

Teheran Speech – Mr. Böllhoff

Ladies and Gentleman,

Thank you for inviting me to speak to you today. At first, I have to apologize. My speech will be in English.

The current German finance minister, Wolfgang Schäuble, joked once: “Badly spoken English is however the most spoken language in the world.”

I would like to start with a brief overview of who Prognos is.

Prognos is an independent think-tank with a strong focus on macroeconomic analysis and megatrends. It was founded in Basel, Switzerland, in 1959. Our timeline is in the future.

George B. Shaw coined once a wise quote: “Forecasts are difficult, especially if they deal with the future.”

Quite a challenge – but I will try to warm you up for this idea. Think for example of long lasting infrastructure projects and demographic challenge.

Ladies and Gentleman,

The really important things to focus on are the global megatrends. Arguably the most conspicuous and controversial megatrend of our time is globalization. Our projections clearly indicate that globalization processes will continue to exert their impact for many decades to come. We anticipate a tripling of merchandise exports to 32 trillion euros per year by 2040. One reason for this development is the increase in FDI and the ongoing internationalization of the value chains.

The challenges of Iran are not comparable with the situation in China in the 1970s. Iran does not start from such a low level as China did back then. Iran starts again after a long period of stagnation.

The FDI stock of Iran amount 43 billion US Dollar in 2014. That's more than in Pakistan. A country whose population is twice as large as Iran's. In the last twenty years the s FDI stock in developing countries has multiplied more than tenfold. In India the FDI stock increased by a factor of fifty and in Russia by a factor of 100. In the rising developing economies the FDI inflows amount to six to ten percent of the gross fixed capital formation over the last ten years. In Iran just two till three percent.

Let us now take a look at the second megatrend: demographic change. While the headlines have long been dominated by aspects of globalization, the demographic change crept up on us quietly and largely unnoticed. And it is having an enormous impact – starting with a decreasing birth rate, what you call the baby bust, and a steadily increasing life expectancy. Globally, we can say that the world's population is still growing; but the whole world aging. But this varies tremendously from country to country. Iran is an example for that.

The third megatrend, digitalization, is both the most significant and the most underestimated trend. Information and communication technology is no longer just a technology industry. It has penetrated into all sectors of the economy, for example also in the areas of banking and financial services.

I will give you two examples:

1. Foreign bank transfer in developing countries are really difficult and expensive. Western Unions takes for a bank transfer from Germany to Iraq a transfer fee of 10 percent. Paypal or TransferWise will handle this for one-tenth of this cost.
2. Nutmeg, a British wealth management company, offers his clients a “robo advisor”. This robot provides algorithm-based portfolio management advice without the use of human financial advisers. They just ask customers some questions to create a portfolio based on their answers, and then use algorithms to keep to that allocation.

I could continue to give you further examples for a long period, but my time is limited. But let me make clear on crucial aspect: The digital transformation does not mean that banking services will disappear. They will just be transformed. Corporate and investment banking will be necessary in the future, too. The economic functions of credit institutions are still required. But the digitalization can and will restructure the process – and make it more efficient.

Digitalization has a disruptive character on the economy. Business models are challenged by the digitalization, job profiles and activities are changed, and business process are destroyed and reassembled from scratch.

Digitalization is a game changer, an occurrence that completely reshuffles the cards. That's a threat, but that's also a huge opportunity. If you have to implement new process and instruments after lifting the sanction, you may have the unique possibility to interlock this with a higher digitalization.

Ladies and Gentleman,

To be able to deduce recommendations and courses of action from trends, it is necessary to map these trends in long-term forecasts.

At Prognos we have been compiling long-term forecasts for more than 50 years now.

Long-term forecasts distance themselves from current events to constitute well-grounded guidelines for the future. Well-grounded means that we let the numbers talk, rather than allow ourselves to be influenced by individual opinions and breaking news. Many people measure the world based on media reports. But it's necessary to measure it on the basis of economic impact. In order to have a reliable tool for strategic planning.

Now, I would like to present some of the results we obtained in our reports.

In the period up to 2040 we expect to see an average annual real growth rate of 2.1 percent in the United States. Private consumption will continue to be the main driver of growth. Although public debt, a legacy from the financial crisis, will increase in absolute terms, over time it will become less perceptible with increasing economic performance. By 2040 the United States will be contributing about 23 percent to overall global growth. According to our calculations, in 2040 the gross domestic product of the United States will still be the highest in the world.

Now to Europe: Following the launch of the euro in 1999, the euro zone experienced a decrease in international competitiveness caused by fast rising labor costs in conjunction with a sharp increase in the debt ratio. Serious economic fault lines could be observed. But the European patient is on the way to recovery. By 2040, Europe, and now I mean the European Union, will account for 17 percent of global growth. European gross domestic product will be slightly higher than China's. The growth rate of 1.7 percent will be overall weaker than in the United States.

In Germany the retirement of the baby boomer generation will result in a considerable slow-down of the growth rate. Overall, by 2040 we expect economic growth of around 1.3 percent per employee. For comparison, US growth per employee will be weaker at around 1 percent per annum. International trade will continue to play a vital role, the importance of industry will remain high at more than 25 percent of gross value added.

Ladies and gentlemen

I'm always being asked: "What will happen with China?" China will continue to grow, but the growth rate will slow down or, better said, normalize.

"China used more cement between 2011 and 2013 than the U.S. used in the entire 20th century. All of America's cement consumption during the century adds up to around 4.4 gigatons. In comparison, China used around 6.4 gigatons of cement in the three years of 2011, 2012 and 2013."

In the past China drew the commodity market like a vacuum cleaner.

I hope you will agree that in view of cement consumption in this dimension, the term normalization of the growth rate is more preferable than slowdown. The income of the Chinese people will more than triple, but it will be still less than a quarter of Americans' by 2040.

Ladies and Gentleman

Let us leave China and return to the Iran.

At first, I would like to say: I am surprised. I am surprised about the good state of your economy. After years of sanction, after years of isolation from the international capital markets comparable with a low oil price I expected a worse picture. But the macros for Iran are not looking so bad. The GDP per capita is higher than in Tunisia. The government fiscal balance is small and the total government gross debt is with 15 percent on a very low level. I am convinced that Iran can catch up the backlog by the FDI with a clever approach within a decade.

Of course, it is a challenge to create jobs and generate wealth for millions of young people. But it isn't impossible. It's not the time for sadness and desperation. Europe after 1945 is a good example for an economic improvement and recovery. The German economic miracle and the French Les Trente Glorieuses, "The Glorious Thirty", are the evidence.

If Iran manages these challenges and transformations successfully, it will become a model for countries with similar challenges and macroeconomic fundamentals – from the Maghreb region over the Levant to Kashmir.

I would like to give you some ideas for the further steps.

Please do not concentrate your investments in the oil, gas and mining industry. Commodity prices are volatile. The employment effect in this industries are small. Enhance your value chain. Claim a significant share in the manufacturing sector.

The industrial core has several advantages:

- Enterprises from the manufacturing sector are generally more export-oriented. A greater customer diversification also means a better macroeconomic risk diversification.
- In addition, a high dependence on exports exerts pressure on export-oriented producers to modernize and adapt. Exports and innovations are mutually stimulating.
- Moreover, domestic industry increases the demand for inputs.
- The manufacturing sectors create jobs with a high level of productivity and attractive salary.
- The manufacturing industries are the basis to advance your skill into other product lines.

Iran has a manufacturing basis. Modernize it. Start partnerships with foreign companies and use the possibilities of knowledge transfer.

Ladies and Gentleman

At the end I would like to say some sentences about the banking sector. The banking sector is a key driver for the economy. They have the potential to strengthen – but also to weaken – the economy.

The distribution of the benefits between commercial banking and investment banking depends on your decision, which model you prefer. I'm not a banking expert, but the financial meltdown shows that systems that are based on smaller leverages are less risky. Equity has a higher loss absorbance.

A great responsibility comes to the Central Bank of Iran. After the lifting of sanctions a lot of capital will flow into your country. But this constellation also can lay the seeds for a new crisis. To avoid this you have to steer the process.

First: Capital inflow should come into the country as FDI, not as foreign currency loans. Implement instruments to reduce the amount of foreign currency loans. A higher minimum reserve for foreign currency loans could be an option.

Second: Capital inflows could compromise competitiveness, because your currency can revalue. To interrupt this process you could transfer money into your sovereign wealth fund or the central bank. Invest these money, buy assets and securities.

And third: KYR – know your risk. Do not allow shadow banks to operate outside of your supervisory.

Ladies and Gentleman,

I believe in the potential of the Iranian economy. If you improve the framework of doing business, if you continue to embrace entrepreneurial risks and if you build a diversified economy, a promising future should lie ahead of Iran's economy.

Your national football team is on good way. They allocate the first place in the qualification group for the world championship in 2018. I'm convinced that we will meet us there.

Thank you for your attention.

Merci. Khodahafez.