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The American Century

By Leo Melamed

If one had to pinpoint the birth of globalization, a good bet would be Aug. 15, 1971, when President Richard Nixon dropped the U.S. dollar's convertibility to gold. This led to an irreversible breakdown of fixed exchange rates, initiated the modern era of globalization, and provided the rationale for the launch of financial futures by the Chicago Mercantile Exchange (CME).

As the world left the gold standard in favor of the information standard, the U.S. had the so-called "first mover advantage." For the next three decades we dominated the world's capital markets, dwarfing everyone. With derivatives, the CME, Chicago Board of Trade and New York Mercantile Exchange initiated the modern futures era. In over-the-counter, financial engineers created a vast array of financial instruments. In securities, Chicago Board Options Exchange stock options were born, and the New York Stock Exchange, Nasdaq, as well as other American exchanges grew without equal—deeper and more liquid than anywhere else.

Merton Miller, Nobel Laureate in economics, liked to say the period between the mid-1960s and mid-1980s was unique. In his view, no other 20-year period in recorded American history witnessed even a tenth of the financial innovation of those two decades. But time marched on. Suddenly, American first mover advantage was over. The growth track the U.S. maintained in the decades after the onset of globalization has been steadily leveling off, while the growth track of other industrial nations has ramped up. The U.S., its commercial

enterprises and its exchanges are facing serious competition from other capital markets.

Recently three major studies, one led by Glenn Hubbard and John Thornton, another by Sen. Charles Schumer and Mayor Michael Bloomberg and the third by the U.S. Chamber of Commerce and Treasury Secretary Henry Paulson, have concluded that America is losing its dominance in world securities markets.

We have what it takes to compete with India and China.

These studies were a wake-up call. But reducing the Sarbanes-Oxley regulatory requirements, as these studies suggested, while a good idea, will by itself not alter the dynamic. Nor will we fix the problem with populist demagoguery advocating a protectionist agenda. "America First" solutions have been tried before and are self-defeating. In today's globalized marketplace, such remedies would be devastating to both U.S. capital markets and the American standard of living.

To find a solution one must first recognize the cause of the problem. We have entered a new era in the global marketplace. The industrial world has caught up with us. It has learned the value of Milton Friedman's free-market precepts, adopted them and put them to work. All major capital markets have modern trading capabilities, competent securities and derivatives exchanges, cutting-edge technology and banks that are as solid as our own. We are beginning

to feel the competitive pinch from the Asian giants China and India. Within a decade their competitive presence will be felt in every segment of the marketplace. Needless to say, we were excellent teachers and our students learned well.

To remain competitive in the 21st century, the U.S. must first accept the reality of the modern global paradigm. We cannot pretend or assume that things will ever again be as they were. In the future, our private sector will have to fight for business flows on a world stage. It will require our best efforts and brightest minds. Similarly, U.S. government officials must accept the fact that U.S. businesses face competitors from across the ocean rather than across the river.

The old road map is history. The new map necessitates continued deregulation to promote continued innovation, reduction of burdensome compliance costs, containment of baseless litigation and open markets for goods. Beyond that, we must redouble our efforts to sustain the academic excellence that helped give us our first-mover advantage in the first place.

The fruit of our labor resulting from a three-decade, first-mover advantage is a priceless intellectual legacy—a unique reservoir of knowledge, ideas and experience that can become an arsenal of competitive weaponry for the future. This, coupled with the constitutional and cultural birthright that encourages Americans to think freely, experiment and create, gives us an endowment of extraordinary potency.

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