

Dr. Alberto Desirelli

Alberto.Desirelli@gmail.com

Dr. Marc Faber

Marc Faber Limited
Suite 3311-3313, Two International
Finance Centre
8 Finance Street, Central
Hong Kong

Geneva 14 March 2010

Dear Dr. Faber

I would like to convey to you some information "from the field" concerning what you mentioned at page 4 in your March 2010 Monthly Market Commentary (The Failure of Economic Interventionism May Move Markets Higher!) where you say:

" Above, I mentioned that along with the shift of industrial production and capital spending to Asia a massive transfer of technology occurred. I am mentioning this because until this very day some Westerners are in their arrogance under the impression that European and American companies will innovate, invent, and excel at research and development (R&D), and so enjoy the benefits of high margin while Asian companies will employ miserably paid workers who will assemble goods in sweatshops and, therefore, only achieve low profit margins. But because R&D is far less expensive in Asia than in the West, more and more Western companies have set up research facilities in Asia (notably in China and India) with the result that there are today more people employed in Asia in research than in the West (see Figure 4)."

I could not agree more with you, and there is much more to all this.

I am a scientist by training. I have worked in academia in Milan, as an art dealer in London and as a scientist in different countries on international R&D and scientific projects for the past twenty years. What I am writing below is drawn from direct experience and observations. I am currently living in Geneva.

Before giving my arguments below, I have to warn that I am neither a moralist nor an indoctrinated lefty any sorts. My standpoint is very practical.

Yours Sincerely

Alberto Desirelli

Hamam and with a banker

Some months ago I was in the hamam with a friend/gym buddy of mine who works for one of the big Swiss banks. In the steam room we usually talk about life or ex/current girlfriends. This time he was complaining about the difficult situation in the banking sector and the fact that bonuses would be low.

I told him that the positive thing was that at least he had chosen a profession – banking – where one does get, in general, good salaries and bonuses. I told him that I have friends with 20 years of experience, who are in R&D, at the top of their field, successfully designing things, which nobody on the planet ever managed to conceive and build, who are on a GBP 50,000 salary and get a GBP1000 bonus when they are lucky.

His answer was that probably these people are in a business that is not as profitable as banking. He also explained to me that the banking sector must offer high salaries and bonuses in order to attract the best talents.

I have many friends who work in banking and they all have the same arguments and their arguments always get me thinking.

Then again one cannot but wonder whether the talents attracted to banking are of the right type. From what one gets from the reports of the testimony before the Financial Crisis Inquiry Commission in Washington DC one gets the impression that these high levels of compensations have been attracting talented comedians.

Anyway from there we went on to dinner.

Dinner with a banker

At the risk of passing for some sort of fanatic in Churchill's sense - A fanatic is someone who can't change his mind and won't change the subject - during dinner I tackled the issue again.

The attract-the-best-talent argument always makes me wonder – I told him - why a society must be so skewed as to want to attract the best talents in one or two fields and not to care about the talents flowing to other fields. To be clearer in the case at hand, not to care about the talents flowing to other more fundamental fields for society¹. Just to give one single example - I said - our knowledge in the field of medicine is mediaeval, as it should be apparent for anybody who has ever needed the services of the medical profession. I stopped short of telling him how will the average banker feel about the best talents being attracted to banking the day he lies in a hospital bed knowing he does not stand much of a chance as he is being looked after by scarcely talented doctors. After all we were having a nice dinner, his eyes were glazing over and Churchill would have disapproved of my fanaticism, so we went on taking about skiing – we both live in Geneva and in Geneva in winter one talks about skiing, it's a non-optional social convention.

As we were moving on to the dessert I picked the issue up again though. Now on the argument that banking is just a more profitable business than others and so it can afford to pay large salaries and bonuses. Well it is indeed the most profitable

¹ A few memories come to mind: a friend of mine was working at top university in London doing research on AIDS. The lady in question with a PhD was on a GBP 20,000 salary when she decided to drop it all join a corporation. At the same time one of my ex students aged 25, with no previous experience in finance, got a GBP 40,000 job in the City, and after one year, a GBP 20,000 bonus.

business of all - I told him. When I go visit my banker in Geneva I am always amazed by the pink marble in the lift. I like it, but I always invariably and automatically think that I am obviously being charged too much. My friend was nodding in agreement. However, the banking sector cannot be the motor of the world economy, banking is and should always be a service, which should help the development of businesses. To be more specific with no underpaid scientists and engineers who can produce affordable objects, there would not be any economy and there would not be any business on which the banking sector could thrive. In other words, if the iPhone were designed and produced by bankers it would be an item that very few people would be able to afford.

So being banking the last link of the wealth chain it can “pick up the slack” and rake in what all the other actors of the wealth chain have saved. Of course – I told him – we all know why this is. It is the power of capital, which controls the whole process.

Feeling a bit guilty for having grilled him and sympathetic for the low bonus situation I picked up the bill.

The depletion of talents from other fields

I have no problem per-se with bankers being overly well paid and to be sure I would love to be working in banking. However, despite my sympathy for bankers, this situation is causing a depletion of talents in other fields, which in turn could cause a decline of power of the western world. We see this in some countries more than in others². This will not happen overnight of course, and maybe it will not happen at all if somehow things get corrected, but the process is highly non-linear, so the effects on society could be sudden and surprise our political leaders - another profession which does not seem to be attracting the best talents.

Of course society is well aware of this. I see posters in the tube in London, when I go there, saying science is cool and encouraging teenagers to chose a technical or scientific career. There is a multitude of TV and radio programs aimed at drawing teenagers to science and technology. I find it fairly amusing when people discuss, in these programs, what the reasons might be for this decrease in interest for technical or scientific careers. The reasons are very simple.

Reason # 1: money. We do not seem to be needing TV programs on banking or corporate law to encourage people to go into those careers. A disparity in compensation between these more lucrative and other fields has always existed. Within certain limits this is well tolerated by the system. However this effect has become more and more apparent over the past 30 years with the gradual erosion of the wealth of the middle class. We have gone beyond the threshold the system can absorb without some equally apparent adjustments.

Reasons # 2: social prestige. In different societies a scientific or technical career is perceived differently. In most of the developed world, and especially in the Anglo-Saxon world a technical or scientific career is seen with some dose of contempt. “You will always be able to replace an engineer with another one who will do the same job with lower salary” is a phrase I have heard repeatedly in that part of the world. So in the end reason # 2 coincides with reason # 1.

² In Europe the UK is an example of a country where this process is so advanced that entire science departments of universities have to close business as there are not enough students.

By the way, it is not only banking

Let us face it. It is not only banking. It is also the way corporations are structured in general. Even within corporations based on technological innovation or science, the people who are actually developing those products, which might give the company an edge, are underpaid compared even with their own colleagues who do marketing or management in the same company. I know some very successful R&D scientist who went into marketing out of frustration for their inadequate salaries. To get to their level of expertise one would probably have a PhD and 10 years experience after that. Dropping out and moving into a field where one's competences are lost represents an amazing drag for the economic development of our society taking into account the cost of developing those cutting edge competences.

The annihilation of the middle class

It is always bad per-se to oppress a part of society. However the annihilation of the middle class, which is underway, is especially dangerous for our society. The middle class is in fact the class that produces those competences that have been so important in the development of wealth and social stability in the western world. Western society is killing the goose that laid the golden eggs. This is leading to several pernicious effects already well visible. One to which I am exposed frequently is the state of the industry in the developed world.

The state of the industry in the developed world

Most stock analysts live in fantasy world and rarely see below the surface. In the same way rating agencies failed to see the impending disaster of the credit crisis and were maintaining that everything was under control, many stock analysts miss the real issues in high tech companies. In many of these companies people are demotivated and productivity is low beyond belief. In those companies with international operations you might get different answers to the same technical question asked in Europe ("we can't do it, it's impossible"), the US ("we can't do it, it's impossible") or China ("we'll do it, it's ready tomorrow"). These are the same western high tech giants which shaped the technological revolution of the past 30 years and which indeed produced amazing R&D in the past. Now they are resting on their laurels, they have shortsighted policies, which will gradually decrease their competitive advantage and ultimately drive the value of these businesses down. Of course more often than not their CEO's have just a very vague understanding of the business of the companies they run and no vision. They do have, however, shiny mass-produced MBA's from Ivy League schools. In those companies R&D as we knew it is dead.

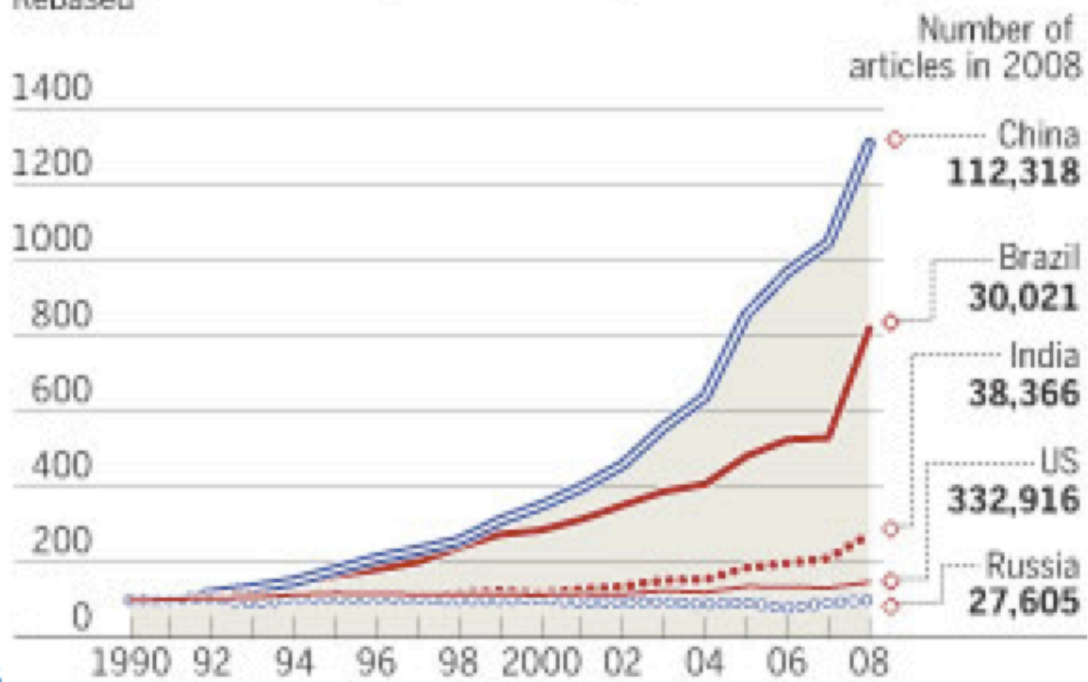
China

The shortsightedness of the developed world seems to be contrasted by China. In a recent speech the Chinese Premier Wen Jiabao said that he wants Chinese firms to improve their ability to innovate, producing high-tech and high-quality products (Source BBC: <http://news.bbc.co.uk/2/hi/asia-pacific/8550930.stm>).

Not surprising, after all most Chinese leaders have a scientific or a technical background, they also seem to have the vision ours seem to have lost. The figure below gives a snapshot of the situation regarding scientific research in the world. (Source: FT January 25 2010: "China scientists lead world in research growth" By Clive Cookson)

Growth of articles published in peer-reviewed journals

Rebased



Sources: Thomson Reuters; Web Science Database