy, second time as farce, which may as well have been said about Afghanistan.

And a good small example as how this is turning out, now we're selling \$60 billion worth of weapons to Saudi Arabia. \$60 billion worth of weapons to Saudi Arabia may be the last thing Saudi Arabia needs, and it's going to turn out to be very destructive and self-destructive.

MR. LAURENCE: This has to be the first time that Marx was cited approvingly twice in one session at Brookings. Please, can we get a microphone to Ruth?

MS. SANTINI: Ruth Santini, Brookings. I have a question to Tamara, and then three very short questions to Managing Director Mingarelli.

To Tamara, don't you think there is a problem -- a rising problem for U.S. foreign policy in the region of expectations capability gap? I mean, since the Cairo speech there have been rising expectations in the region. And they've been dashed until the Arab uprisings in terms of U.S. engagement for pro-democracy movements on a pragmatic basis, more engagement with the Middle East peace process, maybe less presence of military troops on the ground, et cetera.

Don't you think that this -- I mean, the Obama speeches in the past couple of months are just going to increase this expectations capability gap in the region?

To Director Mingarelli on the revised ENP, I see it as a step not really forward; it's a step -- the upgraded circle, the proposal to the European Parliament that has just come out. But I see three potential flaws in the revised approach. And I would really appreciate a comment on that.

The first possible flaw is -- you mentioned that we need a more cost-effective approach in our system in how we deal our assistance policies. I completely agree. But it's not just an intra-EU institution problem. It's mainly a challenge in terms of reaching vertical consistency between the EU and European member states. Is there any proposal concerning that? So, diminishing the divergences in how funds are used across member states in supporting democracy in the region?

The second point is linked to -- you mentioned differentiation. This is a long-standing claim of the European Neighborhood Policy. The real differentiation, though, is you mentioned at the beginning would be between the Mashreq and the Maghreb. So, subregional clusters within the ENP, which, obviously, need specific approaches. And they don't share much with the Eastern neighborhood. What is the kind of debate we are getting on this possible change of the ENP?

And the third and last point, you mentioned regional conflict. They remain there. They pose a huge problem to the consistency of our foreign policy. So, how are we thinking about linking -- for example, we should have done it since the very beginning in our action plans towards Israel or the Palestinian authority, the resolution of the Middle East peace process. Is there any chance we are thinking more strategically on linking the security that I mentioned in our democracy promotion policy?

MR. LAURENCE: I'm just going to reverse the order of respondents. Ana?

MS. PALACIO: Well, I will just pick up the -- in order to save time, this idea of conditionality. I think this is an extremely important aspect. And I personally, I favor conditionality.

I think that in part, the failure of the Barcelona Process and part of the failure of the Neighborhood Policy -- because it's true that the European Union has spent a lot of money in the region -- is that there was no conditionality whatsoever at all or little conditionality or the conditionality was watered down progressively, and especially the conditionality in terms of reforms, because there was other aspects of conditionality that were present and that were benchmarked and that worked better. And this is why in countries like, for instance, Morocco, when you have a reasonable legal security in economic terms -- I won't speak about freedom of the press or other areas, but in this area of economy, yes, you have.

I think that we have to go back to the Barcelona Declaration and just establish the conditionality with reforms; intelligent, feasible, realistic, but establish the conditionality.

MS. WITTES: Okay. I'll try and take each of these in turn quickly. First on Syria -- and Rafi, I know you attended the panel I was on about Syria yesterday. So perhaps I'm repeating this more for the benefit of others in the room than for you. But in

case there's any lack of clarity in terms of our policy on Syria, I think what you heard from the President last week is a determination on our part to support the aspirations of the Syrian people. And their aspirations are clear: they want to transition to democracy.

So, the President's words to the Syrian government were that what we want to see is to see that government end violence, respect the rights of its citizens, release detainees, and, very specifically to President Assad, either to lead a transition to democracy or to get out of the way for that process to move forward. I think that's pretty clear.

The question of engagement with different kinds of organizations and what criteria do we use and do we have favorites? I think the first thing that's very important to say is that our interests -- and I think that this is something on which we would very much agree. Our interest is in seeing a credible and open democratic process. And we're concerned about the integrity of the process and the credibility of the process much more than about seeing any specific outcomes. That's a very important point.

And I think really, across the board, we -- our approach is conditioned on the fact that what's happening in the region is driven by people in the region. It's not driven by us and we have to be respectful of that.

That said, I think it's important to recognize that there are a set of criteria that are necessary for any political actor, no matter what their ideological or ethnic or religious coloring might be if you want to play a constructive role in a democratic process. And again, these are criteria that the President laid out in Cairo in June of 2009: that you have to be committed to nonviolence; that you have to respect equality under the law, including for women and minorities; and that you have to respect the democratic rules of the game after an election as well as before. And that's something that applies across the board.

Our view is that if you have good institutions -- as Ana said, if you have good rules in place and an open political marketplace where actors who embrace those core criteria for the democratic process are engaged, that you're going to see people able to have a good debate about who's going to meet the needs and aspirations of citizens. And you will see a quality election and a quality outcome.

There was a question raised about expectations following the Cairo speech, and U.S. policy. And I really have to say -- I mean, number one, again. What's going on in the region is really not about the United States. It's really about the citizens of the region themselves. And I think we have to keep our eye on the fact that their judgment about whether things are going well or badly is not primarily about how they feel about our policy. So, we may be very focused on our policy, but let's not make the mistake of seeing everything in the region through that lens.

That said, I think that we've done a tremendous amount of work to deliver on the expectations that the President laid out in Cairo, whether it's regarding our military posture in the region and the fact that we're on track to complete our drawdown of military forces from Iraq, as agreed, by the end of the year. The fact that in terms of support for democracy we have increased substantially in the last two years our support, for example, Egyptian civil society organizations. And as I said earlier, I think that that expanded engagement and expanded support for civil society across the region has been a really core feature of the work that we've done over the last couple of years.

And on the Middle East peace process as well, this is an issue that this President and his envoy have worked literally every day since they've come into office. There's no question it's a tough issue. If it weren't a tough issue, it would have been resolved a long time ago. And unfortunately, it's also not an issue that relies merely on the political will of the United States. In fact, it relies primarily on the will of the parties on the ground.

But because of that, it's our firm belief that we're not going to get anywhere until those parties sit down and negotiate the issue directly. And that's what we've been working to do. It's not going to happen because we impose it on them.

MR. LAURENCE: Mr. Mingarelli?

MR. MINGARELLI: Everybody will agree with you when you say that regional integration is of the essence. And I think that the EU has been working on that for years now.

There is a free trade agreement between four countries of North Africa: Egypt, Jordan, Tunisia, and Morocco. This is the Agadir Agreement -- that has been instrumental in bringing about this Agadir Agreement. But we should do far more than that.

We have spent weeks talking about the secretary general of (French), the former Tunisian foreign minister. And they are perfectly aware of the fact that as I said, the non-Maghreb has a huge cost for the population of Tunisia, Morocco, Algeria.

But we should do far more and, you are right, we should probably apply some kind of conditionality. And there is no doubt about the fact that the EU could be serious about conditions, because simply we are the first trade block. And we have levers, many levers, but there is a question of political will.

The flows in our new approach need to have more coherence between what the EU institution and what the EU member states do. You are totally right. And by the way, in the communication we say as well that we should ensure that our member states feel bound by this European Neighborhood Policy. Because you are right, this Neighborhood Policy has been, up to now, something which has been promoted by the EU institution, while the EU member states have continued to develop their own national bilateral policies. So we have to make progress on this account.

Differentiation East and South. Well, for the first time in a paper written

on our Eastern neighbors, there is an explicit reference to Article 49 of the Lisbon Treaty, which said, basically, that any country on the European Continent, provided it complies with a number of conditions related to rule of law and democracy, can apply to the EU. This is clearly to show that for some of our neighbors, there is a prospect to apply to the EU. For others, for the time being, there is no such prospect.

And as regards to regional conflict, we have already answered. I think it's clear that for many of our neighbors, the existing regional conflicts are a real obstacle to democratic and economic reform. This is true, as I said, for countries like Tunisia and Algeria, because they cannot develop their trade as long as the border is closed. But this is true as well in Moldova, in Georgia, or in Armenia and Azerbaijan.

So, we have to be more involved in the solution to these regional conflicts. And the EU is better placed than many other actors to play a key role in these conflicts.

MR. LAURENCE: Mr. Mingarelli, it sounds like you probably have enough on your plate with the rather Herculean task of herding 27 member states into a single policy front. But thinking about the transatlantic relationship, is there anything that you'd like to see happen on the American side that hasn't been happening? Or anything that your transatlantic partner has been doing that you wish it wouldn't?

MR. MINGARELLI: Well, over the last years I must say that we have seen a real improvement in the way we work in these countries. And we are in constant contact on the ground and in the capitols with our American partners to make sure that basically we have the same policy objectives. And we called on as much as we can -- we coordinate as much as we can our instruments.

I don't say that there is no room for improvement. There is, without any doubt. But we cannot say that we do not exchange views. And it's clear, once again, that over the last three to four years there has been a marked improvement in this regard.

MR. LAURENCE: Tami, what are those areas where there's room for improvement?

MS. WITTES: No, I think we have very regular coordination at -- across the capitals, as well as in each of the countries in the region, both in terms of donor coordination, which is important, and diplomatic coordination.

I think donor coordination is probably the hardest area, because things move quickly on the ground. We each have our own mechanisms, and so it's often a challenge to make sure that we're using funds effectively and we're not duplicating, and so on. But you know, in Tunisia for example -- I think we've learned some lessons here. So in Tunisia, within weeks after the revolution we had established a donor coordination group on the ground that's meeting, I think, every other week at this point. And given that the U.S. and the EU are the two donors who are doing the most to support the electoral process, both the technical side and the political development side, it's absolutely crucial that we do that well. So, I think that's an area where we can probably do even more.

On the policy side, I think we've done a lot to work closely over the last year. I mean, I'm just thinking back to the period running up to Egypt's extremely flawed parliamentary elections last fall where we had a lot of back and forth as events were developing about how we were each engaging with the government of Egypt about our public stance. And I think that that was very important in having greater impact jointly.

MR. LAURENCE: Thank you both for your candor.

I'm going to gather the next set of questions. First is this gentleman in the front.

MR. MABROUK: Thank you. Asadin Mabrouk, World Bank retiree.

I hear a lot about regional integration. However, it seems to me that it's still the traditional way of seeing regional integration that is the MENA region versus Europe or the MENA region and the U.S.

But there is another regional integration that is really missing and lacking, and which will make a real difference mainly post-revolution. That's the integration between -- economic integration between the MENA countries as a whole. The trade between the MENA countries is so low. There's a kind of 2 percent only trade between the different MENA countries.

Ms. Palacio said, well we should promote market economy, and what have you, and emphasize this. I would think it's probably a waste of time because the idea of market economy is well sold within the MENA countries. Historically, geologically, religiously. I don't think you need to sell market economy or even invest one penny on promoting market economy. They all think about market economy. It's true, they are emerging political countries in -- political parties with the heading of Communism and Socialism and what have you.

First of all, if we are to promote democracy in this region, I think let them talk about communism and what have you. Why not? But the region, in essence, is market-oriented.

And I would think the best policy that Europe and the U.S. and other partners could do is to promote an economic integration between the MENA countries. And I think that would have a real positive outcome, even for the traditional European integration. And that is -- I think we need to promote south-to-south cooperation rather than always north-to-south cooperation.

And I think we should have a vision. Europe should espouse a vision, as well as the U.S. for really pushing and naming that -- what you are trying to do is really to develop this regional integration between the Arab countries. And investment does not that --

MR. LAURENCE: I'm sorry, I'm going to have to cut you off. Our panelists have to leave --

MR. MABROUK: Just one thing, because these frozen issues like the Sahara, with regional integration between the MENA countries, that issue will just disappear by itself.

MR. LAURENCE: Thank you. I'm going to give our panelists to respond, since I know that Madam Palacio has to leave. And I just want to ask one quick question about the refugee issue, whether or not balancing a fair asylum policy in Europe is consistent with the desire to ensure a viable and secure environment at home in these countries of origin.

But please, a concluding remark.

MS. PALACIO: Well, you are speaking about immigration at large? Or refugees?

MR. LAURENCE: Refugees.

MS. PALACIO: Refugees. Well, you know, the issue right now is how to address the question of refugees. And who is a refugee and who is an economic immigrant?

And you know what? If we get into these waters, it's extremely complicated. Right now, it's difficult to claim for immigrants -- for citizens that come from Tunisia that they have -- that they qualify under any of the Geneva conventions. It's very difficult to justify.

So, what kind of refugees are we speaking about? The thing is that, of course, because of our immigration -- and I fully agree with Mr. Mingarelli that one of the main added values of this new version of the Neighborhood Policy is that it addresses, frontally -- I hope it will be implemented now because it addresses the paper frontally this issue of immigration, that we have to -- we cannot just -- I mean, because if not we are confronted people that, legitimately, try to circumvent all these hurdles by just going through the -- just one comment on what you said.

Absolutely, integration. Physical integration, I said first because you need to vertebrate this integration. And, of course, economic integration. And I myself, I highlighted that all these economies are enclaves. That there is no trade between the region. And I think that you are absolutely right.

Honestly I disagree. Of course, as I said, this is brush strokes. But I'm not that sure that this idea of the benefits of the market economy is pervasive in the region. My impression is that it's not that pervasive. Yes, it is in certain strata of the society. It's not pervasive in all the society. But of course, we -- this is different perspectives.

MR. LAURENCE: Thank you. And we just have time for a concluding paragraph from each of you.

MS. WITTES: I'll just say very quickly on the trade issue. I don't think it's either/or. I really don't. I think that regional integration and integration with European and American markets are part -- should be part and parcel of the same process. And fundamentally, what we envision is something that is a high standards trade arrangement that -- you know. And so if you're working on the basis of common standards, then you can work all of those types of integrations simultaneously.

MR. MINGARELLI: There is no doubt that it is extremely important to boost south-to-south economic development and trade. This was, by the way, one of the main objectives of the Barcelona Declaration in 1995, to develop a free trade area in the south of the EU, not between the EU and North Africa, but between the countries of Maghreb, Mashreq. And it has been repeated last week by President Obama, when he said that we should, at the same time, open our markets to the exports of these countries, but, at the same time, boost intra-regional trade. So it has been one of our constant objectives.

We have not been very effective in promoting it. But here comes a

problem of the conditionality. And it's another debate. But it's clear that it's not enough to put in a piece of paper that our intention is to develop or to boost. We have to take the necessary measures to make sure that it happens.

MR. LAURENCE: Well, thank you all for coming. And please join me in thanking our panel. (Applause)

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