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Recoil

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Politics this week

May 29th 2008
From The Economist print edition

Israel's prime minister, Ehud Olmert, came under pressure to resign after more revelations of payments made to him when he was mayor of Jerusalem (and a minister) by an American businessman, Morris Talansky. See article

Iran's parliament elected Ali Larijani, a former nuclear negotiator, as its speaker. He is a critic and rival of President Mahmoud Ahmadinejad. But his first target was the International Atomic Energy Agency, which he lambasted for a new report that expressed concerns about Iran's nuclear programme. See article

Following a peace deal brokered in Qatar, **Lebanon's** parliament elected General Michel Suleiman, a Christian, as its president. A new government of national unity is expected to be formed soon. See article

The **Japanese** government hosted 40 **African** leaders in Tokyo and pledged to double Japanese aid to the continent by 2012. Like China and India, which have recently hosted similar get-togethers, Japan wants more access to Africa's natural resources. See article

In **Somalia**, Islamist insurgents attacked an African Union peacekeepers' base in the capital, Mogadishu, killing at least 13 people, most of them civilians. The country remains virtually ungoverned.

Ethiopia's Supreme Court sentenced the country's former ruler, Mengistu Haile Mariam, to death in absentia. His Marxist regime, known as the Derg, presided over a proclaimed “red terror” after the fall of Emperor Haile Selassie in 1974. Mr Mengistu has lived in Zimbabwe since his own ousting from power in 1991.

A deadly month

Colombia's FARC guerrillas confirmed that their founding leader, Manuel Marulanda, died in late March—of a heart attack, they said. He was the third member of FARC's seven-man commanding secretariat to die that month. See article

AP

Canada's foreign minister, Maxime Bernier, resigned after his former girlfriend, Julie Couillard, revealed that he had left secret government documents at her home. Ms Couillard had previous ties to criminal biker gangs. The political demise of Mr Bernier, who is from Quebec, is a blow to the hopes of Stephen Harper, the Conservative prime minister, of gaining a parliamentary majority by winning seats in the province.

Argentina's farmers resumed a protest strike against an increase in export taxes. They will hold back grain exports and meat sales. See article

The Inter-American Development Bank said that higher **food prices** risked pushing 26m Latin Americans into extreme poverty. It launched a $500m credit line to boost anti-poverty programmes and agricultural productivity. Separately, Mexico's government said it would increase cash subsidies to 26m poor people to offset higher food prices.

To the (belated) rescue

Foreign aid-workers began to trickle into the cyclone-hit Irrawaddy delta after the ruler of **Myanmar**, General Than Shwe, promised the United Nations secretary-general that the country would let in aid-workers “regardless of nationality”. Separately, the military junta renewed the house arrest of the opposition leader, Aung San Suu Kyi.

Two large aftershocks hit **Sichuan** province in China, which was devastated by an earthquake three weeks ago; no deaths were reported. Meanwhile, officials raised concerns about the safety of so-called “quake-lakes” created by landslides that block rivers; plans were made to evacuate 1m people from Mianyang, a city downstream from one such lake.

Wu Po-hsiung, the chairman of **Taiwan's** ruling Kuomintang party, met **China's** president Hu Jintao during an official visit to Beijing. He was the highest-ranking figure from the island to visit China since the two split in 1949. The two sides agreed to resume bilateral talks that had been suspended for a decade.

AFP

A special assembly in **Nepal** voted by 560-4 to abolish the 239-year-old monarchy. The king was given 15 days to leave the palace. Bombs went off in Kathmandu, Nepal's capital, shortly before the assembly convened. See article

Brown left black and blue

Troubles mounted for **Britain's** prime minister, Gordon Brown, following the humiliating defeat of his Labour Party in a by-election in Crewe. Amid reports that he might capitulate to fuel-tax protesters, speculation grew about a leadership challenge. See article

London's new mayor, Boris Johnson, ended an arrangement with Venezuela's Hugo Chávez that provided the city with cheap fuel for buses. Mr Johnson's critics accused him of putting ideology above London's interests.

The Social Democrats upset their grand-coalition partners, the Christian Democrats, by nominating their own candidate to be **Germany's president**. Tensions within the coalition have increased as next year's federal election draws closer. See article

A UN report confirmed that Russia had shot down a **Georgian spy plane** over Abkhazia in April. Georgia called it an act of Russian aggression and demanded an apology.

At a meeting in Dublin, more than 100 countries agreed to ban the current generation of **cluster munitions**. America, Russia and China want to keep them.

McCain reaches out

John McCain made a big speech on nuclear security, in which he said America and Russia were no longer “mortal enemies” and called on Russia and China to help strengthen the world's non-proliferation regime. The presumptive Republican nominee made a point of stressing his commitment to multilateralism, a sharply different approach to that taken by George Bush.

Speculation about **vice-presidential** candidates was rife after Mr McCain met three hopefuls: Charlie Crist, the governor of Florida, Bobby Jindal, the governor of Louisiana, and Mitt Romney, Mr McCain's early rival. Other strong favourites are Tim Pawlenty, the governor of Minnesota, and Rob Portman, who is from Ohio and is a former director of the budget office at the White House.

The spacecraft *Phoenix* touched down on **Mars**, the first successful powered landing on the planet since the *Viking* missions in 1976. As scientists at NASA celebrated, *Phoenix* got on with its task of scouting for evidence of life on Mars. See article

EPA

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Business this week

May 29th 2008
From The Economist print edition

Arun Sarin said that he would step down as chief executive of **Vodafone**, the world's biggest mobile-phone operator by sales. During his five years in the job Mr Sarin endured rocky relations with shareholders, some of whom wanted him to sell the company's 45% stake in America's Verizon Wireless. But he also made important investments in emerging markets, including a controlling stake in Hutchison Essar, an Indian mobile operator. Mr Sarin's replacement is Vittorio Colao, who heads Vodafone's European business. See article

MTN, a mobile-phone operator based in South Africa, said it was talking to India's **Reliance Communications** about combining somehow. The talks were made public soon after the breakdown in merger negotiations between MTN and **Bharti Airtel**, Reliance's larger domestic rival.

Trouble in the boardroom

Privacy advocates in Germany voiced concern as allegations surfaced that the phone conversations of senior officials at **Deutsche Telekom** had been tracked, possibly at the behest of internal sources, in 2005 and 2006, around the time the company pushed through a controversial restructuring plan. René Obermann, Deutsche Telekom's boss, said he was "shaken to the core" by the revelations and turned the matter over to the authorities.

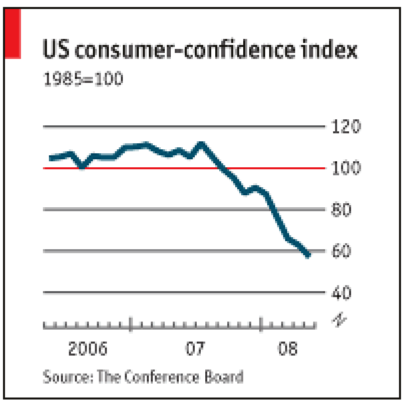
Société Générale held its general meeting, at which shareholders vented their anger about a rogue-trading scandal that has rocked the French bank. Earlier, an internal investigation found that SocGen had been slipshod in overseeing the activities of Jérôme Kerviel, the futures trader at the centre of the alleged fraud. See article

The first trial in connection with a big corruption case at **Siemens** got under way in Munich. Reinhardt Siekaczek, a manager in the company's telecoms unit, has admitted playing a part in what may be the biggest ever instance of corporate **bribery**, but insists he was working under the guidance of his superiors.

A proposal to split the jobs of chairman and chief executive at **Exxon Mobil** was defeated by shareholders. The resolution rose to prominence with the support of the Rockefeller family, descendants of the founder of Exxon's forerunner, Standard Oil.

Franco-American sentiments

American **consumer confidence** dropped to a 16-year low in May, according to one measure. Americans were not the only ones to register rising pessimism. High prices and worries about economic prospects also caused French consumer confidence to slide in May, to its lowest level since 1987, according to France's national statistics office. See article



There was more gloomy news in **housing markets**. Sales of newly built homes in America were down by 42% in April compared with a year earlier; home sales in Spain, another overheated housing market, fell by some 40% in March; and house prices in Britain dipped in May by 2.5%, compared with April, according to Nationwide—the largest ever monthly fall in its index. See article

The International Monetary Fund appointed **Olivier Blanchard** as its chief economist, following the departure of Simon Johnson. Mr Blanchard is a professor at the Massachusetts Institute of Technology and the author of numerous textbooks on macroeconomics. Separately, **Frederic Mishkin** tendered his resignation from the Federal Reserve's board of governors. A highly influential member of the board, Mr

Mishkin is returning to Columbia University.

In a decision that contravenes the spirit of a European court ruling last autumn, the German government approved a draft law that retains the ability of the state of Lower Saxony to block a takeover of **Volkswagen**. Lower Saxony is VW's second-biggest shareholder and is not happy with Porsche's intention to increase its holding in VW to a controlling stake.

Stella looks to Bud

Markets were rife with speculation that **InBev**, a brewer that includes Stella Artois and Becks among its brands, may launch a takeover for **Anheuser-Busch**, which produces the Budweiser range of beers. Consolidation among beermakers has picked up of late, but a bid for Anheuser could face stiff resistance from American politicians. The company's headquarters are in the swing state of Missouri; InBev is based in Belgium.

CKX, which owns and develops entertainment brands, agreed to a $1.2 billion management buy-out. CKX owns the rights to the name, image and likeness of Elvis Presley and of Muhammad Ali, as well as the format of the “Idol” television programmes, the American version of which recently ended with 97m people voting in the final.

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KAL's cartoon

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Illustration by Kevin Kallaugher

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Economist.com OPINION LEADERS

The oil price

Recoil

May 29th 2008
From The Economist print edition

Painful though it is, this oil shock will eventually spur huge change. Beware the hunt for scapegoats

IN THE early 1970s a fourfold rise in the price of oil almost brought the world to a standstill. The shock of the Arab embargo left a deep mark in many countries: America subjected its cars to fuel-efficiency standards, France embraced nuclear power—though sadly *shoene rukku*, or “energy-conscious fashion”, the inspiration for Japan's fetching short-sleeved business suit, was ahead of its time.

Thirty-five years on, oil prices have quadrupled again, briefly soaring to a peak of just over $135 a barrel. But, so far, this has been a slow-motion oil shock. If the Arab oil-weapon felt like a hammer-blow, this time stagnant oil output and growing emerging-market demand have squeezed the oil market like a vice. For almost five years a growing world shrugged it off. Only now is it recoiling in pain.

This week French fishermen clogged up the port of Dunkirk and British lorry-drivers choked roads into London and Cardiff. Nicolas Sarkozy, France's president, suggested subsidising the worst affected and curbing taxes on petrol; Britain's beleaguered government is being pressed to forgo its tax increases on motorists. In America falling house prices have left consumers resentful—and short of money. Congress and presidential candidates have been drafting schemes and gas-tax holidays like so many campaign leaflets.

Gordon Brown, Britain's prime minister, thinks the big oil producers can be persuaded to come to the rescue. But only Saudi Arabia shows any enthusiasm for that. Elsewhere, output is growing agonisingly slowly. That is causing hardship and recrimination. But it could also come to represent an opportunity. The slow-motion shock seems irresistible today, but in time it will give rise to an equally unstoppable and more positive slow-motion reaction (see article).

Action replay

It is clear that high oil prices are hurting many economies—especially in the rich world. Goldman Sachs reckons consumers are handing over $1.8 trillion a year to oil producers. The wage-price spiral of the 1970s has been avoided, but the income shock is painful. Beset by scarce credit, falling asset prices and costly food, developed-country households are hardly well-equipped to foot the oil bill. America's emergency tax rebate, voted this year to help people cope with the credit crunch, has in effect been taken right away again.

Stuck for answers, politicians have been looking for scapegoats. Top of the list are the speculators profiting from other people's hardship. Some $260 billion is invested in commodity funds, 20 times the level of 2003. Surely all that hot money has supercharged the demand for oil? But that is plain wrong. Such speculators do not own real oil. Every barrel they buy in the futures markets they sell back again before the contract ends. That may raise the price of “paper barrels”, but not of the black stuff refiners turn into petrol. It is true that high futures prices could lead someone to hoard oil today in the hope of a higher price tomorrow. But inventories are not especially full just now and there are few signs of hoarding.

If the speculators are not to blame, what about the oil companies, which have failed to increase output in spite of record profits? Profiteering, say some. However, that accusation doesn't stand up to much scrutiny either. The oil price is set in a market. For Shell, Exxon et al to hoard oil underground would be to leave billions of dollars of investment languishing unused. Others fear that oil is pricey because it is running out. But there is little evidence to support the doctrine of “peak oil” in its extreme form. The Middle East still seems to contain a sea of the stuff. Even if new finds elsewhere have been rarer and less accessible than in the past, vast quantities of oil could now be profitably stripped from tar sands and shale.

The truth is more prosaic. Finding and developing new oil fields is an expensive and time-consuming business. The giant new fields in the deep water off Brazil are unlikely to produce oil for a decade or more. Furthermore, oil is perverse. When prices are low, oil-rich countries welcome the low-cost, high-tech and well-capitalised oil firms. When prices are high, countries like Russia and Venezuela kick them out again. Likewise the engineers, survey ships and seismic rigs that oil firms need to find and produce new deposits are expensive right now. The costs of finding oil have, temporarily, doubled precisely because everybody wants to give them work.

Hope at the bottom of the barrel

So the oil shock will take time to abate. Some greens may welcome that, seeing three-figure oil as a way of limiting greenhouse emissions. Conservation will indeed increase. But everything high prices achieve could be done better by sensible carbon taxes. As well as curbing oil use, high prices have put tar sands in business which create far more carbon dioxide than conventional oil. Profits are going to ugly oil-fed regimes, not Western exchequers. And the wild unpredictability of prices will blunt the effect of dear oil on people's behaviour.

From this perspective, governments should speed up the adjustment—or at least stop delaying it. Half the world's people are sheltered from fuel prices by subsidies—which, perversely, have boosted demand and mostly benefited the better off. Now countries like Indonesia, Taiwan and Sri Lanka have begun to realise that they can ill afford this. Cutting fuel taxes in the rich world makes no sense either (see article). There are better ways to return cash to struggling voters.

The 1970s showed how demand and supply, inelastic in the short run, eventually give rise to conservation and new production. When all those new fields are on-stream, when the SUVs have been sold and the boilers replaced, the downcycle will take hold. By then the slow-motion oil shock could have catalysed momentous change. Right now motorists have no substitute for oil. But it is no coincidence that car companies are suddenly accelerating their plans to sell electric hybrids that are far cheaper to run than petrol or diesel cars at these prices. The first two oil shocks banished oil from power generation. How fitting if the third finished the job and began to free transport from oil's century-long monopoly.

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Economist.com OPINION LEADERS

Gordon Brown's travails

Picking fights

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Listening to voters has not done the prime minister much good. Leading them might

Reuters

DEFIED by his backbenchers, derided by the opposition and dismissed by most of the press, Gordon Brown must find it painful to stick his nose out of the door of Number 10 these days. Since his £2.7 billion ($5.4 billion) handout last month to blunt the impact on the poor of a misjudged tax change, he faces pressure from all sides to give way on other fronts.

Mr Brown's astonishing loss of form since the autumn has created a free-for-all at the heart of Labour. Some would tug him to the left in pursuit of the party's vanishing “core voters”. Others—more wisely from this newspaper's point of view—would have him cling more vigorously to the New Labour reform agenda that the Tories are trying to expropriate. Populist measures of any hue appeal powerfully to MPs whose seats suddenly look marginal after their party's stunning defeat in a northern by-election on May 22nd. And over it all wafts a whiff of sedition, as ambitious second-rankers assert their loyalty to the leader rather too loudly (see article).

Bobbing and weaving

It is too early to write off Mr Brown. Other prime ministers have slogged through diabolical mid-term elections to eventual success; and a general election need not be called until May 2010. But if he is to have a chance of governing effectively at least until then, Mr Brown must change tack. He claimed not long ago that his job was to “listen and lead”, but the two are not the same. He needs to figure out when to listen and when to lead.

That is less easy than it sounds, for Mr Brown is in a quandary. The man who liked to be known as the Iron Chancellor has come to be seen as weak; the idealist who championed social justice seems out of touch with the concerns of ordinary voters. If he makes further concessions, his government risks losing authority. Yet if he clings to bad policy for the sake of looking leader-like, he risks being ditched by his party. Where should he bull ahead, and where concede gracefully?

Two sets of U-turns are now mooted: he should avoid one and make the other. The first involves motoring. The duty on fuel is due to rise in October, and higher road taxes will hit dirtier cars in 2009. Queues of protesting lorry-drivers and hate-mail from constituents have persuaded many MPs to insist that the fuel-tax rise be dropped or postponed and the higher road tax at least confined to new cars. Households, they argue, already face sticker shock on fuel, food and more; and it goes against the grain to tax anything retrospectively.

But there are also powerful reasons to hold the line. Even if you think Britons are over-taxed (and, thanks in part to Mr Brown, they are), this particular tax is hardly the worst one on offer. Fuel tax is lower in real terms than it was in 2000. People should be nudged towards energy-efficient cars: global warming has not vanished just because oil prices have shot up. And the budgetary consequences of surrender could be dire: give way on this, and you leave the impression that the government can be leaned on by all and sundry.

By contrast, Mr Brown should jettison his insistence on increasing the time for which terrorist suspects may be held without charge from 28 to 42 days. This is an extraordinary breach of habeas corpus, for which no hard justification has been produced. Britain's police already have longer than most to assemble a case, and an impressive array of those who should know oppose the extension (see article). Worst of all, the government's current position reeks of politics, not principle: it was designed mainly to position Mr Brown to the populist right of the Tories as tougher on terrorism. That was the wrong sort of listening in the first place.

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Corporate governance in Japan

Bring it on

May 29th 2008
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A few signs of progress in Japan; but it must let young workers compete with older ones

Illustration by David Simonds

JAPAN has always wavered between being open and closed. As late as the 1850s foreigners were technically forbidden from setting foot on its soil. Today that sentiment lingers in the way that the country's politicians and companies resist activist shareholders and dealmakers. On May 29th Steel Partners, an American investor, successfully ousted the boss and six directors of Aderans, a wigmaker—a big victory for shareholders. More often though, Fortress Japan survives: the Children's Investment Fund (TCI), a British activist investor, has just failed to boost its 9.9% stake in J-Power, an electric utility.

In fact it is worse than that. Japanese companies are not so much wary of foreigners as they are closed to outsiders of any stripe. Assertive Japanese investors have also been beaten back. Companies sheltered from demands to improve performance have slid into some bad old habits. In the past couple of years they have renewed their cross-shareholdings and built takeover defences, which protect them from outsiders. Corporate governance is weak. Companies look to the stockmarket for prestige rather than capital. Noisy shareholders are seen as a nuisance. Independent outside directors are rarities. Hostile takeovers are unheard of. Foreigners may complain most loudly about the isolation of Japanese companies, but everyone, especially the Japanese public, is a victim.

The hope now is that the cost of all this is beginning to sink in. Two influential committees, appointed by the prime minister's office, have issued a package of structural reforms that serves as a rebuke to parochial bureaucrats and business leaders. It calls for low corporate taxes and a simpler system to attract foreign direct investment. It recommends breaking the $1.5 trillion public pension fund into several “baby” funds to be separately managed by professional investors—an idea that would boost the domestic market and fuel competition over returns. And it urges the Tokyo Stock Exchange to set guidelines that discourage poison-pill takeover defences.

The problems of senior service

At the same time, Japanese institutional investors are getting uppity. The Pension Fund Association, which manages $120 billion on behalf of its 29m members, has begun to vote against the renomination of directors unless their companies attain a return on equity above 8%. Although that is only half the norm for American and European firms, it would be a useful symbolic step to improve the Japanese average of 9.5%. Even some corporate leaders are starting to acknowledge the need for change (see article).

Turning the committee's proposals into reality will require political will. The prime minister, Yasuo Fukuda, will come under huge pressure to water down the ideas before he submits them to the Diet (parliament), as part of an economic plan, in June. Yet, even if Mr Fukuda stands firm, he will have only made a start. That is because the most important area for competition to take hold in Japan is not among organisations, but among the people who work in them.

One reason why Japanese managers fail to strive for better corporate performance is that they lack the incentive to do so. Blame this on Japan's “seniority-wage system”. Employees receive low salaries early in their careers in return for job security and a big payout in their final years. Tenure, not performance, determines what they take home. This system provided stability during the post-war period, when a booming Japan was rebuilding itself. But today it almost guarantees that exceptional performance goes unrewarded and mediocre work goes unpunished. Japanese managers have little stake in raising the value of their company, since they stand to gain very little by it. And why should senior staff welcome new ownership if it would jeopardise their own company's informal commitment to its employees?

This is not just a Japanese problem: elderly American managers hardly queue up to support foreigners taking over their employers. But payment-by-age is chronic in Japan. In fact, the gerontocracy has few legal underpinnings; rather it has to do with culture and tradition. A few business leaders have condemned it, but the politicians have largely kept mum. A good test of Mr Fukuda's reforming resolve will be whether he is prepared to preach the virtues of payment-by-performance. And the same goes for those domestic investment funds.

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Enlarging the European Union

Chicken or Kiev?

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The European Union must not abandon its most successful policy when it comes to Ukraine

IT IS, quite simply, the European Union's greatest achievement. The offer of EU membership to its neighbours in the east and south has proved a masterly way of stabilising troubled countries and inducing them to make democratic and liberal reforms. The contrast with the United States, which despite spending billions of dollars has failed to find an equivalent policy for the countries of the Caribbean rim, is striking.

Enlargement is, however, unpopular in many older EU members. It is accused by some of making the club unwieldy. Others blame it for an unwelcome inflow of cheap labour and an outflow of jobs. Still others complain that too many countries have been let in before they were ready. Indeed, the recent wave of EU enlargement has precious few defenders in western Europe. Even fewer stand up for the principle of letting in anyone else: France is poised to confirm that any big country's membership must be put to a national referendum.

Yet scare stories about enlargement have led to false alarms. Several studies confirm that the club functions as well with 25 (now 27) members as it did with 15. Cheap labour helps hosts as well as new members. Fears of job losses and rising competition have more to do with China than eastern Europe. The economies of several old EU members, notably Germany and Austria, have gained massively from enlargement—making their hostility especially perverse. As our special report this week argues, far from joining too soon, most of eastern Europe arrived in the nick of time.

This is not to say that enlargement has been trouble-free. Some countries may have come in unprepared, notably Bulgaria and Romania. The EU mistakenly guaranteed these two, plus Cyprus, a membership date in advance, instantly losing leverage for more reforms (or, in Cyprus's case, for a deal with the north of the island). The eurocrats have learnt that, once a country is in, they have less influence on it. But less is not none. Bulgaria and Romania now face sanctions for failing to fight hard enough against corruption and organised crime.

Catching a Ukrainian wave

In any case, teething troubles with a few new members should not become an excuse for slamming the door on others. It is right for the EU to be tough in negotiating entry terms, as it is being with Croatia and Turkey, the two countries now engaged in membership talks, even if that causes delay. But to suggest that these places, or others such as the western Balkan countries, should be kept out indefinitely, regardless of their progress with reform, risks provoking instability or even downright hostility from places smack on the EU's borders.

In reality, the case for eventual EU membership of the western Balkan countries is widely understood. Turkey is more controversial, as a big and mainly Muslim country—but it is *sui generis*. In many ways the bigger test of the EU's commitment to enlargement lies to its east, in countries like Moldova and, above all, Ukraine. Ukraine matters: it is the largest European country after Russia, with around 46m people, a lot of fertile farmland and significant industrial capacity, including in large aircraft and steelmaking.

The recent story of Ukraine seems, at first blush, depressing. The country's political leaders have been squabbling among themselves almost since the heady “orange revolution” in the Kiev snow during the winter of 2004-05 (see article). Inflation is worryingly high and corruption is rife. Yet some encouragement can be found behind the headlines. The country's political chaos and its vigorous media are testimony to a healthy democratic debate. Although Ukraine has no oil or gas, its economy has been growing strongly. It has just joined the World Trade Organisation, ahead of Russia.

Nobody could pretend that Ukraine is ready for membership of the EU. That could take a decade or more. But it would be wrong permanently to bar it as a candidate. It is as much a part of Europe as Bulgaria, and arguably more so than Turkey. Although many Ukrainians have doubts about joining NATO, almost all—even in the Russian-speaking east of the country—want to get into the EU. If Ukraine were kept out, it could easily fall back under the sway of a newly resurgent Russia; and the knock-on effects for other vulnerable places, such as Georgia and Moldova, could be serious. If, on the contrary, it were welcomed as a candidate, that would hugely encourage liberals who hope to bring proper democracy to Russia as well. It is high time that western Europe's political leaders began explaining to their voters just why both past and future enlargement of the EU is so much in their own interests.

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Nuclear proliferation

Iran's endless filibuster

May 29th 2008
From The Economist print edition

The world must once again ratchet up its efforts to stop Iran from enriching uranium

Reuters

IF THERE was an easier way to end Iran's nuclear defiance, Britain, France, Germany, America, Russia and China would have hit on it by now. The six countries trying to coax Iran into negotiation are stuck.

Diplomacy through the United Nations is jammed; force is both unpalatable and unlikely to finish the job. When the going gets this tough, the weary have one last option: to wish the problem away. Some latched on to last December's National Intelligence Estimate (NIE) from America's spying agencies saying that, alongside efforts to enrich uranium, Iran had been doing secret work on warheads but called it off in 2003. A jubilant Iran, which says it has never sought nuclear weapons, claimed vindication. Mohamed ElBaradei, head of the International Atomic Energy Agency (IAEA), the UN's nuclear inspectorate, even took it upon himself to bring Iran "out of the doghouse". Yet the latest report by his sleuths suggests Iran is anything but innocent. So it is time to step up the pressure once more, and mean it.

Helped by new intelligence from America and from several other IAEA members, as well as their own digging around, the inspectors have put some pointed questions to Iran about military connections to its nuclear programme. They especially want answers about studies that appear to show as yet undisclosed uranium-related work, high-explosive testing of triggers for nuclear bombs, a plan for an underground nuclear-test shaft and efforts to redesign the nose-cone of Iran's far-flying Shahab-3 rocket to accommodate a nuclear warhead.

A nuclear weapon requires other work too, but all this would get any bomb-builder off to a grand start. The inspectors say the information they have, from multiple sources at different times, is both detailed and "generally coherent". Iran replies that some of the allegations make no sense, that some of the documents are forgeries and that the high-explosive tests and other activities listed by the agency were done to aid civilian industry or else develop conventional weapons. But it has yet to provide access to records, people and places to back this defence up; and inspectors think it has more information, in particular about high-explosive and missile work.

So what next? The IAEA report will be presented to the agency's 35-nation board next week. Until now Iran has defied successive sanctions-bearing UN Security Council resolutions calling on it to suspend its uranium enrichment. While ignoring the stick of sanctions, Iran has also dismissed the many proffered carrots. It has brushed off offers by the six countries of wide-ranging economic and political inducements, including co-operation in less proliferation-prone nuclear technologies, once it stops enrichment. Instead, Iran has insisted on ignoring the Security Council and on dealing only with Mr ElBaradei and his team. But the inspectors, armed now with better intelligence, have been able to ask

Iran some hard questions and have received no convincing answers. This means that they can offer the world no assurances about either Iran's past nuclear intentions or its present ones.

No time to go wobbly

Iran is fuming. It had been counting on a strategy of finesse and filibuster: ignoring the Security Council, continuing to enrich uranium and trickling out bits and pieces of information to the nuclear inspectors only when they have presented clinching evidence of their own. All the while, Iran has loudly proclaimed its “right” to a supposedly peaceful nuclear programme. Some have been inclined all along to give Iran the benefit of that peaceful doubt. Others have tired of the drawn-out confrontation, wanting to get back to oil-business-as-usual. After the American NIE report, even some of the six seemed to wobble. The new inspectors' report at the very least ought to inject new mettle into their diplomacy.

Earlier this month, the six agreed to present Iran with an even more detailed offer of the goodies available if it suspends enrichment and sits down to talk. Next week's IAEA board meeting can help get Iran's attention by passing a resolution supporting the inspectors' demands for full disclosure. And if Iran still refuses to heed? The last UN sanctions resolution, just after the NIE was published, pulled all its punches. The next one needs to be tough enough to make Iran sit up and blink.

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Economist.com OPINION LETTERS

On competition law, Canada, Belgians, privatisation, EDS, tourism, LSD, reading

May 29th 2008
From The Economist print edition

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The law and competition

SIR – You pointed out that, although the gap between antitrust agencies in the European Union and the United States is far narrower than it was a few years ago, American authorities still bring fewer cases against the allegedly abusive behaviour of large companies ("Oceans apart", May 3rd). There is a fundamental difference between Europe and America that might provide an explanation for this and can be added to the points you mentioned: the recourse for private action in the United States.

In cases that are global in character, firms that ask the European Commission to act against the alleged anti-competitive practices of a large company can also pursue private lawsuits against that company in American courts, and often do so with success. Private antitrust action in Europe is encouraged by the commission to complement public enforcement, but it is still in its infancy. The stakes are therefore higher for Europe's competition authorities because the risk of potential under-enforcement in the region is greater.

Paul Csiszar
Directorate-General for Competition
European Commission
Brussels

Driving in Canada

SIR – Your story on electric cars in Canada implied that Transport Canada is responsible for vehicle licensing in Canada ("Not on our roads", May 3rd). This is a provincial-territorial responsibility. Nothing in Transport Canada's proposal to clarify the definition of low-speed vehicles (LSVs) stops provinces from licensing them for city use, and some are reviewing their laws to allow such vehicles on their roads or are conducting pilot programmes to determine their safe use.

Transport Canada will conduct crash tests that mimic collisions typically observed on city streets with low-speed limits in order to evaluate the protection offered by LSVs. Furthermore, the electric car manufactured by ZENN Motor Company that you mentioned would not be classified as a LSV under the law and would need to be fully certified for safety as a passenger car.

Kash Ram
Director general
Road Safety Directorate
Transport Canada
Ottawa

Questionable citzenship

SIR – You describe Gustave de Molinari as a "liberal Dutch economist" ("The poor relation", May 17th). Even though Molinari was born in what was at the time the United Kingdom of the Netherlands, he became a Belgian at the age of 11 at the time of Belgium's independence. His most important essays were written in French and he spent most of his life in France and Belgium. So he hardly qualifies as a Dutchman.

Quentin Michon

Paris

Record of achievement

SIR – Tony Blair's and Gordon Brown's record on privatisation does not conform to the Thatcherite model, as you suggest (Bagehot, May 10th). At least in its later stages, Thatcherite privatisation was concerned with the restructuring of government-owned industries to introduce price mechanisms, competition and transparent regulation, to offer a share of ownership to the public, and to promote general economic efficiency. The restructuring of the electricity industry was an extraordinary achievement that became the template for restructuring utilities around the world.

New Labour's stab at “privatisation” might have kept the name but it has changed everything else. New Labour's Orwellian public-private “partnerships” are more concerned with granting lucrative long-term contracts, often to mates of the government, often without adequate tendering, usually under the secret veil of “commercial confidentiality”, and generally in a way that conceals prices and suppresses the possibility of competition in the future. Its main objective seems to be to raise revenue without appearing to borrow or levy taxes. Privatisation under New Labour is more reminiscent of the Stuart kings than the Thatcher government.

Stephen Morris
Coorparoo, Australia

Corporate culture

SIR – Electronic Data Systems is no longer an “overwhelmingly American” company (“Now services”, May 17th). Only 34% of the workforce is based in the United States; 90,000 employees are located elsewhere. Moreover, the characterisation of the company's style as “military, buttoned-down, and staid” is dated and misses the mark. EDS is very much team-focused, and our dress sense is typically business-casual. In fact, if you visit one of our campuses on a Friday you are likely to see a fair share of denim.

Jeff Baum
Vice-president for communications
Electronic Data Systems
Plano, Texas

Trouble in Margaritaville

SIR – The protection of a country's natural wonders is a worthy goal, but your leader on the problems wrought by booming tourism in emerging economies smacked of snobbery (“Asia, beware Benidorm”, May 17th).

You claim that Cancún in Mexico is “a cautionary tale” because it has “nearly 24,000 hotel rooms, roughly 4m visitors a year and an average of 190 flights daily”. I assume you think that this situation is simply ghastly, but what exactly are you cautioning against? Job creation? A flourishing economy? Enjoyable and affordable recreation? The rising demand for tourism from the developing world will create a massive supply that cannot be catered for by the kind of boutique hotel that one suspects is favoured by *The Economist*.

Duncan Robertson
Liverpool

Experimenting with LSD

SIR – Your obituary on Albert Hofmann, the inventor of lysergic acid diethylamide, suggested that research into LSD stopped in the 1970s and never resumed (May 10th). Actually, a protocol evaluating LSD-assisted psychotherapy in people with anxiety related to end-of-life issues was approved in Switzerland last year. This is the first scientific controlled study of the therapeutic potential of the drug in more than 36 years. Mr Hofmann spoke about the Swiss approval as “the fulfilment of my heart's desire.” The first LSD session in that study took place recently.

Furthermore, to set the record straight, Mr Hofmann took LSD for the last time when he was 97 years old.

Rick Doblin
President
Multidisciplinary Association for Psychedelic Studies
Ben Lomond, California

Beach material

SIR – Regarding the redesign of your home-page ("We have lift-off", May 17th), no amount of tinkering with Economist.com can match the pleasure of reading your articles in the print edition late on a sunny Saturday morning on a beach near Athens.

Deucalion Rediadis
Athens

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America's suburbs

An age of transformation

May 29th 2008 | VALENCIA AND WILLINGBORO
From The Economist print edition

Alamy

America's suburbs are coming to resemble its city centres. That is both good news and bad

FIFTEEN miles east of Philadelphia, Willingboro's Grand Marketplace is a chaotic place. Merchants hawk Christian T-shirts, Amish quilts, Chinese food, massages and Afrocentric literature. Salsa music blasts from a CD stall. Most of the shoppers are black; the shopkeepers are a variegated mix of blacks, Latinos, Asians, Arabs and whites, including Pennsylvania Dutch farmers in traditional garb. Welcome to bland, homogenous suburbia.

In 1960 fewer Americans lived in suburbs than in central cities or the countryside. Ten years later the suburbs had overhauled both; by 2000 they contained more people than the cities and countryside put together. Despite more than a decade of urban boosterism, beginning with sitcoms like “Friends” and “Sex and the City” and continuing with expensive efforts to spruce up downtown districts, the drift to the cul-de-sacs continues. Between 1990 and 2006 the city of Chicago added 50,000 residents, reversing a long decline. Not bad—but in the same period the sprawling metropolis outside the city proper grew by well over a million.

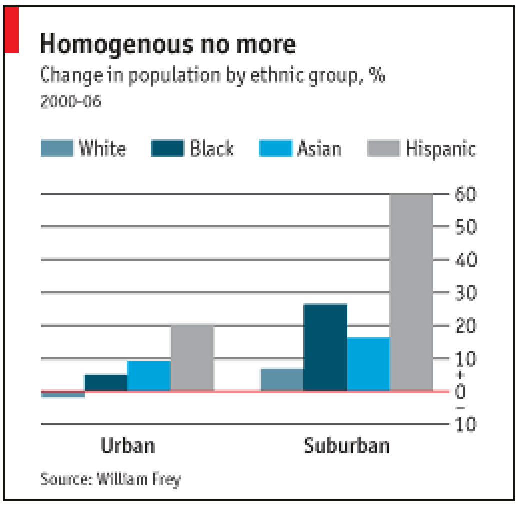
As they swell, the suburbs are changing. Perhaps none ever quite resembled the colourless domestic enclaves popularised by 1970s television programmes such as “The Brady Bunch”; now, they look nothing at all like them. America's suburbs are ethnically and demographically mixed—sometimes more so than its cities. Many are less dormitories than economic powerhouses. Among the most changed is one of the most famous.

Willingboro, or Levittown as it used to be known, was built 50 years ago this summer. It was created by William Levitt, who kept costs down by bringing in ready-made walls and buying cookers and refrigerators direct from manufacturers. As he boasted to *Time* magazine, his company was the “General Motors of the housing industry”. The new suburb was composed of self-contained neighbourhoods, each with its own school and swimming pool. Every street was reassuringly curved and shared the first letter of its name with the neighbourhood to which it belonged. Holyoke Lane, Henderson Lane and Hummingbird Lane all lay within Hawthorne Park.

One of Willingboro's first residents was Herbert Gans, a sociologist who wanted to find out whether suburbia conformed to the popular image of bored commuters and alienated housewives. His great book, “The Levittowners”, proved it did not. But Gans had to admit that Willingboro was homogenous. Virtually all home-buyers were white people in their 20s and 30s, with young children. The population was overwhelmingly lower-middle-class and less than 1% black.

These days Willingboro is two-thirds black. Although it remains child-oriented, it is no longer exclusively so. One in eight residents is now aged 65 or over. As the proportion of children has fallen, schools have been converted to other uses. One has been turned into a community centre where, on a recent Friday afternoon, an R&B band entertained a mixed-race crowd of old folk. The music drifted into a small room where Muslims, a growing presence in the neighbourhood, had gathered for prayers.

Such diversity is now common in suburbia. According to William Frey, a demographer, the white population of big-city suburbs grew by 7% between 2000 and 2006. In the same period the suburban Asian population grew by 16%, the black population by 24% and the Hispanic population by an astonishing 60%. Many immigrants to America now move directly to the suburbs without passing through established urban ghettos. Having conquered suburbia, ethnic-minority groups are now swiftly infiltrating the more distant “exurbs”.



As the suburbs become more mixed, some inner-city areas are turning less so. Los Angeles, which markets itself as the city “where the world comes together”, and New York (“the world's second home”) both added whites and lost blacks between 2000 and 2006. So many blacks moved out of Los Angeles that, were the exodus to continue unabated, they would disappear from the city around 2050. Manhattan and San Francisco lost Hispanics as well as blacks, which is remarkable given that group's speedy growth in the country as a whole. Meanwhile, the world came together on their fringes.

Gary Gates, who follows the subject at the University of California at Los Angeles, says the number of gay and lesbian couples in suburbia is also increasing. Much of this can be put down to greater tolerance: more same-sex couples are coming out of the closet, at least to census-takers. But some of it is due to migration from central cities. Atlanta, Detroit and Philadelphia all lost gays and lesbians between 2000 and 2006. The suburban counties surrounding all three cities saw increases in the number of same-sex couples, sometimes huge ones.

Why are gays and ethnic minorities moving to suburbia? The obvious answer is that they can. No suburban developer would dare bar blacks or any other group from buying houses, as William Levitt did until 1960. It has taken longer to overcome local prejudices—and the fear that behind twitching net curtains live intolerant neighbours rather than merely curious ones. Yet such anxieties are now fading. The Rev Willie James, who launched a lawsuit in 1959 that led to the desegregation of Willingboro, says overt racism is no more, and the covert kind is so covert as to be almost undetectable.

To the extent that ethnic-minority groups have needs distinct from those of whites (which they do less and less) they can increasingly meet them outside city centres. Los Angeles' best *dim sum* is to be found in the largely Chinese suburb of Monterey Park. Its best Indian restaurants are in Artesia, another suburb. Gays can go online to socialise, points out Mr Gates—or they can go to ordinary bars and clubs, where same-sex couples raise fewer eyebrows than they used to. Many young gays hardly see the point of pricey enclaves like Chelsea in New York or the Castro in San Francisco.

Despite recent falls, property prices in cities like Los Angeles, New York, Miami and Washington have risen far more than the national average since the mid-1990s. Many Americans find it worthwhile to move out and commute to jobs in the city. And they may not have to commute at all. The most important reason people are moving to the suburbs is economic: that is where the jobs are.

From bedrooms to boardrooms

Even when seen from a car at 65 miles per hour, Valencia does not conform to the popular image of suburbia. Drivers heading north from Los Angeles along Interstate 5 see few houses, because most are hidden behind a golf course. Instead they pass factories, warehouses and offices. It is not a bad introduction to the place. With some 60,000 jobs and 20,000 houses, Valencia boasts a better ratio of employment to homes than the city of Los Angeles. And still its businesses grow. Between 2002 and 2009 its supply of offices will have increased by half.

Valencia was designed by Victor Gruen, an architect who did as much to shape American suburbia in the 1960s as William Levitt had done in the 1950s. Gruen was an idealist: his most enduring invention, the two-storey enclosed shopping mall, was supposed to evoke a European city centre. For Valencia he devised a dense urban core and a series of neighbourhoods connected to each other and downtown via walkways known as *paseos*. The settlement was supposed to be orderly and self-contained, unlike the chaotic San Fernando valley just to the south. As one of the town's early planners explained, it would be "an island of reason in the path of metropolitan sprawl".

It didn't quite work out that way. Valencia contains no building taller than six storeys and few taller than three storeys. These days the *paseos* are used mostly for walking dogs, and by children. Everybody else drives. Nor did Valencia prove to be economically self-contained. Each morning about half of its residents leave for jobs in Los Angeles. Roughly the same number make the reverse trip over the Santa Monica mountains to toil in Valencia's offices, sound stages and warehouses.

This is an increasingly common pattern. In a forthcoming report, Alan Berube of the Brookings Institution, a think-tank, calculates that 45% of the jobs in America's 100 biggest metropolitan areas are found more than ten miles from the downtown core. Between 1998 and 2004 fully three-quarters of all new jobs emerged in this area. Many of these new positions were filled by local people, who were delighted to drop their long commutes to traditional city centres. But more and more Americans wake up in one suburb and go to work in another. Others, including many of Google's Bay Area employees, wake up in a city and go to work in a suburb.

America's suburbs have had shopping malls since the 1950s, and factories for longer. Increasingly, though, they are centres of white-collar work. The Inland Empire, a vast, sprawling area east of Los Angeles, accounted for more than a quarter of California's new professional and business-services jobs between 1998 and 2007. Over time, Mr Berube reckons, urban and suburban employment patterns will continue to merge. Health-care providers, for example, are drifting out of city centres to serve suburbia's increasingly aged residents.

Suburbs generally have cheaper land, newer offices and less crime than city centres. Companies that want to expand may well be able to do so in situ, and will not have to look for a new building across town. In Valencia they have another explanation for the suburbs' economic success. As Jim Backer, a developer, explains: "In the end, companies tend to move where their presidents want to move." And many presidents want to live in places like Valencia.

To those who like their cities plain, without a dash of urban grit, Valencia seems delightful. Its streets are safe and well-kept. Its purpose-built "town centre" contains shops, cafés, wine bars and art studios. Although nobody would mistake it for San Francisco, it also lacks that city's homeless problem and has more public seating. Teenagers coming out of the cinema enter a vaguely Mediterranean village square, complete with fountains, that is a far more pleasant place to linger than anywhere in, say, New York's Chelsea.

Valencia was one of the first places in America to build a shopping district that evoked an old-fashioned town centre. These days such things are popping up all over the country. Rick Caruso, a master of the genre, has built them in the heart of Los Angeles as well as in suburbs like Glendale. San Jose, in the Bay Area, has the hugely successful Santana Row, which is vaguely French, whereas Mr Caruso's developments are vaguely Italian. The popularity of such confections suggests that Americans want to spend time in places that look like cities but feel like suburbs. They hint at a broader pattern: cities and suburbs are converging. This is not entirely good news.

Trouble in Wisteria Lane

Right-thinking people disapproved of suburbs when Gans moved to Willingboro, and they dislike them today. James Kunstler, an American urbanist, says they represent "the greatest misallocation of resources the world has ever known". Richard Florida, an influential writer, sees them as incidental, at best, to cities' highest purpose, which is to concentrate young, creative folk who will come up with brilliant innovations. Now that America worries about global warming, the acres of bungalows and freeway exit ramps seem not just pointless but harmful.

Although much of this is nonsense, it cannot be denied that a little sheen has come off America's suburbs in the past year. Especially in the West, many have been hammered by foreclosures and falling house prices. As a result, their budgets are a mess. The fact that this is largely a consequence of success—the suburbs and exurbs grew rapidly at a time when lending standards were lax, and are now suffering the consequences—is little consolation. Nor is the fact that, as Joel Kotkin of Chapman University points out, the bottom has also dropped out of the city-centre apartment market.

Other problems are creeping into suburbia. The one that its inhabitants complain most bitterly about is traffic. America has failed to build enough roads to accommodate the suburbs' growing population—a big problem for places where public transport is generally weak or non-existent. Interstate 5, which is the only practical route between Valencia and the city of Los Angeles, is often clogged. Those who make the journey in either direction pay twice as much for petrol as they did in the spring of 2004.

Another worry is crime. Since 2001 the number of violent crimes in suburban areas has risen by 10%, according to the FBI. That is no more than one would expect, given the speed of population growth there. Yet it is a poor record compared with America's big cities, which have cut violent crime by 17%. In the past few years many of America's biggest indoor marijuana farms have been discovered in the suburbs.

In some suburbs fear of crime has risen more steeply. Willingboro's violent crime rate is one-quarter of Philadelphia's, yet its teenagers enter school through metal detectors. Blacks and whites alike worry that new arrivals from Philadelphia and Camden, in New Jersey, are importing gang culture. “They come here to escape, and sometimes they don't leave all their baggage behind,” explains Reva Foster, who works for Willingboro's government.

Perhaps the greatest problem of all is demographic. The suburbs used to be blessed with a young, productive population. Many of the newer, more distant exurbs still are. These days, though, many suburbs built in the 1950s are older than the central cities they surround. Willingboro's growing army of retirees is straining city services and resisting increases in property taxes, which account for almost two-thirds of the town government's revenues. Willingboro desperately needs to improve its schools if it is to continue attracting affluent settlers. Yet it is finding it ever harder to persuade residents to pay for them.

Although many urban mayors would happily swap the suburbs' problems for their own, cities do have one advantage: they tend to have large, centralised governments. In states like New Jersey, many suburbs try to govern themselves and suffer from diseconomies of scale. With just 33,000 residents Willingboro runs its own schools, police force, fire service and public-works department, among many other things. Elsewhere suburbs are controlled by urban city halls that largely ignore them, except as generators of taxes. Both arrangements make it difficult to come up with bold cures for the suburbs' growing pains.

An ordinary place

Weak government is a particular problem because, as suburbs become less homogenous, they are also losing some of their cohesiveness. A big complaint in Willingboro is that neighbours are less sociable than they used to be. Levitt's ideal of self-contained neighbourhoods is largely forgotten: most of the pools have closed, and children may no longer attend their local school. Jim Gray, a longtime resident, complains it is ever harder to rustle up volunteers for civic events. On the other hand, the same could be said of almost anywhere in America. Willingboro has managed to arrange about a dozen events to celebrate its 50th birthday.

Walk around Willingboro in the evening and you will see homeowners mowing their lawns and children squirting each other with water pistols, just as they did when the neighbourhood was much more homogenous. Mr Jones, the pastor, calls it “an ordinary place”, which is an excellent description. It is a reflection of the resilience of the suburban model that such places have changed dramatically while remaining essentially humdrum. At their best, they are even rather dull.

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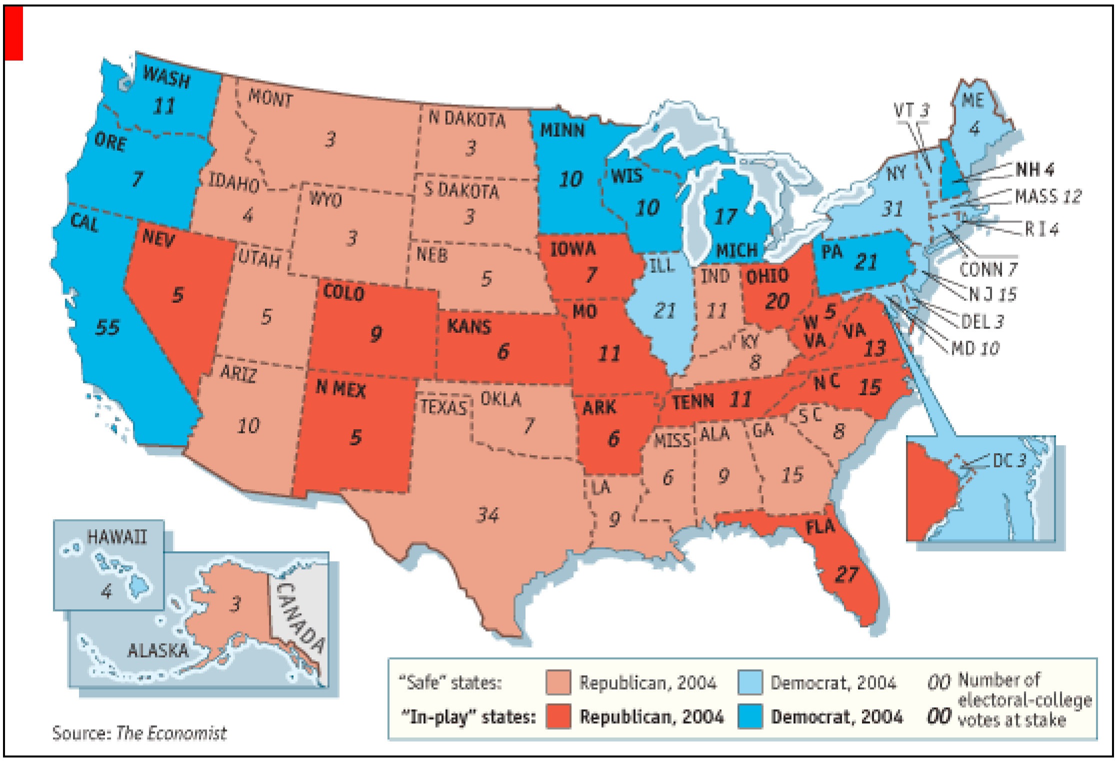
The electoral map

Battlefield America

May 29th 2008 | LOS ANGELES AND WASHINGTON, DC
From The Economist print edition

Under George Bush, red states were red and blue states were blue. This year the map could be drenched in purple



BARACK OBAMA hopes to wrap up the Democratic nomination next week, as the three last primaries, combined with an expected slew of superdelegate announcements, carry him over the threshold of victory. Already, his team is focusing on winning the White House. With an electorate sick of war, costly petrol and George Bush, the odds favour him. Intrade, a betting site, puts his chances at 58%.

If he (or, should a miracle occur, Mrs Clinton) stumbles, however, it may be because the electoral college has worked against the Democrats. With five months of campaigning still ahead, all predictions should be taken with a fistful of salt. Nonetheless, it is at least plausible that he (or she) might rack up pointlessly large majorities in liberal states while narrowly failing to carry enough swing states to win.

Geography, as so often in history, is key. The electoral map did not change much between the last two presidential elections. Only three states, all small, switched sides between 2000 and 2004: Iowa, New Hampshire and New Mexico. But this year could be very different. John McCain is an unusual Republican, distrusted by the party's evangelical base but popular with independents. Mr Obama's prospects are even harder to discern, since no black American has ever come this close to the presidency and people may lie to pollsters about his candidacy.

How, then, might the electoral map be redrawn this year? A good place to start looking is California. Most analysts say that this is probably not a swing state: John Kerry carried it by ten points. But since it is the biggest prize, with 55 electoral votes out of the 270 needed to win, it cannot be ignored. California's Latinos like Mr McCain's pro-immigration stance, but many of them loathe his party. The California Republican Party is a mess, stuffed with nativists and managing to be simultaneously chaotic and doctrinaire. Mr McCain's age may also count against him in a state where youth is worshipped.

On the plus side for Mr McCain, his defence of free trade will hurt him less in the Pacific West than in the rustbelt, since the region visibly benefits from trade with Asia and Mexico. Coming from next-door Arizona, he has a feel for Western issues, such as water and public-land use, which Mr Obama lacks. And California's popular Republican governor, Arnold Schwarzenegger, will lend Mr McCain some star power on the hustings.

In Florida, with its crucial 27 electoral votes, the picture is reversed. Even though he cannot take anything for granted, Mr McCain is roughly eight points ahead in the polls. Mr Obama has serious problems in the Sunshine State. He struggles to woo elderly voters. His idealistic approach to tyrants strikes Cuban-Americans in Miami as naive. What is more, if the Democratic Party cannot find a way to make the votes cast in Florida's Democratic primary this year count, many Florida Democrats who supported Hilary Clinton will still be seething in November.

Another point in Mr McCain's favour is that Florida's governor, Charlie Crist, who is even more popular and perma-tanned than Arnie, backs him whole-heartedly. There is talk of Mr McCain picking Mr Crist as his running-mate—he was one of three possibles invited to the senator's ranch last week. Mr Crist's current bachelorhood may count against him with socially conservative voters, but Mr McCain really needs to win Florida.

The closest battles in big states could be in Pennsylvania and Ohio. Both states have a lot of white working-class voters who think the economy is in terrible shape and foreign trade is much to blame. Their protectionism pulls them to vote for Democrats. But their love of guns and distaste for abortion pull the other way.

Mr Obama simply has to hold Pennsylvania. Polls show him six points ahead of Mr McCain, but his thrashing by Hillary Clinton in the primary should give him pause. He might woo her supporters by choosing Ed Rendell, the governor of Pennsylvania and a long-time Clintonite, as his running-mate. Doing so, however, would prevent him from picking the governor of Ohio, Ted Strickland, another Clinton loyalist whose help he might well need. Ohio, with its 20 college votes, single-handedly tipped the 2004 election to Mr Bush.

A poll of polls by RealClearPolitics.com shows Mr Obama only a whisker ahead of Mr McCain in Ohio. Voters there tend to prefer Mr Obama's economic populism, but to think Mr McCain would be a more reliable commander-in-chief. Mr McCain could perhaps blunt Mr Obama's advantage on economic issues by picking Rob Portman, a former head of the Office of Management and Budget, as his vice-presidential nominee. Not only is Mr Portman widely admired; he is also from Ohio.

The top ten to watch

State *(votes*)*	2004 results, % R-D	Governor	Comments
California *(55)*	44-**54**	R	Generally safe for the Democrats, but Governor Arnold Schwarzenegger strongly supports fellow-Westerr
Florida *(27)*	**52**-47	R	Barack Obama will struggle in this often close-run state. Governor Charlie Crist was an early McCain back
Pennsylvania *(21)*	48-**51**	D	Essential for Obama to hold, but he may struggle because of weakness among white working-class voters
Ohio *(20)*	**51**-49	D	Best hope for a big pick-up for Democrats. Now has Democratic governor, unlike in 2004 when George Bus
Michigan *(17)*	48-**51**	D	McCain's free-trade policies will hurt him in this close state
North Carolina *(15)*	**56**-44	D	Like most of the South, has recently been rock-solid for the Republicans. But 21% of the state is black, g
Virginia *(13)*	**54**-45	D	Solidly Republican in recent presidential elections, Virginia has elected Democratic governors in the pas
Missouri *(11)*	**53**-46	R	Like Ohio, a bellwether state. The Democrats picked up a Senate seat here in 2006, and have high hopes
Minnesota *(10)*	48-**51**	R	This Kerry-voting state is another important pick-up possibility for McCain. Governor Tim Pawlenty is a p
Colorado *(9)*	**52**-47	D	The biggest of the purple states of the Mountain West, Colorado is a key Democratic target

Source: *The Economist*

Mr Obama faces several challenges in his own backyard. Across the lake from his home state of Illinois lies Michigan, a Democratic state whose 17 electoral votes are up for grabs. As luck would have it, Michigan is the other state where Democratic primary votes seem unlikely to count this year, leaving many Hillary-loving locals angry. Polls show Mr Obama and Mr McCain neck and neck there, though Mr Obama's NAFTA-scapegoating is an easier sell than Mr McCain's blunt assertion that “some of the jobs that have left the state of Michigan are not coming back.”

Three more states that border Illinois will be fiercely contested: Missouri, Iowa and Wisconsin. Missouri went for Mr Bush by seven points in 2004, but turfed out a Republican senator in 2006. Because eastern Missouri touches Illinois, people there have been able to watch Mr Obama's TV adverts since before he was nationally famous. And sizeable black populations in St Louis and Kansas City will flock to him. Many in Missouri are culturally conservative, however, and Republicans will remind them of Mr Obama's ultra-liberal voting record in the Senate.

Wisconsin, with ten electoral votes, narrowly backed Mr Kerry in 2004. Mr Obama, who did well in the Wisconsin primary even among groups he normally fails to excite, such as white blue-collar workers, hopes to do better. The polls are all over the place.

Iowa is smaller, with only seven electoral votes, but the terrain favours Mr Obama. Mr Bush won there by a single point in 2004. Mr Obama kick-started his national career by winning the Iowa caucuses in January. Mr McCain, who resists showering corn farmers with subsidies, lost miserably there.

AP

In happier times

Mr Obama hopes that the vast enthusiasm for his candidacy among African Americans will translate into electoral votes. It will help, of course. But unfortunately for him, America's black population is concentrated in the South, most of which seems impregnably Republican. Some 30% of Georgians, for example, are black, but even a huge increase in black turnout will be hard pressed to overturn the 17-point margin by which Mr Bush won there in 2004. Mr Obama's chances are better in the upper southern states of North Carolina and Virginia. Both voted for Mr Bush, but both are becoming more liberal as yuppies move in. A combination of blacks and college-educated whites has given both states Democratic governors.

Mr Obama is six points behind Mr McCain in North Carolina and only one point behind in Virginia. Armchair strategists urge him to pick a Virginian running-mate. Tim Kaine, the governor, is often mentioned. So is Jim Webb, Virginia's junior senator and a former secretary of the navy. Mr Webb would shore up Mr Obama's perceived weakness on national security. But some harsh things he once said about women in combat will upset a lot of former Hillary voters.

Among Mr McCain's targets is Minnesota, which has not voted Republican in a presidential race since 1972 but is turning purple. Mr Kerry won the state by three points. Mr Obama's poll lead is larger, but fragile. The Republicans will be holding their convention in Minneapolis-St Paul this year. And Mr McCain might pick Minnesota's governor, Tim Pawlenty, as his running-mate. Party insiders warm to both Mr Pawlenty's record and his humble roots. His mother died when he was 16. He says he wants the Republicans to be “the party of Sam's Club [ie, people who shop at Wal-Mart], not the country club”.

The final battleground will be in the Mountain West, where libertarian voters like their taxes low and their government unpreachy. This makes Colorado, Nevada and New Mexico all “purple” states, which is why Mr Obama visited all three this week and the Democrats will hold their convention in Denver.

Colorado voted for Mr Bush by five points but elected a Democratic governor in 2006. Nevada backed Mr Bush by two points but constantly re-elects the Senate majority leader, Harry Reid. New Mexico backed Mr Bush by one point but has a Democratic governor, Bill Richardson.

Mr McCain will make much of his local-boy status, since Arizona touches all three states. Were he to pick the conservative Mike Huckabee as his running-mate, however, he would alienate the Mormons in Nevada, who resented the former Arkansas governor's unsubtle digs at their faith during his Republican primary tussle with Mitt Romney, a Mormon. But even winning all three would not compensate Mr Obama for a loss in Pennsylvania.

The sheer number of battleground states plays to Mr Obama's strengths. He will have much more money than any previous presidential candidate, and will be able to unleash a barrage of ads on every battlefield. He can fight hard for every remotely winnable state and force Mr McCain to spend time and money defending supposedly safe ones. Both candidates' vice-presidential picks will be endlessly scrutinised. Seasoned observers say running-mates seldom affect the final result. But if the race is close, both sides will look for any advantage they can find.

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The economy

Stimulus and shopping

May 29th 2008 | WASHINGTON, DC
From The Economist print edition

Good news for bargain basements

KATE from Baltimore bought a three-foot-tall light-up ice cream cone with her stimulus cheque. Stephen, from Brunswick, Georgia, acquired a brand-new Smith & Wesson pistol. And Nick from Ephrata, Pennsylvania, bailed himself out of jail. But far more typical of the entries at HowISpentMyStimulus.com are those like Monte's from Los Angeles, who resisted his urge to establish a legal fund to try George Bush for war crimes and paid off his credit-card balance instead.

Congress passed its fiscal stimulus package in February, promising most Americans $600 plus $300 more for each child in income-tax rebates—and a hoped-for hefty economic boost along with it. Think-tankers predicted an increase in annualised GDP of between 0.8% and 3% in the quarter in which the Treasury started distributing the cheques, which it did at the end of April. But now that the cash is at last flowing, where is it going?

Retailers are promising big discounts for Americans who spend the rebates in their shops. But surveys find that consumers are planning to spend only somewhere between 20% and 40% of the rebate. The rest will go towards paying down debt or into savings accounts.

Indeed, lean business inventories indicate that retailers do not expect to see a surge in sales. And anyway, the dollars that are spent rather than saved may not go where they are most needed. With food and oil prices both sharply higher since Congress approved the stimulus package, 17% of recipients now plan to allocate their rebate money to these necessities, according to the National Retail Federation, a trade group. That's great news for grocery stores, its spokesman says, but not for struggling big-box retailers.

The American consumer, once a bulwark against economic malaise, is increasingly reluctant to spend. An index of consumer confidence compiled by the Conference Board, a New York-based research group, hit a 16-year low on May 27th. Americans have not been as worried about the future since 1978, it found, with a record proportion expecting their incomes to fall. Rising commodity prices are not the only worry. The labour market is weak, with continuing jobless claims at a cyclical high. Home prices are still falling (see article). And the Federal Reserve reports that banks continue to tighten their lending criteria. More Americans worry about inflation, which could deepen these problems. Such negative consumer sentiment indicates that real spending is at risk of starting to decline for the first time since the recession of 1990-91.

Americans' plans for what to do with their stimulus cheques reflect the changing profile of national consumption. Consumers need to spend more on food and fuel. With disposable income strained by rising prices, they are travelling less and cutting back on purchases of clothing and consumer electronics. Car sales continue to languish. Big retail chains such as Sears Holdings, which was expected to announce a 90% dip in first-quarter earnings on May 29th, have seen shrinking revenues because of aggressive discounting.

Many Americans are trading down: sales at department stores are increasing at sluggish rates not seen since the last recession, while sales at discount stores are still growing briskly. Mid-range and luxury retail chains are postponing or cancelling planned expansions, hurting the commercial construction industry. And even luxury brands are planning to open new cut-price shops in America's discount outlet malls. Higher food costs, meanwhile, are a boon to warehouse clubs; some consumers are even stockpiling stores of frozen meat to hedge against rising prices.

Profligate spending habits are unlikely to return soon. The stimulus is just a one-off boost—though a reprieve from credit-card payments might be helpful to Monte—and commodity prices are likely to stay high. Until Americans see the housing crunch bottom out and can learn to adapt to higher food and energy prices, they will spend more time in Wal-Mart than in Tiffany, and America's once-mighty big retailers will continue to look to their outlet malls.

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The housing market

Dropping a brick

May 29th 2008
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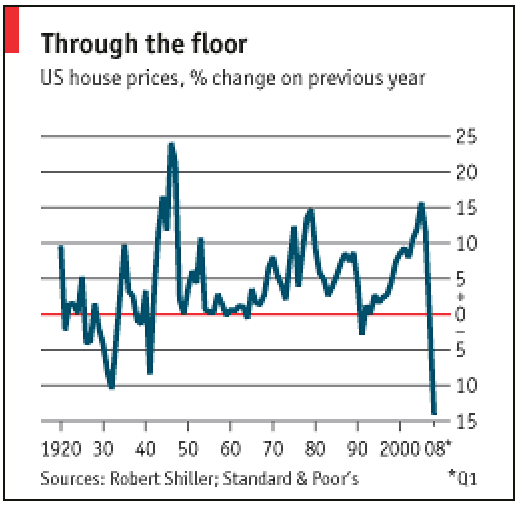
House prices are falling even faster than during the Great Depression



“A DESTABILISING contraction in nationwide house prices does not seem the most probable outcome...nominal house prices in the aggregate have rarely fallen and certainly not by very much.” Alan Greenspan's soothing, if rather verbose, words on America's housing market in 2005 rank high on history's list of infamous predictions. But to be fair, most American economists shared his view that it was highly unlikely that average nationwide home prices would drop. That was the sort of thing that happened only during a deep depression, like the 1930s.

Unfortunately, new figures this week reveal that house prices have already fallen by more over the past 12 months than in any year during the Great Depression. The S&P/Case-Shiller national index fell by 14.1% in the year to the first quarter. Admittedly, other property indices show smaller drops, but most economists now favour this measure. The index goes back only 20 years, but Robert Shiller, an economist at Yale University and co-inventor of the index, has compiled a version that stretches back more than a century. This shows that the latest fall in nominal prices is already much bigger than the 10.5% drop in 1932, at the worst point of the Depression.

And things are even worse than they look. In the deflationary 1930s, America's general price level was falling, so in real terms home prices declined much less than they did nominally. Today inflation is running at a brisk pace, so property prices have fallen by a staggering 18% in real terms over the past year. In nominal terms, the average home is now worth 16% less than at the peak in 2006, and the large overhang of unsold houses suggests that prices have further to fall. If so, this housing bust could well see a bigger cumulative fall in prices than the 26% real drop over the five years to 1933. Most people would call that a pretty destabilising contraction.

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Carbon emissions

And the winner is...

May 29th 2008 | LOS ANGELES
From The Economist print edition

A much-criticised city turns out to be one of America's greenest

AP

FROM the air, Los Angeles hardly looks like an environmental paragon. It sprawls heroically, seeming to begin well before passengers from the east are told to fasten their seatbelts. On warm days a thin brown haze hangs over the city. Its most striking feature is its freeways—rivers flowing with glass and steel that turn red and white at night. Yet on May 29th the Brookings Institution reported that the residents of the “neon-lighted slum”, as Raymond Chandler called it, generated less carbon per person than any other metropolis in continental America.

Sorry? Los Angeles is, after all, a symbol of environmental degradation. It became car-oriented well before most other cities. “If I lose my car it's like having my legs cut off,” explains the doomed hero of the 1950 film “Sunset Boulevard”. These days the metropolis is renowned for jammed freeways. Talk to the mayor of almost any Western city and they will outline their plans for avoiding Los Angeles' fate.

Brookings's number-crunchers calculated carbon footprints mostly by studying highway traffic and household energy use. They excluded local traffic and industry because the statistics are bad. Top of their green list is Honolulu, in Hawaii, whose residents accounted for 1.36 tons of carbon each in 2005. Los Angeles, at 1.41 tons per person, narrowly beats Portland, Oregon, which is widely proclaimed as an über-green city. New York comes fourth. At the bottom of the table, spewing out more than twice as much carbon per person as Los Angeles, is Lexington, Kentucky.

Weather is one explanation. Six of the ten most virtuous metropolitan areas are on the west coast, where Pacific breezes lessen demand for heating and air-conditioning. The worst scores for energy use go to places like Cincinnati and Washington, which have appallingly humid summers and bitter winters. Urban areas in the Midwest receive black marks because so much of their electricity comes from coal. In Los Angeles just under half does, and that will drop steeply as new environmental laws come into effect.

Another reason is that Los Angeles sprawls less than it appears. It may be a low-rise city, but a surprising number of people pack into its “dingbat” houses and bungalows. As Robert Bruegmann, a Chicago urbanist and connoisseur of sprawl, points out, this is especially true of the city's many immigrants. Almost one in four Latino households in the metropolis has more than one person to a room.

It is these suburbanites who are really virtuous. Places such as New York and Portland have pockets of abstemiousness—just 9% of Manhattanites drive to work alone, compared with 75% of Angelenos. Yet they are let down by their hinterlands, which sprawl much more extravagantly than do the outskirts of Los Angeles. Big houses on half-acre lots, common in New York's commuter belt, are rare in southern California.

These days Los Angeles is trying to improve its environmental image by encouraging developers to build blocks of flats. The Brookings report suggests this approach is wrong, or at least inadequate. The metropolis should build more bungalows rather than force families who want them to live farther inland, where temperatures are higher. There is plenty of room for more concrete on the coast. Between Orange county and the city of San Diego, for example, lies little besides tomato farms and a military base. To save the planet, fire up the bulldozers.

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Scott McClellan's memoirs

Unspinning the war

May 29th 2008 | WASHINGTON, DC
From The Economist print edition

A spokesman speaks out

THERE is an old joke about the British Tory party which says that, if loyalty was its secret weapon, it did a good job of keeping it secret. The same is becoming true of Bushworld. Next week Scott McClellan, George Bush's press secretary in 2003-06, publishes a grim account of his time as a Bush loyalist, “What Happened: Inside the Bush White House and Washington's Culture of Deception”.

Mr McClellan argues that the decision to invade Iraq was a “serious strategic blunder”. But it was a blunder that was sold to the American public by a relentless propaganda campaign to hype the threat from Saddam and smear critics. Mr McClellan admits that many of the things he said at his press briefings turned out to be “badly misguided”. He says that matters of state were subordinated to the day-to-day requirements of the “permanent campaign”.

Mr McClellan is also candid about his former White House colleagues. Karl Rove misled him about his role in the Valerie Plame affair and sent him onto the podium to lie. Condoleezza Rice was a master of deflecting blame. Dick Cheney was “the magic man” who steered policy from behind the scenes without leaving any fingerprints. Mr Bush was obsessed about doing what his father had failed to do—win re-election—and shockingly incurious about the world.

None of this is particularly new. But the fact that it is coming from such a source is significant. Mr McClellan is the very definition of a Bushie—an Austin native who joined Mr Bush's staff in 1999 and worked his way up to become press secretary at the most traumatic time in the Bush presidency. It is one thing for left-wing bloggers to assert that “Bush lied, people died”. It is another for the president's own spokesman to question his master's veracity.

Mr McClellan also makes two explosive claims. The first is that Mr Bush's real motive for going to war was never WMD. It was his desire to transform the Middle East and ensure an enduring peace in the region. The gap between the real and stated reasons for going to war forced the White House to engage in a constant campaign of shading the truth. The second is that “Scooter” Libby and Mr Rove held a secret meeting at the time when federal prosecutors were investigating them both over the leak of the name of Ms Plame, a CIA agent. Mr Libby was convicted; Mr Rove has never been charged with anything.

The publication of “What Happened” will not help John McCain. Mr McCain regards his steadfastness on Iraq as one of his chief selling points, and accuses Barack Obama, who opposed the invasion from the first, of naivety about foreign affairs. It is not hard to guess who will be quoting Mr McClellan's book.

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The new gold rush

Miner '09er

May 29th 2008 | ANCHORAGE
From The Economist print edition

A price of $900 an ounce is quite an incentive

STEVE HERSCHBACH has seen it all before. There is a number, he explains, at which greed overcomes fear, and rationality goes out the window. “Last year the price of gold hit $700 an ounce and I thought it was going to take off, but it really didn't happen,” says Mr Herschbach, an amateur prospector for more than 30 years and owner of the Alaska Mining and Diving shop in Anchorage. But when it broke $1,000 earlier this year, “Well, we're in the middle of it now. Everyone hoping to make a buck has suddenly come out of the woodwork.” The price has fallen back a bit, but is still over $900.

Mr Herschbach's annual order of prospecting gear—shovels, dredges, gold pans, sluiceboxes, metal detectors and the like—sold out in March, months before the season generally gets under way, and he has since put in a second order. His equipment suppliers, however, are running a three-month backlog.

Most of his customers are doomed to disappointment. The game has not changed that much since the 1850s, Mr Herschbach reckons. “If you think digging ditches in pouring down rain while being eaten alive by bugs is fun, well you're gonna love gold mining.” Not only is prospecting hard, physical work, but “you really gotta know your stuff.” Experience, he explains, really does count. “You can have the best equipment and a great location, but if you don't know what you're doing it's going to be pretty tough.” If it was easy, he adds, gold wouldn't cost as much as it does.

Yet, for those willing to give it a try, there are dozens of websites and forums willing to dole out advice or sell you something. Membership in gold-prospecting clubs and associations has surged. The 45,000-member Gold Prospectors Association of America reported that renewals at the close of 2007 had doubled over the previous year. In addition to a bi-monthly magazine and an online forum where members can exchange stories and tips, the GPAA hosts a number of events where members congregate at sites to dig for gold and meet other members.

Alaska, because of its size, remoteness and relatively relaxed regulatory climate, tends to draw the most, and most serious, prospectors. With vast tracts of land accessible only by air or boat, there is still a lot of gold left to be discovered.

However, most sites of any potential will have some sort of claim on them. For those who don't want to hassle with the paperwork, there are numerous “pay-to-mine” operations which, for a fixed fee, will provide the site, the equipment, some basic guidance and then let the novice try his or her hand at prospecting. A lucky few may find enough gold to help pay their expenses (which can run up to $2,500 per week plus another $500 in airfares from Anchorage), but most will go home with just a sore back and a story or two to tell. The odds are better in Las Vegas.

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Mining and pollution

National treasure

May 29th 2008 | BUTTE, MONTANA
From The Economist print edition

Paying for a toxic legacy

ONE of the more unusual tourist attractions in Montana is the Berkeley Pit, an enormous man-made lake in Butte. It was originally an open-pit copper mine, but when industrial operations stopped it began to fill with highly acidic groundwater. In 1995 several hundred migrating geese landed on its surface. The next day they were all bobbing in the dark water, dead. It seems that nothing can live in the pit except for a few microbes known as extremophiles, which thrive on adversity.

Mining in America is still governed by a law from 1872. At the time, Congress was keen to see the West settled. The General Mining Act said that anyone swinging a pickaxe could acquire public land for $5 an acre and keep whatever they dug up there. There have been a few tweaks over the past 136 years. Coal, oil and gas operations have to pay royalties. Since 1994 Congress has paused on the practice of selling the land to anyone who asks for it. But hardrock miners, who extract hard minerals rather than hydrocarbons, pay no royalties on the $1 billion worth of metals and gems they extract annually. And although new outfits are supposed to show that they can afford to clean up after themselves, various federal agencies have had to spend at least $2.6 billion cleaning up abandoned mine sites over the past 11 years.

Previous calls for reform have been swatted away by sympathetic politicians, who point out that mining creates jobs. But the issue is becoming harder to ignore. A report in May from the Environmental Working Group found that the number of mining claims within 10 miles (16 km) of the Colorado river has more than doubled over the past five years. Metal mining releases more toxic chemicals than any other industry in America. The Colorado supplies water to 25m people in the south-western United States.

Late last year the House of Representatives passed legislation that would impose royalties on mining revenue and give the government more power to protect public land. Similar efforts are expected to face trouble in the Senate in the shape of Harry Reid of Nevada, the Senate majority leader. The industry is a big employer in his state, not to mention a significant campaign contributor. He opposes any idea of extracting royalties.

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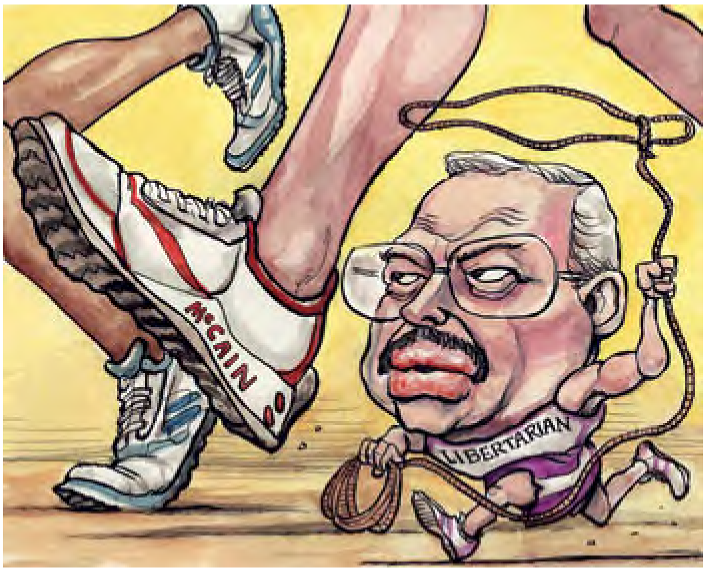
Lexington

Raising the Barr

May 29th 2008
From The Economist print edition

Angry libertarians could be a problem for John McCain in November

Illustration by Kevin Kallaugher



ON MAY 25th a dysfunctional minor party picked a grumpy ex-Republican as its presidential candidate. This may be just another quirk in the quirky history of the Libertarian Party. But it just might be something more than this: a further sign that the Republican coalition is splintering under John McCain's feet.

The new Libertarian champion, Bob Barr, a former four-term Georgia congressman, is most famous for his poor judgment and sour temper. He led the fight to defang anti-terrorism legislation after the Oklahoma City bombing (among his achievements: preventing the government from designating foreign groups as terrorists and denying their members visas to enter the country). He championed social-conservative causes such as the Defence of Marriage Act, which he drafted, and the impeachment of Bill Clinton. His moralistic fervour faltered only when it came to his own conduct: twice divorced, he was once photographed licking whipped cream off the breasts of a particularly buxom woman. He says he was raising money for leukaemia research. (Well, he would, wouldn't he?)

The Libertarian Party is one of the perennial jokes of American politics. Barry Goldwater, a party hero, once argued that “extremism in the defence of liberty is no vice”. Many Libertarians have interpreted that as meaning that extremism in defence of liberty is a positive virtue: one of the liveliest debates in the party is whether all drugs should be legalised, and all federal taxes abolished, next Monday or next Tuesday. The party's best presidential performance was back in 1980 when Edward Clark won 921,128 votes, or 1.1% of the electorate. Most Libertarian candidates have hovered around just 400,000 votes. The party is also badly divided between what might be called its Ruby Ridge wing and its Reefer Madness wing. The Ruby Ridge wing, which has still not recovered from the terrible day when the FBI shot several survivalists at Ruby Ridge in Idaho, believes that freedom comes from the barrel of a gun. The Reefer Madness wing is more interested in keeping the government's hands off its spliffs.

Mr Barr's candidacy is not likely to heal this division. The Georgian has a solid record on guns—he once accidentally discharged an antique pistol at a gun show—but he is much dodgier on other Libertarian shibboleths. He joined the party in 2006 only after being redistricted out of his congressional nest. He once supported both the Patriot Act and the “war on drugs”, though he is now repentant. He won the party's nomination only after six ballots and five hours of voting.

Yet the Republicans would be unwise to write him off as irrelevant: instead, they would do well to consider the reasons for the enduring success of Ron Paul, a Republican who shares many of the Libertarians' views. His presidential campaign has been one of the wonders of this election cycle, powered by hyper-motivated supporters and an endless supply of small donations. Mr Paul won 24% of the Republican vote in the recent Idaho primary, despite the fact that Mr McCain has the nomination locked up. His book, “The Revolution: A Manifesto”, leapt to the top of the *New York Times*'s bestseller list.

The libertarian pool also contains more fish than you might think. Polls suggest that 10-20% of the electorate are willing to define themselves as “libertarians” in the sense that, like this newspaper, they are “conservative” on economics and “liberal” on social issues. These soft libertarians have been strikingly willing to break party ranks, whether to support John Anderson in 1980 or Ross Perot in 1992 and 1996.

Libertarian-leaning Republicans are also hog-wrestling mad about what has become of their party under George Bush. Mr Bush has presided over the fastest growth in federal spending since the Great Society in the 1960s. He put the Republican seal of approval on the biggest intrusion of federal power into the classroom in history (No Child Left Behind), the most expensive public-works programme ever (the 2005 highway bill) and the largest new entitlement programme since the creation of Medicare and Medicaid (the prescription-drug benefit). He launched an open-ended “war on terror”. He rode roughshod over states' rights on issues such as assisted suicide. And he has expanded the government's power to eavesdrop on its citizens.

Spot the difference

Mr McCain is not Mr Bush. He has an honourable record as a fiscal conservative (he opposed the prescription-drug benefit, for example). He is Washington's leading campaigner against pork. He is a principled federalist on issues like gay marriage. But there is plenty in his record to upset small-government conservatives. He likes to think of himself as a latter-day Teddy Roosevelt blowing the trumpet of “national greatness conservatism”. He broke the conservative covenant by supporting campaign-finance reform. His defence of the Iraq war may also cost him votes from small-government conservatives.

Mr Barr and the Libertarian Party, as well as Mr Paul, are both imperfect vehicles for all this pent-up anger. But they are vehicles nonetheless. Libertarians claim that they will put their candidate on the ballot in 48 states, as they did in 2004. They have already managed 28. Mr Barr claims that (admittedly sparse) polls give him 6-8% of the electorate. He could do particularly well in his native Georgia and the libertarian-leaning West. That could hurt Mr McCain badly in states like Colorado and Nevada, which he needs to hold on to.

The fact that Mr Barr's running mate, Wayne Allyn Root, is the author of a self-help book entitled “The Joy of Failure!” takes some of the air out of this speculation. But it would be wrong to underestimate how angry many small-government Republicans are with Mr Bush. Ronald Reagan once remarked that he did not leave the Democratic Party: the Democratic Party left him. That is what many libertarian sorts now feel about the Republicans.

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South American defence

Speak fraternally but carry a stick

May 29th 2008 | CARACAS, SANTIAGO AND SÃO PAULO
From The Economist print edition

Reuters

Is there a new arms race—or just overdue retooling of armies?

GIVE or take the odd border raid and attempt to undermine a neighbour, fraternal feeling abounds in South America. Many countries are governed by people who were once leftist soul-mates. They talk of ever-greater integration. This rhetoric abounded on May 23rd, when 12 leaders met in Brasília and formally set up a Union of South American Nations. Yet like many such initiatives in the region, ambition ran far ahead of reality.

Unasur (or Unasul in Portuguese) replaces a South American Community declared in 2004 and supposed to unite two existing free-trade areas, Mercosur and the Andean Community. That proved too difficult—and is likely to remain so. The new group will have the appearance of purposefulness, including a secretariat in Ecuador and a parliament in Bolivia, but not much more than that.

The leaders also discussed setting up a South American Defence Council as a forum to talk about defence and security. Brazil has been pushing for this. Its diplomats thought that they had an agreement to make it happen. Yet they were thwarted when Colombia declined to join because of its neighbours' equivocal attitude to its FARC guerrillas.

Even as its leaders talk, Latin America is re-arming—or rather some South American countries are. In the broader region, including Mexico, Central America and the Caribbean, total defence spending shot up to $38 billion in 2007 from $25 billion in 2003, according to the International Institute for Strategic Studies (IISS), a London think-tank. The military budgets of the biggest spenders—Brazil, Colombia, Chile and Venezuela—have been rising faster. Brazil announced a rise of 50% (or $10 billion) in its spending on hardware for 2008-11.

Two things are driving the spending increases. First, military budgets were cut after many Latin American nations turned their back on military rule in the 1980s. In many countries, equipment is now ancient and dilapidated. Replacing it is a sign of more normal relations between civilian governments and their armies. Venezuela is the exception: although its leftist president, Hugo Chávez, is elected, he is a former army officer and his power base lies partly in the barracks. Venezuela's recent purchase of two dozen Sukhoi-30 fighter aircraft and 50 military helicopters from Russia may have been presented as a show of strength to the imperialists in Washington, but it was also designed to shore up support from the generals at home.

The second reason is that after four years of faster economic growth, partly induced by high prices for commodity exports, governments have more money to spend. In Chile, the link between commodity prices and arms is written into law: the armed forces get 10% of the export revenues of Codelco, the state copper producer—a sum that amounted to $1.4 billion in 2007—for capital spending. Over the past dozen years this money has bought 340 German tanks, eight frigates, two new submarines and 28 F-16 fighters.

Chile's appetite for new kit is a worry for both Bolivia and Peru, which dispute its land and maritime borders respectively and which were the losers in a 19th-century war. In early May Alan García, Peru's president, urged his peers in the region to stop buying weapons and to concentrate instead on fighting poverty. At a day-to-day level, however, relations between Chile and its neighbours are less tense than they were three decades ago when all were ruled by generals.

Similarly, Brazil's arms build-up, which includes plans for a nuclear-powered submarine and new jet fighters, has not alarmed its neighbours much. Economic stability and growth, and an increasingly solid democracy, have recently made Brazilian governments more confident about acting as the regional superpower—but through diplomacy. Some Brazilian officials look askance at Colombia, whose military build-up against the FARC has the backing of the United States. But the main threat to Brazil's ambition is Mr Chávez, who has sought to develop a network of clients in the region, dependent on his gifts of cheap oil and cash.

Venezuela's arms purchases alarm several of its neighbours. Mr Chávez this month said airily that more tanks for Venezuela “shouldn't worry anybody”. He promised that he would place yet more orders for Russian weapons on a planned trip to Moscow in July. What for? The president says that he would prevent the United States from setting up a military base near Venezuela's border “whatever the cost”. He has also said that demands for greater autonomy in eastern Bolivia could lead Venezuela to intervene in support of the socialist government there.

Mr Chávez seems to have his eye mainly on Colombia. He resents its alliance with the United States, and has expressed sympathy for the FARC. Captured guerrilla documents suggest that Venezuelan military and intelligence officers have actively helped the guerrillas. Mr Chávez responded to Colombia's cross-border raid into Ecuador in March (which killed a FARC leader) by briefly ordering tanks to the border. “Look at the evidence and [you] conclude that Venezuela is arming for war with Colombia,” says Rocío San Miguel, a defence analyst in Caracas. It recently bought 100,000 Kalashnikov rifles (more than its total number of regular troops). These are to replace ancient Belgian rifles. But the ammunition they fire is compatible with guns used by the FARC.

Hitherto Colombia's military build-up has been wholly focused on counter-insurgency. But in what appears to be a defensive response to Mr Chávez, it has placed an order with Israel for Kfir fighter jets. According to Mark Bromley of the Stockholm International Peace Research Institute, Colombia has also been talking to Sweden about buying an airborne early-warning system and a tanker plane.

Take into account the weakened dollar as well as economic growth, and in many countries the arms spending looks less threatening. At least until 2006, defence spending in Latin America as a whole was running at only 1.3% of GDP, according to the IISS. Only the non-NATO European countries spend less. Some of the recent spending in South America involves retooling armies that used to repress their own populations for new roles, such as peacekeeping or Amazonian surveillance. Nevertheless, some of the recent purchases are cause for concern—especially given that so much talk of South American unity is just that.

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Colombia

After Sureshot

May 29th 2008 | BOGOTÁ
From The Economist print edition

Without its veteran leader, the FARC's defeat looks to be only a matter of time

PRESIDENTS have come and gone over the past four decades in Colombia but one man remained constant. Pedro Antonio Marín, better known by the *noms de guerre* of Manuel Marulanda or “Tirofijo” (“Sureshot”), led his FARC guerrillas through army bombardments, bogus ceasefires and failed peace talks, never giving up his quixotic and destructive campaign to turn a large South American democracy into a clone of the long-vanished Soviet Union. Mr Marulanda's death was always going to be of moment for Colombia. In the event, it has almost certainly coincided with the FARC's demise as a serious military threat to the state.

AP

Cano's no softie

A FARC commander announced that Mr Marulanda died on March 26th of a heart attack. Army chiefs believe that he might have expired as a result of their bombardments. In the same month, two other members of the FARC's seven-man secretariat were killed, Raúl Reyes by a bombing raid on his camp across the border in Ecuador and Iván Ríos by his own bodyguard. Mr Marulanda will be replaced by Alfonso Cano (real name: Guillermo León Sáenz), the FARC's chief ideologue. But there are reasons to suppose that the guerrillas will never recover from their March setbacks.

Mr Marulanda was the last link to the FARC's origins as a peasant self-defence force against landowners, an offshoot of a rural civil war in the 1940s and 1950s between Liberals and Conservatives. A man of peasant cunning and stubbornness, he was said never to have visited any city larger than Neiva, of some 315,000 people. Later recruits were middle-class Marxist students, such as Mr Cano.

The FARC survived the end of the cold war, but at the cost of its ideological purity, by turning to drug-trafficking and kidnapping. Thus fortified, Mr Marulanda was by the mid-1990s leading a force of 19,000 operating in large units, overwhelming army garrisons and threatening Bogotá, the capital. That prompted the government to open peace talks, abandoned after three years in which the FARC carried on kidnapping, bombing and recruiting.

Colombians turned in despair to Álvaro Uribe, their tough president since 2002. He has expanded the security forces by a third, to 270,000, including a core of 80,000 professional soldiers, some of them in mobile brigades and special forces. They are backed by a large helicopter fleet, Brazilian-made Super Tucano tactical bombers and American advice, especially in intercepting communications.

This build-up transformed the war, driving the FARC away from the towns. Recent changes of government strategy are now bearing fruit. These involve encouraging guerrilla desertions and targeting the leadership (partly with intelligence from the deserters). The FARC are now losing more deserters than they are gaining new recruits, according to General Freddy Padilla de León, the armed-forces' commander. “They are reduced militarily, isolated politically, have a reduced social base and we are cutting their finance [by acting against their drug business]. It's impossible for them to return to the cities,” he says.

What has worried Colombian officials most has been signs that Venezuela has been helping the FARC. But Venezuela's government is likely to be more circumspect after evidence of ties emerged from documents on Reyes's computers.

So what future do the guerrillas have? Mr Cano is sometimes portrayed as a moderate, in contrast to

Jorge Briceño (aka “Mono Jojoy”), the FARC's military commander. But in a two-hour interview with *The Economist* in 2001, Mr Cano showed himself to be a rigid Marxist, unprepared to accept democracy. “Our struggle is to do away with the state as now it exists in Colombia,” he said. The FARC wanted power and would not demobilise in return for “houses, cars and scholarships” or a few seats in Congress. That was echoed by Timoleón Jiménez, the guerrilla commander who announced Mr Marulanda's death. He added that the FARC would continue its “struggle for political power”.

Mr Cano's first task will be to assert his leadership and prevent the FARC from fragmenting into its constituent “fronts” in the absence of the unifying Mr Marulanda. Constant army pressure means the fronts now find it hard to communicate with each other. Some, including Mr Cano's in the centre-south, are on the run; others, such as that in Nariño, in the south-west, are still awash with drug money. Yet others rely on havens across the borders in Venezuela and Ecuador.

By maintaining the pressure, the government hopes to force the FARC into negotiations that would see its demobilisation. Relations of hostages kidnapped by the guerrillas hope that the death of the obstinate Mr Marulanda will speed their release. (The hostages include Ingrid Betancourt, a politician with dual French and Colombian nationality, and three American defence contractors.) Neither may happen soon. “Marulanda's death is not the death of the FARC,” says Camilo Gómez, who negotiated for the government during the peace talks. Since perhaps 9,000 guerrillas are still under arms, that is clearly true. But after the events of March, defeat looks only a matter of time.

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Canada

Much ado about not much

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From The Economist print edition

Multiculturalism debated in Quebec

QUEBEC and the defence of cultural traditions have long, and not always happily, been linked in the minds of Canada's English-speaking majority. Now Quebeckers are themselves seeing things from a majority point of view, bridling, in this context, at the claims of immigrants in their French-speaking province. An official commission, however, thinks the complaints are overdone.

Back in 2006 several unrelated incidents led some Quebeckers to think that too much was being asked of them in welcoming immigrants, and too little of the newcomers themselves. A Sikh boy went to court and won the right to wear a ceremonial dagger to school. A gym bowed to a request from Hasidic Jews to frost over windows so the Lycra-clad bodies of women working out wouldn't be visible to their nearby congregation. A man was asked to leave a pool so that a group of Muslim women could swim in private.

These cases were seized upon by a declining Montreal tabloid and by Mario Dumont, the popular young leader of an upstart conservative party. To defuse the issue, Jean Charest, Quebec's Liberal premier, set up the commission and asked two prominent intellectuals—Gérard Bouchard, a pro-independence sociologist, and Charles Taylor, a federalist philosopher—to chair it. This worked politically: Mr Charest scraped back for a second term, though Mr Dumont's party catapulted from four to 41 seats in the provincial parliament, becoming the main opposition.

After a year in which it held endless town meetings and received 900 written submissions, some inflammatory, the commission reported this month. Its conclusions were nuanced and moderate. The crisis was one of “perception”, in which the media had grossly distorted the controversial incidents, the chairmen said. To soothe both sides they made a long list of recommendations. They urge speedier recognition of foreign qualifications to make it easier for immigrants to get jobs (of more interest than cultural accommodation to most). They want the government to coax more of the 45,000-odd immigrants who come to the province each year to settle outside Montreal, in the rural regions where misgivings about migration are highest. And more should be done to ensure that migrants quickly learn French—and more Quebeckers learn English.

The report pleased immigrant organisations but not the original grumblers. They want more stress on making immigrants integrate and conform. “Does it mean that in our daycares, our primary schools and in all milieus we will have to hide our Christmas trees and Easter bunnies in the closet?” asked one of Mr Dumont's aides of a proposal that the Quebec government produce an annual calendar showing holidays of all faiths. No, is the answer. Mr Charest is enjoying a rare spell of popularity, and seems to have no intention of jeopardising it. Even before the report was released, he rejected its symbolic proposal to reinforce Quebec's secular image by removing the crucifix over the speaker's chair in the provincial legislature.

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Argentina

Deadlock

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From The Economist print edition

Angry farmers v an obstinate president

AFP

Farmers, big and small, against taxes

IN BRILLIANT autumn sunshine on May 25th, Argentina's national day, some 200,000 people packed into a riverside plaza in Rosario, Argentina's third city and its farm capital, in the largest anti-government rally in years. The crowd booed every mention of Cristina Fernández de Kirchner, the president, and cheered the country's farmers, who are protesting against her government's decision to raise export taxes.

Ms Fernández had planned to use the national day to announce a corporatist “social pact” on wages, prices and investment. She was forced to change her plans. After comfortably winning a presidential election last year, she succeeded her husband, Néstor Kirchner, on December 10th. Her mishandling of the farmers' dispute, together with rising inflation that is eroding living standards, has curtailed her honeymoon: her approval rating has fallen from 54% in February to just 26%, according to Poliarquía, a polling firm.

The dispute was triggered by the government's decision in March to introduce a new sliding scale of export taxes: the levy on soyabeans rose to 40%, from 27% last year, slashing profit margins. Moreover, the scheme set a virtual price ceiling: if the price goes over $600 a tonne (it is currently $495), the government pockets 95% of the proceeds thereafter. That brought trading in agricultural futures to a halt.

The farmers responded with strikes and roadblocks. In subsequent talks, the government offered sweeteners for small-scale farmers, but refused to reverse the increase. On May 28th the farmers began a new strike, holding back exports and cattle. That may strain public sympathy.

The dispute has undermined confidence in Argentina's economic revival. This month the central bank has spent $1.4 billion to defend the peso, according to *La Nación*, a newspaper, and some money has left the banks. Behind Ms Fernández stands her notoriously obstinate, and still popular, husband. In Rosario they seemed equally determined.

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Economist.com WORLD ASIA

Thailand

Protests and coup rumours return

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From The Economist print edition

Thailand's squabbling elites seem intent on ruining the country

AFP

WHEN an elected government took office in January, after 16 months of military rule, Thailand looked as if it might be returning to stable democracy. The army chiefs who had removed Thaksin Shinawatra's government in a coup in September 2006 accepted being overruled by the public, who voted into office a coalition led by Mr Thaksin's supporters. But political tension is now rising again. Anti-government protests have returned, raising fears that the army might use street violence, or the supposed threats to the monarchy from Mr Thaksin's allies, as pretexts for another coup.

On May 25th the People's Alliance for Democracy (PAD), an anti-Thaksin group, returned to the streets with a rally in central Bangkok. Only a few thousand people turned up, nothing like the masses who poured onto the streets before the 2006 coup and far fewer than the 30,000 the organisers had predicted. But it was enough to trigger a counter-demonstration from Thaksinites, with each side chucking plastic bottles at the other. More protests are promised. The police can contain such minor disorder easily. In 2006, however, similarly small-scale clashes were among the coup leaders' excuses for deposing the elected government.

The protests' return may mark the end of several months of phoney war between the two main camps in Thai politics. On one side are the Thaksinites, led by Samak Sundaravej, the new prime minister. (Mr Thaksin himself has kept a low profile, busying himself with Manchester City, the English football team he owns.) On the other is a fuzzy coalition of conservative and royalist bureaucrats, academics and soldiers, middle-class Bangkokians and the opposition Democrat Party. The Thaksinites believe the guiding force behind their opponents is General Prem Tinsulanonda, the elderly chief adviser to King Bhumibol, though the general denies this.

What has prompted the PAD's return to the streets is Mr Samak's plan to undo some of the constitutional changes made during the former military-backed government. One of these is a measure making it easier to ban a political party. Under this, the Thaksinites' new political vehicle, the People's Power Party (PPP), and two of its coalition partners face disbandment for alleged vote-fiddling in December's elections. Another constitutional change the Thaksinites want to undo is one that legitimised all the coupmakers' actions—including the creation of a powerful panel to investigate corruption allegations against Mr Thaksin. Removing this clause from the charter could get Mr Thaksin off the hook and open the possibility of putting the coupmakers themselves in the dock.

Mr Samak wants to hold a referendum to ask voters if they wish the constitution changed again. He hopes thereby to demonstrate his party's continuing popularity among the poorer, rural majority of Thais and to undermine the claims of his opponents—a group of mostly elite Bangkokians—to be “defending democracy”. This week, despite rising worries about the street clashes, the cabinet backed Mr Samak's plan to hold the referendum.

General Sonthi Boonyaratglin, the former army chief who led the 2006 coup, seems to have gone quietly into retirement. His successor, General Anupong Paojinda, keeps insisting that there is no coup plot—but then so did General Sonthi, right up until the tanks rolled. Mr Samak is said to have built good relations with General Anupong, perhaps as a hedge against being dumped by Mr Thaksin. This might make a coup less likely. However, lower down the army's ranks Mr Thaksin has both supporters and diehard opponents, any of whom might conceivably hatch their own plots.

The anti-Thaksin movement's language, accusing the government of “divisiveness”, sounds much as it did in the build-up to the last coup. So do its accusations of *lèse-majesté*. Mr Thaksin's supposed disrespect for the king was yet another of the coupmakers' excuses, though they failed to produce any evidence of it. Now the same accusations are being made against Jakrapob Penkair, a minister in Mr Samak's government, over a speech he gave to foreign correspondents last year about Thailand's “patronage system” and how it hinders the country's development. The anti-Thaksinites interpret this as criticism of the monarchy, an offence punishable by 15 years in jail.

Mr Jakrapob is correct that the system under which Thais owe loyalty to their patrons, rather than the institutions they are supposed to serve, undermines the rule of law and fosters corruption. That said, Mr Thaksin's government, far from ridding Thailand of this feudal mindset, was busy creating its own patronage system. Whether the patronage mentality derives from the monarchy or not is something Thais surely have a right to discuss. The king has said he would accept criticism. But it suits the conservative establishment to retain the severe *lèse-majesté* law as a weapon against anyone who threatens their privileges.

After the 2006 coup the army and its allies in the bureaucracy ran the country dismally, and Thailand's economy is now among the region's slowest-growing. Even so, both sides in the conflict are talking up the chances of another coup—which would be the country's 19th since the absolute monarchy came to an end in 1932. Even if it does not go that far, prolonged political strife risks doing further economic damage. Instead of regaining its reputation as an admired, fast-developing tiger, Thailand risks becoming one of those perennially unstable, tragi-comic countries, such as the Philippines, which the outside world overlooks.

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Nepal

Goodbye to all that

May 29th 2008 | KATHMANDU
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The abolition of the monarchy may be the easy part for Nepal's government

AP

Off with his crown!

AT 6.15pm the fountains were switched on. The water danced. The white-clad military band stood to attention. And waited. And waited. After 239 years of rule by the Shah royal dynasty, perhaps it was inevitable that the last few hours of waiting for the monarchy to be abolished and a republic set up should also be long and drawn-out. When the announcement came, it was greeted with cheers. Three bombs had gone off earlier in the day. Yet all things considered, the decision, momentous as it was, sparked neither bitter complaint nor intense celebration.

Perhaps the long period of violence and uncertainty beforehand had something to do with it. Nepal has seen a decade-long civil war; two postponed elections; a massacre of the royal family; the grabbing of absolute power by the king and the handing back of it again; and most recently, victory in elections by Maoist former guerrillas. Nepalis could be forgiven for being uncertain of what lies in store.

The country's constituent assembly voted to abolish King Gyanendra's house by 560 votes to 4. The king's unpopularity, among assembly members and the ordinary Nepalis who elected them in April, was well earned. In 1990, his brother, King Birendra, bowed to popular demands and became a constitutional monarch, attaining respect and affection as a result.

When the Maoists began their insurrection in the western hills in 1996, getting rid of the crown was not on their agenda. Yet Gyanendra alienated supporters by grabbing dictatorial powers in 2005, only to be forced to hand them back again after a clumsy attempted crackdown turned peaceful protests into nationwide strikes. Most Nepalis believe—without any evidence—that Gyanendra and his unpopular playboy son, Paras, were involved in the royal massacre of 2001 when Crown Prince Dipendra killed his immediate family, several other relatives and himself.

The royal family was once revered as the reincarnation of Hindu gods. But the massacre undermined faith in the monarchy in general, and turned Nepalis against this king in particular. Before he ascended the throne, Gyanendra had been a successful businessman. He will be allowed to stay in Nepal and return to commerce. His palace will become a museum.

But for the man who engineered the king's departure, tougher choices lie ahead. This is the leader of Nepal's Maoists, Pushpa Kamal Dahal, better known as Prachanda, which means “awesome”. Prachanda has long said he would become the first president of a Nepalese republic. He stands on the brink of achieving that ambition. His problems start then.

The Maoists are the biggest party, but do not have a majority. Nepal is led by a fractious coalition, which the Maoists want to widen by including regional parties from the south and south-east. That may make managing the coalition trickier.

The abolition of the monarchy is a first step in a much wider reform. Laws and even customs deemed to go against the country's status as a republic are to be repealed. Many politicians who supported Prachanda's demand to abolish the monarchy will not necessarily back proposals for what should replace it. For example, the parties of the south and south-east want extensive regional autonomy. Prachanda seems unlikely to give it to them.

He will also have to get to grips with the aftermath of the civil war. The former royal army is 90,000-strong. Nepal also has 23,000 Maoist ex-combatants kicking their heels in temporary camps. The Maoists want to merge the two forces. The army's high command is reluctant.

Then there are economic and social promises to fulfil. The Maoists want to push through land reform, emancipate the lower castes and seek foreign investment. With growth slowing, that would be hard enough by itself. Uneasy lies the head that wears a crown—and the breast that sports a presidential sash.

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Taiwan's charities

Help with a bow

May 29th 2008 | TAIPEI
From The Economist print edition

An unexpected bringer of relief in Myanmar and China

EPA

Taiwan to the rescue

THE natural disasters that recently befell Myanmar and China have tested the willingness of both stricken countries to let in foreign helpers. Western relief organisations are still waiting to see whether Myanmar's armed forces meant what they said when they promised to let in all aid workers, regardless of nationality. China, though quick to accept money and material from the West, was slower to let in its people. But whereas Western do-gooders have queued for entry, volunteers from Taiwan's non-governmental organisations (NGOs) received a warmer welcome. A chartered relief mission from Taipei, led by a Burmese-born Buddhist monk, was among the first to land in Yangon, Myanmar's main city. In China, emergency workers from a Taiwanese foundation were among the first to reach Sichuan. This first-responder feat is all the more remarkable given the political impasse between China and Taiwan.

Disaster relief plays to the strengths of Taiwan's NGOs. They have plenty of experience coping with earthquakes and typhoons at home, and can mobilise legions of volunteers at short notice. Operating in a vibrant democracy that encourages civil society is also handy, as is the charitable impulse of many Taiwanese. This is often channelled into Buddhist philanthropy, which troubles receiving countries less than the proselytising zeal that comes attached to some brands of Christian charity. Paradoxically, Taiwan's diplomatic isolation helps: its aid agencies can plead neutrality in countries such as Myanmar.

The largest NGO in Taiwan—and by all accounts in the Chinese-speaking world—is the Tzu Chi Foundation, which has dozens of international chapters, around 10m supporters and annual donations of $300m. In Taiwan it runs hospitals, schools, a university, recycling centres and one of the world's largest bone-marrow banks. It began overseas relief work in 1991, responding to flooding along China's Yangzi river. Initially, its offer of help got a cool response from both sides of the Taiwan Strait. Critics at home asked why they wanted to aid “the enemy”. Eventually both sides relented, and China is now the biggest overseas recipient of Tzu Chi's low-key largesse. Earlier this year, it finally got a licence to operate freely as a 100%-foreign NGO, a first for China, it claims.

With projects in dozens of countries, Tzu Chi is starting to resemble its Western counterparts, except that its aid workers are trained volunteers who pay their own way to disaster zones. Master Cheng Yen, a Buddhist nun who founded the organisation in 1966, teaches that charitable givers must thank those they help in person, preferably with a bow. That is not just a wonderful bit of courtesy. It is also a way to make sure that aid reaches its recipients, rather than ending up in the hands of an unworthy government.

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Economist.com WORLD ASIA

Australia's skills shortage

Give us your huddled masses, mate

May 29th 2008 | SYDNEY
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Where immigration is still booming

Get article background

LAST time Australia's airlines turned to other countries to recruit large numbers of pilots, the year was 1989 and they were trying to break an unprecedented strike by their own pilots. But when Jetstar, a low-cost carrier, revealed recently that it was planning to hire more than 75 pilots from Britain, America and South Africa, it was seeking a solution to a problem facing many employers across the country: a severe shortage of skilled labour.

With an economy in its 17th year of uninterrupted growth, Australia's skills shortage has never been worse. People are crying out for plumbers, doctors and nurses. In states that are booming thanks to a mining bonanza—Western Australia, Queensland and South Australia—engineers, surveyors and truck drivers are in short supply. One state-owned water authority complains that it is losing truckers to mining companies offering A$100,000 ($96,000) a year—more than double their previous salary.

In many rich countries where immigration is a politically sensitive matter—America, Britain and Ireland—the number of immigrants seems to be falling as the economy turns down. Not in Australia. The Labor government, under Kevin Rudd, is looking to increase the numbers of foreigners allowed to settle. His predecessor, John Howard, the former conservative leader, had already begun to increase the number, but had to pretend otherwise, since his party claimed to put “Australia first”. Mr Rudd is playing up the increases. On May 13th his government said that Australia would take 190,300 immigrants next year, a rise of 25% on this year. The biggest jump comes in the proportion of those chosen for their skills in a booming economy: at 133,500 they now account for a record 70% of the total intake.

These so-called “permanent” settlers tell only part of the story. With another 100,000 arrivals expected under a short-term visa scheme that allows employers to fill urgent job vacancies from outside Australia, the total intake is likely to be closer to 300,000. Other changes will make still more foreigners available for work. The government is abolishing a restriction enforced by the Howard government that meant illegal immigrants later found to be refugees could get only temporary permission to stay in Australia. And it is thinking about letting in guest workers from Pacific Island nations—a measure used successfully in New Zealand and which Mr Howard sternly opposed.

The latest annual figures are the highest since Australia launched an immigration programme soon after the second world war. They also signal something of a revolution in the way Australia tackles this politically charged issue. Originally, immigration was a way to populate a big, empty country with “ten-pound Poms”, Britons who paid just £10 (then $27) to start a new life down under.

That approach, says Chris Evans, the immigration minister, was designed for a world in which people did not move much. Today, he argues, the country needs a policy fit for a world in which people move often for work. He points out that 500,000 people with “work rights” entered Australia last year: students and holiday-makers, as well as those on work visas. And the country still suffers skilled-labour bottlenecks.

Australia is in some respects paying a price for failing to invest in skills and infrastructure to meet the demands of what the Treasury calls a “once-in-50-years boom”. Not long ago, the sight of a Labor government bowing to demands from bosses and opening the gates to foreign workers would have produced howls of anguish from unions. Not now. With unemployment at a 30-year low, falling union membership and an ageing domestic workforce, the Rudd government can afford to be bold about using immigration as a tool of economic management. Mr Evans says that from now on immigration will play a bigger role in the “structure of Australia's workforce”. He can probably count on Australians tolerating that—so long as the boom continues.

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North Korea's new rich

How the other 0.0000001% live

May 29th 2008 | PYONGYANG
From The Economist print edition

The hermit kingdom's elite spend, spend, spend

EVERY developing country worth its salt has a bustling middle class that is transforming the country and thrilling the markets. So does Stalinist North Korea. Oblivious of rumours that famine is gathering again and that the state's food-distribution system is breaking down, the country's pampered elite went on a shopping spree at the Pyongyang Spring International Trade Fair, held on May 12th-15th.

Originally designed to promote business-to-business contacts, the trade fair, along with a companion event in the autumn, has become one of the few opportunities for North Koreans—or, more accurately, a few thousand residents of the capital—to buy, or gawk at, foreign merchandise. More than 100 Chinese companies, together with some from Taiwan, Indonesia, Britain and North Korea itself, offered up everything from T-shirts to heavy machinery. Cutting-edge technology it wasn't. Duvets, refrigerators, flat-screen televisions, DVD players, cooking pots and cosmetics were the most popular items. More than 15 units of one of the show's most expensive items, a $1,200 refrigerator from Haier, a Chinese company, were snapped up. Counterfeit iPods were also popular, even if downloading is illegal.

North Korea's new rich make their money from political connections. But one shortage they don't seem to face is that of American dollars. The main sources of foreign exchange—apart from counterfeiting (fake $100 bills circulated at the fair)—are foreign trade and North Koreans' relatives abroad, particularly those in South Korea and Japan. Kim Kwang-jin, a senior research fellow at the Institute for National Security Strategy in Seoul, estimates that $50m-60m in American currency circulates in the hermit kingdom, based on a survey conducted at the behest of the “dear leader”, Kim Jong Il, in the late 1990s.

In pursuit of the country's goal of becoming a net exporter, around 40 local enterprises also displayed their wares, including medicines, oil paintings, machinery, spectacles and a polarised-light device that the makers claimed could cure any disease. But it was the imports that galvanised people's inner shopper. A billboard at the entrance trumpeted the slogan “Building an Independent National Economy” and included numerous photographs of Kim Jong Il and his father inspecting farms and factories, a reminder to visitors of the all-embracing love and compassion of the Kim family. As the shopfest ended, however, some North Koreans refused to leave, demanding that the event's organiser allow them to continue their buying spree. The dear leader's love apparently wasn't enough.

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Economist.com WORLD ASIA

India's Maoists

Sentence first, verdict afterwards

May 29th 2008 | RAIPUR
From The Economist print edition

India's anti-Maoist laws become an international embarrassment

HOTEL MAHENDRA, in the capital of the Indian state of Chhattisgarh, seems an unlikely spot from which to hatch a plot against the government. It is a humdrum hotel overlooking the city's jail. But, according to state prosecutors, it is one of the places where Binayak Sen, a celebrated doctor and human-rights activist, conspired with Chhattisgarh's Maoist insurgents. The doctor, whose trial began in April, has now spent over a year detained on the other side of the prison wall.

Tribulation, but not a trial, for Dr Sen

Dr Sen worked in the remote reaches of Chhattisgarh, one of several places where India's Maoists (known as Naxalites) hold sway, raiding police stations, sabotaging telecom towers and intimidating villagers. He helped set up a hospital for miners and trained community health-workers. He is also an official of the People's Union for Civil Liberties (PUCL), which campaigns against human-rights abuses. He became a vocal critic of the government's strategy of arming and mobilising villagers against the Naxalites, thereby relying on vigilantes to quell an insurgency which the state itself has failed to end.

Dr Sen was charged under both the national penal code and a sweeping state law. The Chhattisgarh Special Public Security Act criminalises a broad array of dealings with unlawful organisations, including the Communist Party of India (Maoist), the main Naxalite party.

Dr Sen's alleged crime was to pass on letters from an imprisoned Naxalite leader, whom he treated in the city jail. According to PUCL, the law has also been used against two cloth merchants for providing “camouflage” uniforms, two journalists, and a doctor whose prescription was found on a Maoist. The union describes the measure as a draconian law that relies on guilt by association. PUCL is disputing the law's constitutionality in the Indian Supreme Court. It filed its petition on May 14th, the anniversary of Dr Sen's arrest last year.

The state may well struggle to prove its case against the doctor. His meetings with Naxalite inmates were supervised and approved by the prison authorities. The manager of the Hotel Mahendra, called as a prosecution witness, turned hostile on the stand. But perhaps the state does not really need to convict Dr Sen. He has now spent more than a year imprisoned without bail. The next hearing is not scheduled until late June. The authorities have shown all too clearly that they can punish people under their “special” law without having to prove their case in court.

But if the act was intended to keep Chhattisgarh's troubles out of the media, it has backfired spectacularly. Dr Sen's case is becoming a *cause célèbre*, championed by 22 Nobel prizewinners, who signed a letter to the prime minister in May calling for his release. In April Dr Sen won the Jonathan Mann award for global health and human rights. The prize-giving ceremony will take place in a luxury hotel in Washington. Meanwhile, Dr Sen will remain in his wretched cell, in the shadow of Hotel Mahendra.

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Israel

The prime minister is tottering

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From The Economist print edition

Is time finally up for Israel's Ehud Olmert?

Getty Images

GO, OR we'll make you. That was the message this week to the prime minister, Ehud Olmert, from his close colleague in the governing coalition, Ehud Barak, leader of Israel's Labour party and minister of defence. Mr Barak had not intended to force such a choice on Mr Olmert after the latest in a series of corruption scandals engulfed the prime minister. But the wave of outrage following revelations in court by an American businessman, Morris Talansky, took the Labour leader by surprise. The prime minister is under mounting pressure to step down.

Mr Talansky testified that over the course of 14 years he had given Mr Olmert, first as mayor of Jerusalem and later as a government minister, around $150,000 in cheques, cash and payments of bills that Mr Olmert had run up. Mr Talansky says most of the money was to finance campaigns for Mr Olmert, but at least $40,000 was in personal loans never paid back.

Prosecutors originally said they were investigating Mr Olmert for bribery. They are now being more cautious. Though they allege that Mr Olmert did Mr Talansky some favours in return, proving bribe-taking will be hard. A charge of tax evasion, though, is starting to look more likely. The emerging tales of first-class flights, expensive gifts and plush hotel rooms are shredding Mr Olmert's reputation. The stench of wrongdoing that has long hung over him may now become unbearable even for Israel's jaded public.

Mr Barak, as leader of the second party in Mr Olmert's coalition, can bring the government down. But Labour trails in the polls and may be weakened further if Ephraim Sneh, a parliamentarian who left the party this week to form his own, manages to lure away a few of its members. Opinion polls suggest an election would be won either by Tzipi Livni, currently foreign minister, if she took over from Mr Olmert as leader of his centrist Kadima party, or by Binyamin Netanyahu, leader of the right-wing opposition party, Likud.

Mr Barak wants Mr Olmert to resign so that someone else in Kadima, most likely Ms Livni, could take over without an election. He hopes Kadima's members will oust Mr Olmert rather than risk a new election, in which some of them might lose their seats. However, Mr Olmert is resisting. And Mr Barak, to give himself flexibility, has not set a deadline, so Mr Olmert could survive a few months more.

If there is an election, Labour might still get into the next government by striking a deal with Likud. Such odd bedfellows are not rare in Israeli coalitions; there is bad blood between Likud and Kadima, which previously split from Likud and took some of its best people. It is a reasonable gamble for Mr Barak. Having reneged on a promise to quit the government after the damning inquiry into Mr Olmert's handling of the Lebanon war in 2006, he would look a fool not to take a stand this time.

The irony is that Mr Olmert has recently made some notable diplomatic strides. Besides the peace talks with the president of the Palestinian Authority (PA), Mahmoud Abbas, he has begun indirect negotiations with Syria, though Israeli leaders have usually been loth to do both at once. He has also been holding indirect ceasefire talks with Hamas, which controls the Gaza Strip. And he now seems close to a prisoner exchange with Lebanon's Hizbullah to bring back the two Israeli soldiers whose abduction sparked the 2006 war, though whether alive or dead is unknown.

What would happen to these initiatives if Mr Olmert were to go? The timing of the Hizbullah deal, coinciding with the Talansky affair, made some Israelis suspect it was a deliberate distraction. A Syrian peace would require Israel's departure from the Golan Heights and co-operation from the currently sceptical Americans, so it is not an immediate prospect. The idea of a ceasefire with Hamas has wider support, not least in the defence establishment, though it might be short-lived.

As for the talks with Mr Abbas, expectations are already low: the two sides have made little obvious progress and are no longer aiming for a full-fledged peace deal, the goal when the talks were launched in Annapolis in November. Both Mr Olmert and Mr Abbas look too weak to make the concessions needed for an agreement. And even if they did, the deal could not be implemented against Hamas's wishes. Yet Mr Olmert and Mr Abbas at least seem to get on well. Palestinians who deal with Ms Livni in the current negotiations say she is harsher. And Mr Netanyahu says that now is not the time to hold talks at all.

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The Palestinian economy

It all depends on the politics

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From The Economist print edition

A big investors' conference has created goodwill, but it won't reduce the Palestinian economy's reliance on aid and its need for a lasting peace

Illustration by Peter Schrank

FOR anyone with an image of Palestine as a place of misery and conflict, the recent Palestine investment conference in Bethlehem was impressively hopeful—perhaps falsely so. Some 2,000 people packed into the opening session were soon drenched in sweat as the air-conditioning struggled. For the next two days they swarmed in and out of sessions on high-tech, construction, tourism and financial services, and huddled in every corner to talk over business opportunities. Pragmatism filled the air; whenever the Israeli occupation came up, the usual refrain was: “We know the conditions. Let's talk about how to work around them.”

Officially, the conference exceeded its goals. An unusually co-operative Israel granted visas to some 550 mostly Arab business people. Local entrepreneurs produced business plans for over 100 projects worth some $2 billion, ranging from housing developments to high-tech services to a scheme for generating power from household waste. At the end, the organisers said that deals worth $1.4 billion had been struck during the conference.

But those figures are deceptive. Most of the deals, such as a $650m investment by a new mobile-telephony firm, Wataniya, and the $350m to build Rawabi, a new town in the West Bank, had been agreed on long before. Of the foreign visitors, more than half were diaspora Palestinians, many probably seizing a rare chance of a visa to visit their families and homeland rather than to launch new ventures.

The meeting's heart was in the right place. Salam Fayyad, the prime minister of the Palestinian Authority (PA), and Muhammad Mustafa, head of the Palestine Investment Fund, which manages the PA's investments, have been trying to wean Palestinians off their massive dependence on aid by encouraging entrepreneurship. Mr Mustafa has arranged complex coalitions of local and foreign investors, banks and foreign donors to create such things as a small-business development fund, a mortgage fund aimed at young couples, and housing and commercial developments like Rawabi. Mr Fayyad is also trying to slim the bloated PA payroll. To help do so, foreign donors recently pledged $7.7 billion in aid to the PA for the coming three years, more than ever before.

At least some outsiders see the potential. Muhammad Ahmed bin Abdul Aziz, an official from the United Arab Emirates economy ministry, who brought a UAE delegation, describes Palestine as an “untapped market”. Since it has among the highest rates of literacy and education in the Middle East, it could perhaps come to provide back-office services over the internet for the Arab world, the way India does for the English-speaking world.

Thanks to the young population and Israeli restrictions on building in much of the occupied territories, there is also huge demand for cheap housing. The number of hotel guests has recovered almost to the levels before the *intifada*, or uprising, began in 2000; what holds tourism back now is as much the lack of hotel rooms and facilities as worries about safety.

Arab consciences tweaked

Some people are willing to invest in Palestine just because it is Palestine. Ghanem bin Saad al-Saad, the CEO of Qatari Diar, co-builders of Rawabi, admits that the project is more a “symbolic” than hard-headed business deal. The IMF estimates that a combination of PA reforms and investment projects could return the economy to strong growth by the end of 2009, after a 2% drop in GDP since 2000.

But that is only if Israel at the same time eases the restrictions on movement that stifle the Palestinian economy; otherwise, predicts the IMF, GDP will continue to fall. So far there is no sign of a let-up. The number of checkpoints and roadblocks in the West Bank has increased by some 10% since Israel undertook to reduce them at the Annapolis peace conference in November. Even when it has promised the PA that it will remove specific checkpoints, in most cases it has not done so.

Businessmen are sceptical that Israel will grant visas to Arab visitors again as willingly as it did for the conference. Some donors, particularly Arab ones, have been holding back the money they promised the PA in December because they do not want it to go to waste.

Tony Blair, Britain's former prime minister, who has been mediating between Israel and the PA to unblock particular projects, such as industrial parks, has largely run into a brick wall too. Though he announced a list of successes earlier this month, some of them have not actually been fully agreed, say officials familiar with the talks; Mr Blair has achieved true breakthroughs in only a couple of cases.

In some others the success is mixed. The cellular frequency band that Israel allocated to Wataniya, after over a year of wrangling, is far too small for it to compete seriously with existing firms, and company officials are not confident that Israel will grant a wider spectrum within a few months, as it says.

Besides, Palestine is not the only place clamouring for business. Across the Arab world governments are shaking off bureaucracy and wooing investors; and, unlike the PA, they are fully in charge of their own territories and borders.

Above all, many business people are waiting for the outcome of peace talks between Israel and the PA before committing themselves. “We are investing very little at this time,” says Samer Khoury of the Consolidated Contractors' Company, a Greek firm founded by diaspora Palestinians, which has spent some $200m in Palestine since the Oslo peace accords of 1993. “We are waiting to see if the peace process does develop into a framework agreement,” as it is meant to by the end of the year. If it does not, he foresees little growth beyond building projects. And if a corruption scandal brings down Ehud Olmert, the Israeli prime minister, it may hamper the already shaky negotiations.

So a lot of Palestinian businessmen fear the conference will have served as little more than political window-dressing. America wants the economy in the West Bank to flourish so as to boost Mr Fayyad and his boss, Mahmoud Abbas, the Palestinian president, over the Islamist Hamas movement which runs Gaza. Israel is meant to have the same aim, but because of fears about security it has usually blocked the moves needed to achieve it.

The Bethlehem conference was an exception to that rule. But if it remains the exception, its achievements may all too easily be wiped out.

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Lebanon

The prospect of a wider peace

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If Lebanon's latest deal holds, why not bring in Syria and Israel?

JUST two weeks ago, Lebanon was on the verge of civil war. Suddenly, it seems to be on the brink of a lasting peace. And just as Lebanon's own troubles reflected wider tensions in the Middle East, the fractious country's sudden mood of conciliation is sending positive ripples through the region. At least, that is how things appear on the surface.

Following a deal cut on May 23rd in Qatar between Lebanon's bickering factions, Lebanon's parliament swiftly voted into office a new president, a 59-year-old former army chief, General Michel Suleiman. The second part of the deal looked well on the way to being fulfilled, as faction leaders were poised to name ministers for a new cabinet of national unity.

After Syria and Israel, the bigger neighbours who have often sparred for control of Lebanon, confirmed whispers that they had begun talking, Syria's President Bashar Assad even suggested that at some point Lebanon should join in. Meanwhile, Hizbullah, the Lebanese Shia party-cum-militia that started the clashes three weeks ago, revealed that it is close to clinching a deal to trade two Israeli soldiers it holds with five Lebanese men jailed in Israel.

That would be a big breakthrough, considering that Hizbullah's capture of the soldiers, with the intent of using them as bargaining chips for such a swap, sparked a 33-day war with Israel in 2006. There has even been some optimistic talk of an emerging regional bargain, with America and Iran, instead of egging their proxies on to fight, letting them come to terms.

Yet severe doubts linger, in Lebanon and at large. The Hizbullah leader, Hassan Nasrallah, tried to answer them in a conciliatory speech, asserting that despite its swift and violent takeover of Sunni districts in Beirut earlier this month, his Iranian-backed party had no intention of imposing its rule. Every weapon in the country, he said, should “remain in the service of the goal for which it was intended”: defending Lebanon against outsiders (ie, Israel), and not settling internal squabbles.

But he insisted that his “resistance” retained a sacred right to bear arms. Some of his enthusiasts celebrated the speech by riding into Sunni quarters and shooting in the air, sparking violence that injured 16 people. A day later, fighting between Hizbullah fighters and Druze villagers left a soldier dead. Lingering ill-will, especially among Sunni militants who felt humiliated by the Shia show of force, leads many Lebanese to expect more such incidents.

“Ultimately, only a regional deal can get the Lebanese to fix the hard and messy issues, like Hizbullah's guns and how to build a non-sectarian state,” says a diplomat in Beirut. Given the fragility of Israel's government, the reluctance of Israelis to surrender territory in exchange for peace with Syria, and Syria's refusal so far to meet Israeli demands that it drop its alliance with Iran and end support for groups such as Hizbullah, a regional deal looks hard to strike in the near future. But at least its outline looks clearer.

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Iran

Smoke and mirrors

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Iran makes it hard even for benevolent outsiders to understand it

THROUGHOUT its 29 years, the Islamic Republic has puzzled, even baffled, observers. Its leaders proclaim peace and war in the same breath, and pretend to practise both democracy and theocracy. But lately the symptoms of schizophrenia have grown more pronounced.

When the International Atomic Energy Agency (IAEA), the UN's nuclear watchdog, issued a report on May 26th casting doubt on the peaceful nature of Iran's nuclear plans, Iran's diplomats first said it proved their government's goodwill. Then they said they had already answered questions raised in the report. Finally, Iran's new parliamentary speaker, Ali Larijani, himself a former nuclear negotiator, attacked the agency for alleged deceit, charging it with secretly sharing information about the nuclear programme with Iran's enemies. Iran may be forced to reconsider co-operating with the IAEA, he suggested.

After an explosion killed 12 worshippers at a mosque in the southern city of Shiraz in April, officials hastily declared it an accident. Two weeks later, they blamed terrorists, and have since charged a dozen people as plotters variously linked to America, Britain, Israel and exiled monarchists. Some Iran watchers ascribe the flip-flop over the explanation to a desire to divert attention from the fact that Ayatollah Ali Khamenei, Iran's supreme leader, had been due to visit the city. Others tie the blast to the arrest of six leaders of Iran's 300,000-strong Bahai religious minority, noting that the targeted mosque was a venue for fierce anti-Bahai sermons.

Iran's president, Mahmoud Ahmadinejad, proclaims himself a champion of the poor and keen to reform the administration. But his spendthrift social policies have sparked painful price rises, say critics, while his shake-up of the bureaucracy has punished competent people and rewarded cronies. This blunderbuss approach has fiercely divided his fellow conservatives, so sowing more confusion. Moreover, the newly elected parliament still has a minority of obstreperous moderates.

The country's foreign policies look erratic, too. Iran has condemned jihadist terrorism, but sheltered al-Qaeda fugitives. It has backed the government of Iraq's prime minister, Nuri al-Maliki, yet has abetted militias opposed to him. It champions Muslim unity but creates division by vilifying pro-Western Muslim rulers, backing Shia factions and expecting Shias everywhere to bow to Mr Khamenei's authority.

Earlier this month, Iran's foreign minister announced an initiative for a wide-ranging dialogue with the UN Security Council, which has imposed sanctions on Iran over its nuclear programme. But amid protestations of working for world peace and solidarity between peoples (bar Israel, whose end Iran predicts and desires), the initiative proposed little new. This raised speculation that it was meant either to pre-empt an expected move by the Security Council to ramp up sanctions or simply to dampen criticism at home by creating an impression of diplomatic movement.

Such behaviour frustrates those, both Iranians and outsiders, who want Iran to enjoy more normal relations with the world. Yet for all the confusion of smoke and mirrors, the arch-conservatives controlling Iran have succeeded rather well. They have purged the government of rivals, cowed liberal critics, punished America in Iraq, basked in reflected glory via the success of their proxy, Hizbullah, in Lebanon, and pushed ahead with their nuclear plans. Along with talk from Western diplomats of tougher sanctions come whispers of an offer of bigger rewards to Iran, should it stop short of building a bomb.

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Chad

Relying on outsiders

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How the fates of President Idriss Déby and Darfur's refugees are intertwined

THESE days, the daily Air France flight from Paris to Chad's capital, N'Djamena, offers a neat summary of the country's problems and opportunities. About one-third of the passengers are foreign troops, the rest an eclectic mix of aid workers, Chinese businessmen, assorted oil workers and missionaries. As in Congo to the south and Sudan to the east, Chad is now the recipient of an influx of peacekeepers and aid, both trying to stop the country falling apart almost as fast as an inept government tries to get rich extracting the country's minerals and oil.

The difference is that President Idriss Déby's looks a lot wobblier than his Congolese or Sudanese peers. A coup attempt in February almost forced him out; the insurgents were turned back literally at the gates of the presidential palace. No one in Chad is betting against the rebels having another go, even as soon as June, before the rainy season.

With little to show for his 18 years in power, Mr Déby is the main author of his own misfortunes. Chad and its 10m people still bump along near the very bottom of most international indices of development and poverty reduction. Its situation is worsened by its proximity to the dreadful violence of Darfur, the battered Sudanese region just across Chad's eastern border. Chad's rebels are backed by Sudan's government, which lets them use Darfur as a base. In the past four years eastern Chad has had to accept more than 250,000 Darfuri refugees from the fighting between rebels in Darfur and Sudanese government forces. This year 10,000-15,000 have arrived. Some huddle in the open, waiting for tents, before joining thousands of others already in camps such as Gaga, near the town of Abéché.

Now, however, Chad could benefit from a new international commitment to help Darfur. While the UN is starting to deploy a planned 26,000-strong peacekeeping force in Darfur, in recent weeks hundreds of European soldiers and UN people have arrived in eastern Chad to protect Darfuri refugees there. In addition, there are 60,000 refugees from fighting in next-door Central African Republic, plus 180,000 internally displaced Chadians.

The European force, known as EUFOR, and the UN Mission in the Central African Republic and Chad, known as MINURCAT, are meant to work together to protect both refugees and humanitarian workers from attack. Unlike the UN force in Darfur, which is obstructed at every turn by a hostile Sudanese government, EUFOR is well-funded and deploying rapidly. At Camp Europa, outside N'Djamena, 2,700 troops have already arrived; the figure should rise to 3,700 by July. It has plenty of vital attack and transport helicopters, from Russia, Poland and France.

But MINURCAT should make more of a difference. Its mandate is to train some 800 Chadian policemen to guard the refugees. It will also send teams of lawyers and human-rights experts to tackle Chad's biggest problem: its lack of law and the impunity with which crimes are committed. Chad's justice system barely functions. Bandits are responsible for most of the rising number of attacks, some of them deadly, on aid workers and refugees in the east.

Indeed, most aid workers say that EUFOR is the wrong kind of force for eastern Chad, since it is over-armed to take on mere bandits yet has no mandate to fight the more heavily armed Chadian and Sudanese rebels who criss-cross the border, displacing more and more civilians.

Be that as it may, the two new forces are strong symbols of a fresh resolve to help Darfur. Maintaining stability in Chad is very much part of that strategy, even if it means propping up Mr Déby. Any alternative, such as letting Chad's quarrelsome and unpredictable rebels take over, would disrupt the flow of humanitarian assistance to the refugees and risk letting many thousands more die. France, Chad's former colonial master, keeps troops and fighter-bombers there and helped rescue its embattled president in February, on that occasion with the UN's open support.

But Mr Déby does not quite get a free pass. He has been persuaded to form an “inclusive” government, embracing four opposition ministers. Foreign donors hope it will use Chad's growing oil revenues better. They also pin some hope on a new prime minister, Youssouf Saleh Abbas, an easterner who at least talks the talk of ending Chad's lethal culture of impunity.

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Japan and Africa

Catching up

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It's sushi for Africa's leaders

THE copper is used in computers. The nickel is for batteries. Tungsten is used to fortify steel for cars. Japan buys much of its rare metal from China to feed its electronics and car industries. But as booming China has begun to close the spigot to safeguard its own supplies, Japan, the world's second biggest economy, has been forced to look elsewhere for an alternative source—in Africa.

On May 28th it hosted the Tokyo International Conference on African Development, a quadrennial event since 1993. About 40 African heads of state or government attended. Japan's prime minister, Yasuo Fukuda, promised to meet each one individually, as well as Bono, a pop singer, without whom no such gathering on Africa is complete.

But whereas in previous meetings aid topped the agenda, this time it has been all about the hunt for natural resources—with Africa's best interests at heart, of course. “If we are able to utilise Africa's plentiful resources more fully by harnessing Japan's technologies,” Mr Fukuda said, “this will surely be a major trigger for growth and without a doubt benefit Africa.”

This has become a familiar refrain from the leaders of Asia's other expanding economies. Japan is following firmly in the footsteps of China and India, both of which have hosted lavish African summits in the past 18 months, both of them keen to buy Africa's oil and metals.

Like the others, Japan is offering sweeteners to make itself a saucier commercial partner. This week it pledged to double aid to Africa by 2012, to $3.4 billion. It will also provide up to $4 billion in low-interest rate loans, which means easing its rules against lending to countries that have previously received debt relief.

Japanese officials stress that all this comes with no strings attached (except perhaps Africa's support for a permanent Japanese seat in the UN Security Council), a not-too-subtle hint that the country hopes to compete on an equal footing with China. Its loans are never linked to improvements in governance or human rights, unlike many of those from Europe, which hosted its own Africa summit in Portugal last December, or America. This reflects the fact that Japan has come late to this second scramble for Africa—and knows it.

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Ukraine's government

A political soap-opera, continued

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The politicians fight among themselves, and liberalising reforms cease

AP

WELCOME to the latest episode of Ukraine's political soap-opera, starring Yulia Tymoshenko as prime minister and Viktor Yushchenko as president. Here is the plot so far. Ms Tymoshenko, the white-clad heroine of the "orange revolution", reunites with Mr Yushchenko and scores a famous victory in a parliamentary election last October. The "villain" (and former prime minister), Viktor Yanukovich, is defeated and recedes into the background. After three months of bargaining Ms Tymoshenko becomes prime minister and forms a coalition government.

Then Mr Yushchenko gets jealous of his more popular partner. Instead of letting her run the government as he promised, he starts interfering in almost every decision and publicly scolding Ms Tymoshenko. She tolerates this humiliation for several months, then explodes.

On May 13th Ms Tymoshenko's party blocked the podium to stop Mr Yushchenko addressing the Rada (parliament), the first time a parliamentary majority has done this. Enter a supporting character: Viktor Baloha, the president's chief of staff, who is plotting against the coalition and accuses Ms Tymoshenko of building a "fascist regime". The episode ends with the orange alliance at breaking-point—and a paralysis of decision-making in Ukraine.

The country has two heads of the state property fund, but neither achieved any privatisations. Ms Tymoshenko and Mr Yushchenko have not spoken for six weeks; both are said to have talked to Mr Yanukovich instead. In the meantime, inflation is approaching 30%, corruption is thriving and reforms have stalled.

Few ideological differences separate Mr Yushchenko and Ms Tymoshenko. Both want Ukraine in the European Union and NATO, both advocate a free-market economy. When they work together, they can be effective, as they were in bringing Ukraine into the World Trade Organisation. But with a presidential election due by the end of 2009, short-term political manoeuvres now take precedence.

In truth, rivalry and squabbles have haunted Ukraine ever since the orange revolution. But because the economy has been doing well, most Ukrainians have paid little heed. Now this luxury is disappearing. One reason why inflation is so high is that Ukraine's central bank, which is under Mr Yushchenko's control (he once ran it), is keeping the hryvnia's peg to the dollar, thus "importing inflation". Anders Aslund, an economist, argued recently that Mr Yushchenko "seems more interested in harming [Ms Tymoshenko] politically than in capping inflation".

Ms Tymoshenko's populism does not help. She has started to compensate Ukrainians for their savings lost in the high inflation of the early 1990s. Public spending has not increased overall, but it is now skewed more to social payouts. Ms Tymoshenko might prefer to be fired (again) than to be blamed for failing to curb inflation. But that is precisely why Mr Yushchenko wants to keep her as long as possible. “Both sides know that the coalition does not work, but neither wants to pull the plug,” says a foreign diplomat.

There is little doubt that Ms Tymoshenko is a politician obsessed with power, whereas Mr Yushchenko is more driven by his vision of Ukraine as a democratic European country. But that does not, of itself, make him more effective. Even his allies blame him in part for the current mess. He has surrounded himself with shadowy advisers and been dragged into petty squabbles between rival camps. He has not allowed Ms Tymoshenko the freedom to do her job. Hryhory Nemyria, deputy prime minister, says that the president's office issued 800 instructions to the government in just 100 days.

A deeper reason for the chronic political crisis is that Ukraine's constitution does not satisfactorily divide the powers of the president and prime minister. Both camps want to change this, but each wants to serve its own interests, says Oleh Rybachuk, Mr Yushchenko's former chief of staff. Ms Tymoshenko wants a stronger role for the prime minister. This, she argues, would be better for Ukraine's EU aspirations and less divisive. “Presidential elections split the country between the west and east,” says Mr Nemyria.

This would be more convincing if Ukraine's parties were not simply vehicles for their leaders and their financial backers. “If you remove Ms Tymoshenko from her party, it would simply cease to exist,” says Mr Rybachuk. At times, Ms Tymoshenko's party resembles a cult, but her charisma does not extend to her colleagues. In the recent mayoral election in Kiev, her candidate lost to the incumbent, despite her insistence that “he is me without the plait”.

Unlike Ms Tymoshenko, Mr Yushchenko does not have much of a following, even within his own party. “After the orange revolution, Our Ukraine had a chance to become a really democratic party and include people who had stood on Maidan Square. Instead it has become a party of the *nomenklatura*,” concedes Mr Rybachuk.

For all its chaos, however, Ukraine is now a recognisable democracy with free media and a strong opposition. The all-pervasive fear is gone. In this respect, it is a lot healthier than Russia, where the prime minister and the president act almost as one. But being more democratic than Russia is no longer enough. Corruption, one of the country's biggest problems before the orange revolution, is little better and infrastructure is still poor.

Indeed, a senior executive of IKEA says that it seems harder to open a store in Kiev than in Moscow. Judging from the mayoral election, things are unlikely to improve. Its winner was the incumbent, Leonid Chernovetsky, nicknamed “Cosmos” for his spaced-out and erratic behaviour and his allegiance to a local sect, the Embassy of God, which professes that “wealth is not for sissies”. It is impossible to say how the recent crisis will play out—probably in a messy compromise—but Ukrainian politicians are on borrowed time.

One sign that many voters are fed up is their strong interest in past leaders. A record number took part in a popular television show, “Great Ukrainians” (based on its British equivalent). The winner was Yaroslav the Wise, an 11th-century Kiev prince. Yaroslav once warned his children that “if you dwell in envy and dissension, quarrelling with one another, then you will perish yourselves and bring to ruin the land of your ancestors.” So far his advice has fallen on deaf ears.

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The European Union and Russia

Uneasy partnership

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The European Union has agreed on what it wants from Russia. But not how fast

WHETHER it was brave or clumsy depends on your point of view. But Lithuania (population 3.5m) has nudged the European Union (population 500m) into a slightly tougher stance towards Russia. Talks on a (long overdue) partnership agreement were first postponed because of Russia's embargo on Polish meat. When that was lifted, the obstacle became Lithuanian demands for firmer terms concerning energy, judicial co-operation and Russia's treatment of countries such as Georgia.

EU diplomats fumed about Lithuania's tactics, complaining of belated timing, poor preparation and unrealistic expectations. A few said this was just the sort of thing to strengthen the view in “old Europe” that letting neurotic and primitive ex-communist easterners into their club had been a mistake. Certainly some foreign ministers' meetings discussing the issue have been remarkably stormy by EU standards.

But a meeting on May 27th agreed upon a new negotiating mandate, with small but significant changes on some points sought by Lithuania. “They have attracted attention to Russia's behaviour in Georgia, which is timely and good,” says an official from a neighbouring country. The talks on the partnership agreement will start at an EU-Russia summit in Siberia next month.

The question is how fast they will go. Germany wants things sewn up, at least in principle, within a year. That seems too soon to countries that are hawkish on Russia, as well as to the European Commission. This camp wants a more detailed deal, in which Russia would have to make big changes on such contentious issues as its energy monopolies, investor protection and illegal migration. In return the EU would offer a laxer visa regime and let Russian energy companies expand westwards more easily.

Other countries are moving to counter what they see as Germany's overly Russia-friendly policies. Poland and Sweden this week launched their own plan, called the “eastern partnership”, to offer generous trade and other co-operation to Ukraine and Georgia, as well as to other interested countries. The aim is to recreate the model of the “Visegrad” group of four central European countries in the early 1990s, which helped ex-communist states to prepare for what at the time seemed the highly uncertain prospect of EU membership.

For the first time in any EU initiative, the plan explicitly includes Belarus (albeit only on a “technical” level for now). Russian regions such as Kaliningrad are also welcome to apply for some of the goodies that a partnership agreement can offer, such as better border crossings and environmental projects. Ex-communist Poland and rich, neutral Sweden may prove an effective combination. Their forceful foreign ministers, Radek Sikorski and Carl Bildt, get on well. Bravery is good. But brains are even better.

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Germany's president

A swansong for the coalition

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The Social Democrats cause new trouble by proposing a president


Reuters

THE job is largely ceremonial but the rumpus over how to fill it has been anything but polite. On May 26th the Social Democratic Party (SPD) nominated Gesine Schwan (pictured), a political scientist, to be Germany's next president, setting up a contest next May against the incumbent, Horst Köhler. Mr Köhler's party, the Christian Democratic Union (CDU), which is in an unhappy "grand coalition" with the SPD, was outraged. Angela Merkel, the chancellor, called the decision to challenge Mr Köhler "regrettable". Some of her allies said it could mean an early end to the coalition, which is supposed to last until the federal election in September 2009.

The SPD had been expected to back a second term for Mr Köhler, a former IMF managing director. Three-quarters of German voters want him to stay. But going along with the CDU has been an unhappy experience for the SPD, which has seen its popularity slide even as Ms Merkel harvests the credit for all the government's successes. The SPD's increasingly assertive left wing insisted that the party nominate a presidential candidate of its own, both to sharpen its profile and to rally its supporters before the federal election.

There is nothing wrong with Ms Schwan, a feisty university president. She lost to Mr Köhler in 2004. Serious challenges to incumbent presidents are unprecedented and could be awkward, given the post's apolitical function, but they are in no way undemocratic. The real problem is what the SPD might do to secure her victory. German presidents are elected by a federal assembly consisting of the Bundestag plus an equal number of delegates chosen by the legislatures of the 16 states. Mr Köhler has the edge now, but that may change if Bavaria's Christian Social Union does badly in a state election next September. Even then, Ms Schwan could win only with the votes of the Left Party, a barely respectable fusion of former east German communists with west German radicals.

The CDU has seized on this. The SPD has promised not to rule Germany with the help of the Left Party. But the two parties govern together in the city of Berlin, and the SPD has opened the door to similar coalitions in west German states. Presidential elections can be harbingers of future alliances among parties. The election of Gustav Heinemann in 1969 presaged the first coalition between the SPD and Germany's liberals, the Free Democrats. The CDU frets that the SPD is plotting something similar with the Left Party—or at least, it intends to exploit this suspicion to its electoral advantage. Last week Berlin's SPD mayor abstained from ratifying the European Union's Lisbon treaty at the insistence of his Left Party allies.

The CDU has backed down from threats to end the grand coalition over Ms Schwan's nomination. But a duo at odds on foreign policy, minimum wages, taxes and climate change, among other things, is under huge strain. There may be no divorce, but the marriage is on the rocks.

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Kosovo's future

Divided rule

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The European Union runs into roadblocks in its plans for Kosovo

WHEN the Austro-Hungarian empire declared war on Serbia in July 1914, few could have imagined that the result would be the demise not only of the Habsburg empire, but also of the Russian and Ottoman ones. Nobody believes that Serbia's challenge to the European Union over Kosovo will be anything like as dramatic; most Serbs want to join the EU, not destroy it. Yet 100 days after Kosovo declared independence, Serbia has done a lot better than anybody expected in thwarting the EU's plans for it.

Serbia still regards Kosovo as a province, but the ethnic Albanians, who constitute over 90% of its 2m people, declared its independence in February. So far 41 countries have recognised Kosovo, including America and 20 of the EU's 27 members. But five of these are microstates like Nauru and the Marshall Islands. And such big hitters as Brazil, China, India and Russia have not recognised the new country. Nor have Spain, Egypt or even most Muslim countries.

Since the end of the war in 1999, Kosovo has come under the jurisdiction of the United Nations. Legally the last word in its government accordingly lies with the head of the UN mission in Pristina. When Kosovo declared its independence, the EU authorised the establishment of a big new police and justice mission named EULEX. With the Americans and others, it also set up the office of the international civilian representative (ICR), investing him with sweeping powers.

On June 15th Kosovo's new constitution is due to come into force. It foresees no role at all for the UN. But legal and technical problems mean that the EULEX mission has been postponed. As for the ICR, whose (Dutch) head, Pieter Feith, is also the EU's special representative in Kosovo, one UN official scoffs, “He and his team are here as tourists. What are they doing? They can't take over the role they were assigned, as we are still here.”

Since independence the Belgrade government has consolidated its grip on Serbian areas of Kosovo, including almost all of the region north of Mitrovica. It even held local elections, condemned as illegal by the UN, the EU and the ICR. EULEX and the ICR will be unable to operate in these areas. De facto, Kosovo is thus divided not only into Serb and ethnic-Albanian areas, but also into places where the UN will keep operating and the ethnic-Albanian areas where EULEX and the ICR will probably take over. For the EU, says one diplomat, “It is a face-saving operation now. Their plan has been derailed.”

As the June 15th deadline nears, meeting after meeting is taking place to try to resolve the impasse. The UN's future role is now utterly unclear because, as the joke has it, everyone is “waiting for Ban”. Under pressure from all sides, the UN secretary-general, Ban Ki-moon, has done little beyond prohibiting the transfer of cars, buildings and equipment to EULEX and the ICR. The Russians recently warned him that any notion that he might try to resolve the problem without the approval of the UN Security Council (and thus of Russia) was “out of the question”.

Attempts are now being made to square the circle by seeing if EULEX could somehow come under the UN's legal authority, but so far no progress towards a deal has been made. What is becoming distressingly obvious to Kosovo's Albanians is that, despite declaring independence, their future is still tied to Serbia's. Keen to gain more recognition, they are making little fuss. But Mr Feith says “they need to be given some comfort that their interests are being taken care of.” If they don't get it, he sees trouble ahead.

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France and its Muslims

The graveyard shift

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Official representation of Islam works better at regional than at national level

THE Guillotière cemetery in Lyon is much like any other French municipal burial ground. Ornate tombstones in dark stone line the alleys; plaques are carved in memory of Marie-Hélène and Jean-Pierre. Yet in one corner, on an open plot covered with poppies, lie three dozen graves lined up at a diagonal to the rest: simple mounds of earth, marked by wooden stakes in the ground. They are aligned with Mecca, and are the first of 380 places in the cemetery's new Muslim section.

For Muslims who won this plot in negotiations with the local authorities, it is a small triumph. When the Regional Council of the Muslim Faith (CRCM) in Lyon surveyed cemeteries two years ago, it found only 300 burial plots available in special Muslim sections, for a local population of Muslim origin estimated at 300,000. In the past, says Azzedine Gaci, the CRCM's regional head, four-fifths of burials involved repatriation, usually to north Africa. Today, he says, a growing number of families want to be buried in France, where their French children can pay visits.

Members of France's official Muslim body, the French Council of the Muslim Faith (CFCM), bicker interminably at national level. But, step by step, a few are getting practical things done in the regions. The contrast between the dysfunctional national body and its active regional offshoots is striking, because the CFCM is squabbling yet again ahead of a leadership election on June 8th.

The CFCM was launched by Nicolas Sarkozy as interior minister in 2003, to give an official voice to France's 6m or so Muslims, rather like that enjoyed by the country's Jewish community. Since then, Dalil Boubakeur, rector of the Paris Mosque, who has long been seen as the voice of the old Muslim establishment and allied to Algeria, has led the CFCM under a pact loosely dressed up as an election. Now more hardline bodies, notably the Union of Islamic Organisations of France, which is linked to the Muslim Brotherhood, as well as groups tied to Morocco and Turkey, want their turn. Amid a frenzy of lobbying—and, say his critics, a fear of losing in an open poll—Mr Boubakeur has threatened to boycott the vote.

Even if a deal is struck to divide up power again, the CFCM will struggle to win credibility. Non-practising Muslims see it as irrelevant, since it is organised entirely through mosques. It has been split by rivalries among foreign sponsors and financiers. And it has failed to pursue such practical matters as the training of imams, many of whom do not speak French. “The CFCM's track record in terms of organising Islam in France is zero,” says Olivier Roy, an Islamic scholar. “The advantage is that this has left the regional heads to get on with what they want.”

In Lyon Muslim burial plots are not the only achievement. The CRCM has negotiated the building of mosques and official sites for the slaughter of sheep at Eid, the festival of sacrifice, as well as improving contacts with other faiths. In Vénissieux, a run-down suburb of Lyon, opposite a Renault factory, the communist mayor has approved the building of a mosque, the Eyup Sultan, after years of failed applications. “Previous projects were abandoned because we didn't know the rules,” says Sifayi Ozcan over Turkish coffee in a portakabin at the site. “This time, we invited the mayor to lay the first foundations.”

During last December's Eid, the CRCM asked regional prefects to provide five extra official sites for ritual slaughter, to improve hygiene and stop sheep-killing at home. More than 1,200 sheep were sacrificed, along with another 10,000 at abattoirs. Now it is in talks with nearby sheep farmers to guarantee future supply—“to enable us to have good French lambs, not foreign ones,” says Mr Gaci.

Much remains to be done. There are worries about lack of progress on training imams. Vénissieux was home to an extremist preacher, Abdelkader Bouziane, who was expelled to Algeria in 2004 after advocating violence against women and who, said the intelligence services, had links to foreign terrorists. The fear is that without a French interpretation of Islamic texts, younger Muslims may turn to more hardline messages on foreign websites or through satellite television. Another difficult matter is prisons; an estimated 70% of the inmates of one in Lyon are Muslim. In the absence of moderate Muslim chaplains, radical movements are recruiting prison inmates with worrying ease.

In Lyon's cemetery, Mr Gaci frets about the damage that the rivalry within the CFCM does to the image of official Islam in France. Extremist elements, he says, take advantage of the organisation's lack of credibility to recruit disillusioned youngsters. This rubs up against efforts to accommodate Islam in France, and also against the symbolism of such steps as burial plots for Muslims. As he treads carefully round the graves, Mr Gaci adds, as if to convince himself, “it's one sign that Muslims are being accepted as part of France.”

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The Islamic headscarf in Denmark

Covering up

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A far-right party takes on the Islamic headscarf

PIA KJAERSGAARD'S Danish People's Party has a genius for attracting attention. Over the past month its campaign to ban public employees from wearing Islamic headscarves has dominated the headlines and also triggered squabbles within most of the country's other political parties.

The campaign began with a poster of a *burka*-clad woman wielding a judge's gavel. The implicit message was that Danes risk having their courts invaded by Muslim hordes and *sharia* law. Birthe Ronn Hornbech, the immigration minister, denounced the DPP as “fanatically anti-Muslim” and said the judiciary was capable of policing its own impartiality and dress code. Stig Glent-Madsen, a high-court judge, confirmed that the judiciary had always managed this itself.

Yet the government, which relies on the DPP's support to stay in power, has decided that a new law is needed to ban the wearing of all religious symbols by judges—from Christian crosses to Jewish skullcaps and even Sikh turbans. The hapless Ms Ronn Hornbech will have to frame the law. And the DPP is now calling for even broader bans. Muslim headscarves, says Ms Kjaersgaard, are a “symbol of political Islam and the discrimination against women”. She wants them “out of schools, off the streets and outside the doors of parliament”.

Many Danes share Ms Kjaersgaard's sentiments. A poll by Megafon for TV2 found 48% in favour of a ban on public employees wearing “religious garb”, and only 39% against. The international fallout could be large. Denmark is still struggling with the aftermath of the 2006 Muhammad cartoons affair, which led to protests, deaths and burnt-out embassies across the Muslim world.

One response has come from Danish-born Muslims. A poll by *Politiken*, a daily, of 315 young Muslim students, found that two-thirds of them were considering emigrating after graduation. Most gave as their reason “the tone of the Danish debate about Muslims”. Jakob Lange, head of studies at Copenhagen University, says that children of immigrants deliberately choose portable qualifications. “They want an education they can use abroad, where the tone of the debate is different. Which is why they often choose medicine, engineering or business-related disciplines.”

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Charlemagne

A woman's place?

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Why the European Union has so few women on top

Illustration by Peter Schrank

IS THE European Union at heart a female project? Margot Wallstrom, a vice-president and thus the most senior woman in the European Commission, rather thinks so. She points to the EU's fondness for compromise and listening, and its rejection of horrid things like conflict. Ms Wallstrom, who is charged with selling the EU project to the public, suggests that this is a good reason for giving women a bigger share of the union's top jobs.

Specifically, Ms Wallstrom thinks it is shameful that only men's names (eg, those of Tony Blair, Jean-Claude Juncker, Anders Fogh Rasmussen and Wolfgang Schüssel) are being bandied about in connection with three important posts to be divvied up in the coming months: president of the European Commission; EU foreign-policy chief (or “high representative”); and the new position of full-time president of the European Council, representing national leaders. It is all very well for Brussels types to fuss about parity between big countries and small, north and south, or left and right, she argues. Any chance of a candidate who is not a man in a grey suit and tie?

The underlying problem is that “men choose men” for important jobs, and this harms the EU, maintains Ms Wallstrom. Men and women “complement” each other. For example, male leaders traditionally define security in terms of “military investments”. Female leaders focus more on security achieved through access to clean water and education or “keeping children and women safe”. This is not just a woman's way of looking at security, she contends; it is the European way.

Beyond the usual feminist propaganda, Ms Wallstrom is right on one serious point: that it is (at least on the face of it) outrageous that no woman is in the running for any of Europe's leading jobs. It is a sad waste of talent whenever mediocre men fill seats that could go to more capable women. On the next rung down, some of the strongest members of the present European Commission are women, among them Neelie Kroes at competition, Mariann Fischer Boel at agriculture and Meglena Kuneva at consumer affairs.

Yet Ms Wallstrom's wider thesis is misleading, at best. The first problem with it is that European countries are not really all that consensual, or even non-violent. Most may have given up on serious defence spending, and many work hard not to provoke scary powers like Russia and China, but that is not the same thing. Europe may look all nurturing if you are Ms Wallstrom: a Swedish Social Democrat with the job of inviting “civil society” groups to chat about European models of citizenship. But in several other countries the voters have, in recent memory, elected such warmakers as Mr Blair, as well as macho types like Silvio Berlusconi and Nicolas Sarkozy. In western Europe, public opinion in many countries is lurching into an angry protectionism, a scourge that always contains a “dose of xenophobia and nationalism”, as the World Trade Organisation's boss, Pascal Lamy, noted recently. Not much “listening” went on before Italian mobs burnt down Roma gypsy camps recently, with the seeming approval of some local politicians.

The second problem is that the new Euro-jobs, especially the post of full-time council president, will require skills beyond teaching the world to sing in perfect harmony. EU politicians routinely say that the search is on for a “Mr Europe” (a rather sexist formulation), but the holder will not actually lead Europe. Instead, he (or she) will chair summits of the 27 heads of government who make up the European Council, and lobby for national governments both abroad and within Brussels.

The European Council is a rough, swaggering sort of grouping. It operates not by finding cosy consensus, but by reaching grubby compromise after lots of camp-forming, bribery and bullying. Its summits are like meetings of some ghastly men's club. By tradition, they begin in the late afternoon so that political debate can kick off over dinner, and go on until late at night (often accompanied by a *Boy's Own* sniggering over which leader has had too much to drink). Diplomats play this nonsense up, talking with relish about rows that will last till dawn, or about summits that will be “three-shirt meetings”, ie, will go on for 36 sleepless hours.

The European Commission has some good women at the top (plus a couple of dreadful ones) largely because its president, José Manuel Barroso, went to great lengths to recruit them when assembling his team in 2004. He told at least one prime minister that his country could have any commissioner's portfolio it wanted, if only it would send a woman to Brussels. Such unofficial quota systems are easier to justify when you have 26 jobs to distribute, as Mr Barroso did—though even so the commission boasts just nine women.

The Merkel method

Finding a woman for the position of council president is a tougher task, but not impossible. It mainly involves looking for a clever woman who can control a room full of men at their strutting worst. Such figures have been known: Margaret Thatcher in her prime, or Angela Merkel now. The German chancellor has a special genius for appearing self-deprecating, while subtly hinting that she is surrounded by ridiculous men. (Asked by German journalists about her relations with France's president a while ago, Ms Merkel replied: “I think I am the most boring person Mr Sarkozy has ever met.”)

Indeed, Ms Merkel herself reveals the biggest flaw in Ms Wallstrom's argument. The lack of women running for top EU positions is outrageous only on a superficial level, for one big reason. If Ms Merkel wanted to be the first permanent president of the European Council, the job would be hers without challenge. But she says she does not want it: running Germany is an interesting enough task. That is plain common sense. Neither men, nor women, nor Europeans have a monopoly on that.

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The oil shock

Pistol pointed at the heart

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Getty Images

Will high oil prices tip the economy into recession?

FUEL-PRICE protests on May 27th by road hauliers blocking one of the main roads in central London evoked unwelcome memories for Gordon Brown and the government. The only occasion on which Labour got into serious trouble in its first term of office was in September 2000, when a blockade of refineries by angry truckers briefly paralysed the country.

Just as in 2000, the road hauliers want the chancellor of the exchequer to cushion the blow of soaring prices by lowering the heavy taxes levied on diesel. Despite vowing not to cave in to the protest, Mr Brown did exactly that in November 2000, when he announced cuts in the duty charged on the most widely used fuels. Alistair Darling, his successor at the Treasury since June 2007, is now facing pressure to abandon a hike in the duty on petrol and diesel that is due in October. Next year's planned increases in taxes on many existing vehicles to reflect their levels of carbon emissions may also end up on the chancellor's accumulating fiscal scrapheap.

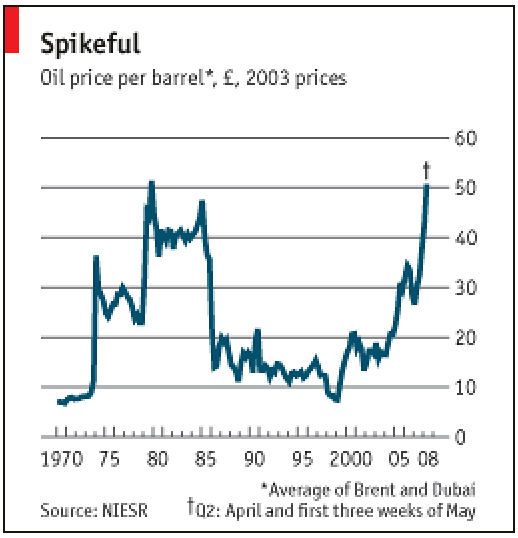
Worrying though the protests may be for the prime minister, the gravest threat he now faces is not a re-run of September 2000. That is unlikely because high fuel prices today have manifestly been caused by the record world oil price, whereas the protests in 2000 followed steep increases in fuel duty in the 1990s. Since then, the real burden of fuel duty has fallen by a sixth, according to the Institute for Fiscal Studies, a think-tank, as Mr Brown frequently ducked raising the tax in line with inflation. Rather, the danger is a repeat of much earlier episodes in Britain's economic past. In the middle and then at the end of the 1970s, two successive oil shocks triggered long and deep recessions.

Despite these disturbing precedents, until now the risk of a recurrence seemed almost as remote as that fated decade. More recent experience lulled fears. Between early 2004 and the spring of 2006, the real oil price in sterling doubled. That was a substantial shock by any reckoning, yet the economy absorbed it without undue damage. Output growth slowed in 2005, but GDP still expanded by nearly 2%, and then grew at an above-trend rate of around 3% a year in 2006 and 2007.

There were several reasons why the economy coped better with the oil shock of 2004-06. For one thing, the rise in oil prices in that period was smaller and more gradual than the spectacular jumps of the 1970s. Furthermore, it was prompted mainly by rising demand in China and other emerging economies rather than by disruptions to supply. The economy has in any case become less vulnerable to oil shocks of any description because it is less oil-intensive than it was, using half the oil per unit of GDP that it did in the 1970s, according to the National Institute of Economic and Social Research.

Britain also benefits from being an oil producer. Although sharp declines in North Sea output turned the country into a net importer again in 2005 (it had been a net exporter since 1980), it is better placed than in the mid-1970s. Still mostly self-sufficient, Britain has not had to transfer the big dollops of income to foreign oil producers that oil-importing countries have been forced to part with. Arguably most important of all, the labour market is now much more flexible than it was in the 1970s, when higher oil prices instigated a damaging wage-price spiral.

The economy may have become more resilient for these reasons, but oil retains the power to disrupt. And unlike the more gradual increases earlier in the decade, the price has shot up this year. In April and the first three weeks of May, the average real oil price in pounds was nearly double that in early 2007, and stood within a hair's breadth of the previous quarterly record in late 1979 (see chart).



This jump in prices is hitting an economy that is already under immense strain. Households have been feeling the pinch since 2004 as a result of rising prices, taxes and the cost of servicing debt. The squeeze intensified in 2006 and 2007, when real disposable income per person rose by less than 1% a year: this was the lowest growth since 1982, when living standards actually fell. Now higher oil prices are, in effect, levying a big extra tax on consumers.

And family finances are already perilously overstretched. Despite the slow growth in real incomes over the past couple of years, consumers nonetheless maintained a brisk rate of spending by borrowing against the rising value of their homes. As a result household saving fell in 2007 to just 2.9% of disposable income, the lowest since records began in 1963. Now that easy recourse to extra finance has been cut off by the credit crisis. As the mortgage market stumbles and house prices fall—by 2.5% in May, according to the Nationwide building society—homeowners will have to start living within their means, which will exacerbate the consumer slowdown.

Other sources of demand are also weakening. Residential investment seems bound to tumble and businesses are likely to curtail their capital outlays. Public spending will grow but at a much slower rate than in previous years. The sharp fall in the pound, especially against the euro, will help exports but the support will be dampened by slowing growth in the euro area, Britain's main export market.

The most serious problem is that the inflationary backdrop to the current surge in oil prices is so much worse than it was earlier in this decade. As soon as June, Mervyn King, the governor of the Bank of England, may have to write an open letter explaining why consumer-price inflation is more than a percentage point above the 2.0% target. That will be the second time that Mr King has had to put pen to paper in just over a year. A survey conducted by pollsters at YouGov for Citigroup, a bank, showed that people now expect inflation of 4.1% over the next year, the highest rate since the series began in 2005 and up from 3.1% as recently as February.

This deterioration in inflationary expectations marks a clear contrast with the position earlier in the decade, when they remained tethered close to the target. With its credibility now at stake, the Bank of England must act as well as sound tough, which means that there will be no early relief through lower interest rates. One encouraging sign is that there has not been a return—at least thus far—to the self-defeating wage-price spiral that made earlier oil shocks so pernicious.

Yet, with so much else going wrong, the sharp rise in the price of oil may prove a blow too many. If oil remains close to its current level, it could well prompt the first recession in Britain since the early 1990s.

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Oil and gas

Drying up

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Production in the North Sea is falling faster than predicted

GORDON BROWN must have found Aberdeen a welcome refuge from London, where mutinous lorry-drivers clogged a main road in protest against the cost of diesel. The Scottish city is the centre of Britain's oil and gas industry, and the only place in the country where the eye-wateringly high price of oil is cause for celebration.

Mr Brown was in the Granite City on May 28th to discuss how to maximise production from Britain's oil and gas fields. Exhorting firms to pump harder, while a useful political gesture, is unlikely to make much difference to global prices. But that does not mean that revving up output is a bad idea.

Britain's glory days as a fossil-fuel producer are over (in 1999 it was the world's sixth-biggest source of oil and gas; today it is 12th), but the business still employs around 30,000 people directly. Petropounds have made Aberdeen one of the most prosperous towns in the country, and expensive oil means more tax revenues. Oil and gas last year overtook banking as the biggest payer of corporate tax, contributing £7.8 billion ($15.6 billion) to the exchequer. Officials predict tax revenues of £9.9 billion this year, although firms say it could be nearer £12 billion if prices stay high.

Mr Brown has his work cut out to raise output. Since its peak in 1999 production has fallen by 40%. The North Sea has been pumped and drilled for 40 years and the big finds are gone. The discovery in 2001 of the Buzzard field, with over 500m barrels of recoverable oil, was a rare exception in a basin where the average new field holds just 20m barrels. Many new finds are technically tricky, which pushes up the cost of exploiting them. And although high oil prices make it attractive to try, they have led to higher operating costs as well.

With the low-hanging fruit plucked, the hope is that smaller companies will come in to pursue modest new discoveries or wring the last drops from existing fields. There are encouraging signs. Apache, a mid-sized American firm, has increased production from the elderly Forties field, the North Sea's biggest, which it acquired from BP in 2003. Reforms to the licensing system have helped, with the latest round attracting a record 193 applications. And there is still unexplored territory. The seabed west of the Shetlands may contain another 3 billion-4 billion barrels of oil and gas.

In spite of all this, production has fallen sharply. Oil & Gas UK, the industry's trade body, had hoped that output would be around 3m barrels a day in 2010, a target that now looks impossible. Worries over decommissioning costs are starting to affect asset trading, says Alex Kemp of Aberdeen University. There are no pipelines west of the Shetlands, and without the prospect of giant new fields to lure them, companies are reluctant to build any.

But Mr Brown has other tools at his disposal. In his previous incarnation as chancellor, he pushed the tax rate for oil and gas firms to 50%, far higher than the 28% other companies pay. If he is serious about maximising production, reversing that would be a good start.

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Detention without charge

Taking liberties

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A parliamentary defeat looms for the prime minister

Reuters

IF PATRIOTISM is the last refuge of the scoundrel, national security, say critics of Gordon Brown, is the last hope of the beleaguered politician. Hit by double-digit poll deficits, whispers of insurrection and, on May 22nd, a huge by-election loss to the Conservatives, the prime minister faces a vote on his proposal to extend the period for which a terrorist suspect can be detained without charge from 28 to 42 days.

Cynics suggest that this challenge, which is due to take place on June 11th, is also an opportunity for Mr Brown. Politicians can never be "too tough" on national security, and even a defeat—which, with roughly 50 Labour MPs considering voting against the bill, is a real prospect—could endear him to the public as a statesman willing to take a political hit rather than compromise on a matter of life and death.

More to the point, however, is the substantive question of whether the breach of civil liberties is justified. Opponents as grand as the director of public prosecutions (DPP), the previous attorney-general and Parliament's joint committee on human rights say that 28 days is sufficient. They also point to alternatives to extension, such as questioning suspects after charging them (which is in the government's bill) and allowing the use of intercept evidence (which is not).

Advocates of the bill (a dwindling band that includes some police chiefs and Lord Carlile, the independent reviewer of anti-terror laws) retort that it makes no sense to wait for a crisis to emerge before acting. It is better to legislate this "reserve power" now. They also cite various safeguards against its abuse: the government can extend detention only with the permission of a chief constable and the DPP, and this would then need parliamentary approval.

Public opinion is mixed, judging by a YouGov poll in March for Liberty, a campaign group and persistent thorn in the government's side. Encouragingly for Mr Brown, voters did not think innocent people would fall victim to the new detention limit, and only 7% wanted to retain both 28 days and the ban on post-charge questioning. However, voters preferred post-charge questioning as an alternative to a 42-day limit by a large margin.

It is partly because of this ambiguous public mood that the Tories think they can vote against the bill without looking weak. Their support for post-charge questioning and intercept evidence hardly marks them out as anguished civil libertarians. Yet the manner in which they oppose the government will be as important as the mere fact of their opposition. The visible glee on the Tory frontbench when Tony Blair's attempt in 2005 to extend detention without charge to 90 days failed (months after deadly bombings in London) did not dispel the notion that the Tories were more concerned with politics than principle.

Of course, a parliamentary defeat does not by itself doom a prime minister. Mr Blair clung on for another 18 months and Mr Brown insists that this vote is not a referendum on his leadership. Neither is he seen now as weak on security—he responded well to botched terrorist attacks last summer (another took place in Exeter, in south-west England, on May 22nd)—which makes his obstinacy on this measure all the more curious.

But such draconianism will damage Mr Brown's stock with the left, already low after recent (and now expensively reversed) tax changes that hit poor households. He used to be reckoned more liberal than his predecessor, and gave an acclaimed speech on liberty last year. Jon Cruddas, a left-wing Labour MP whom some see as a future leader, cites urban intellectuals as one segment of the Labour base that has deserted the party in recent years. Further curtailing of an ancient civil liberty will not charm them back.

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Anti-terrorist laws

Guilty, we think

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An attempt to marry liberty and security

WHY can't Britain do in 28 days what America does in two? Its police already have the most generous pre-charge detention limit in the world. Australia has the next longest with 12 days, Turkey and Ireland seven, France six, Spain and Russia five, Italy four, Germany and New Zealand (like America) two. Canada makes do with one day.

Some suggest that Britain's refusal to allow intercept evidence in court necessitates holding suspects for ages while less easily accessible evidence is gathered. America makes ample use of intercepts, as do most other common-law countries and nearly all EU states.

But of greater importance to America's success in foiling plots speedily is its use of plea-bargaining and “holding charges”. Its prosecutors happily zap suspects with a relatively minor offence and then hold them until they have enough evidence to bring a weightier charge. Some prosecutors deliberately overcharge to encourage suspects to plead guilty on lesser counts. Such tactics are frowned on by British courts.

But English prosecutors have recently hit on a perfectly legal ploy of their own: the application of the so-called “threshold test” when sufficient evidence is not available but looks likely to emerge soon. In such cases, charges may be brought on the basis of “reasonable suspicion” (that the suspect has committed the offence) rather than on demonstration that there is a “realistic prospect of conviction” (ie, that it is more likely than not), as is normally required.

Since taking over charging powers from the police in 2004, the Crown Prosecution Service has applied the lower threshold test in about half of all terrorist cases. Each time the additional evidence has been forthcoming, says Sir Ken Macdonald, the head of the service, and the conviction rate in terrorist cases has remained “extraordinarily high”. Yet even he admits that the practice could lead to a “grave infringement of the liberty of the individual”.

That is why the parliamentary joint committee on human rights has called for the threshold test, along with appropriate safeguards, to be codified in statute. It also wants to see the introduction of bail before charge (with conditions, such as tagging) to let the police continue their investigations while maintaining some control over suspects. It believes these two measures, along with post-charge questioning, could form a “human-rights-friendly” package that would remove any need to extend pre-charge detention—which might anyway breach an individual's right to liberty under the Human Rights Act of 1998. The government has made no comment.

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Knife crime

Tragically hip

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From The Economist print edition

Violent crime is becoming more vicious, thanks to a fad for knives

THE weekend had hardly begun before Rob Knox was dead. The 18-year-old had tried to break up a fight outside a bar in south-east London when he was stabbed, fatally, in the early hours of May 24th. Five others were hurt in the fracas. The rest of the bank-holiday weekend saw two youths injured in a knife fight in Nottingham, five men slashed in a pub in London, one man stabbed to death in Bradford and another dead after a knife attack in Bristol.

From all this one might think that deaths by the blade were becoming more common. That isn't the case. Last year 258 people were killed by sharp instruments, a number that has barely changed since the turn of the millennium. As a proportion of total homicides (which have been rising slowly for decades), death by sharp instrument is no more frequent now than it was ten years ago, though knives remain Britain's favourite murder weapon. The British Crime Survey (BCS), an official annual questionnaire, suggests that violent crime has fallen dramatically in recent years. Yet people are increasingly worried about it.

And with reason. Violent crime may have fallen overall, but that is thanks to the halving of domestic violence and fighting among friends since 1997. Those falls hide an increase in violence at the hands of strangers, which has risen by 14% during the same period. And although murder is not much more common than it used to be, non-fatal attacks seem to be getting more serious. The BCS asks victims if they were traumatised by their ordeal; last year 86% of those who had been attacked by strangers said they were, against 74% in 2002. The likelihood of being badly hurt has gone up too. In 2002 8% of victims needed to see a doctor; by 2005 that figure had doubled.

An increase in knife-carrying might explain the grislier attacks. Youth workers, who have a seen-it-all-before attitude towards most supposedly new problems, tend to agree that blades have become more common. This is tentatively backed up by the Youth Justice Board, which reckons a third of those aged between 11 and 16 occasionally carry a knife (though most are penknives). The police are arresting many more people for possession, though this partly reflects more zealous use of “stop and search” powers. Judges have spotted the trend too. Nicholas Phillips, the Lord Chief Justice, thinks “there has been an increase in carrying weapons.”

The police are stepping up their stops-and-searches, a tactic that some fear will stoke resentment among young black men, who tend to be searched more than others. Black leaders themselves are increasingly in favour, though they say it would be a less touchy subject if the police were not so white. London's new mayor plans to introduce detailed “crime maps”, highlighting hotspots. That is a gamble. Young knife carriers say they go armed for self-defence, to protect themselves from others' blades. Anything that advertises the presence of knife crime might reinforce the idea that going unarmed is risky.

That is, if teenagers' behaviour in this area is at all rational. It may be that knife carrying, and the violence that goes with it, is basically a copycat craze. Lord Phillips suspects it is “a fashion, a bad peer example”. In most years the number of homicide victims between 11 and 19 in London hovers in the mid-teens. Last year it hit 26 and this year is heading higher. The police know of no single thing that has caused the outbreak.

There is an unnerving parallel. A few months ago Bridgend, a Welsh town, witnessed 19 young suicides in quick succession, each apparently inspired by the last. Emotional tributes and alarmist news coverage are now believed to have provided unwitting encouragement, by adding romance to the miserable business of dying young. The teenagers who die in knife fights on the streets receive similar eulogies. Is the same chain reaction at work?

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Pension buy-outs

Outliving the kitty

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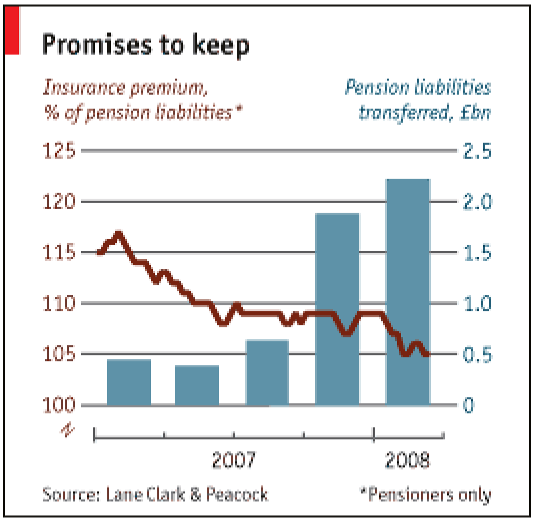
The cost to firms of offloading plans is plunging; pensioners may pay the price



THE prospect that millions of octogenarians will have a few extra years to potter about in gardens or bounce grandchildren on prosthetic knees ought to be an unmitigated good thing. But for employers the healthy glow in a retired worker's cheeks is cause for worry. Having promised to pay employees a proportion of their final salaries, uprated for inflation, until they died, many firms are weighed down by pension funds that swing wildly from surplus to deficit with every gyration of the markets. The deficits grow larger as old folk keep living longer.

Yet hope may be at hand. A fresh wind of competition and innovation is blowing through the pensions world. A host of new entrants are offering, for a price, to liberate companies from their irksome burden. And firms are grabbing at the offers with both hands, transferring their open-ended pension liabilities to insurers for an agreed premium. Over the six months to March 31st companies offloaded some £4.1 billion of pension liabilities, up from just £600m in the previous six months, according to Lane Clark & Peacock, an actuarial firm (see chart).

The sudden leap in pension buy-outs is being driven by a strange confluence of factors. Although companies say that providing pensions has become more onerous in recent years, the fees charged by insurers for taking over those liabilities have dropped sharply. Why the apparent difference in views?

Rising longevity is one reason why companies are anxious to wriggle out from under the promises they once made (though they also keep a weather eye on the risks posed by volatile interest and inflation rates). Actuaries reckon that pension-fund liabilities usually increase by about 3% for every extra year that pensioners live after 65. “In the 1950s and 60s it was simpler, pensioners lived for a few years and then did the decent thing,” says David Blake of the Pensions Institute at Cass Business School. Now thousands of small firms with pension funds are “carrying an unhedged exposure to cures for cancer that they are ill placed to manage”.

Regulation is another reason. Companies are being pressed to pay more into their funds to make good any deficits, and levies charged by the Pensions Protection Fund, a safety net for pension-plan members whose employers go bust, have increased. Mooted new accounting rules may increase the size of pension liabilities on firms' balance sheets, and other proposals could exacerbate the effect of swings in the value of stocks and bonds.

The third main reason for the explosion in pension buy-outs is a sharp fall in the fee that insurers are charging to take on liabilities. John Hawkins of Mercer, an actuarial firm, reckons that premiums have fallen by 10-20% over the past 18 months and Paternoster, a new specialist insurance company, puts the drop at about 8% in the first quarter alone (though premiums rose again by 3% in April).

For this thank competition, first of all. Eleven firms, most of them recently constituted, now scrap for a toe-hold in a market that two sleepy insurers contested a couple of years ago. They are willing to price more keenly to get business and are able to do so because they invest in higher-yielding corporate bonds rather than safe but unexciting government bonds. The credit crisis has sweetened the yields further.

Yet the scramble for market share also creates problems. Regulators and many in the industry fret that the premiums insurers charge do not reflect the risks they are taking on. A Panglossian view is that they are accepting unprofitable business now in the hopes of building up critical mass that will allow them to charge more realistic rates later. They may, however, be mispricing risk just to get the business, gambling with the retirement funds of others.

Insurers claim that they can make do with lower premiums because they earn more money on their investments, and that they have honed their ability to assess pensioners' life expectancy. Maybe.

But although regulators and insurers both say they are aware of the risks and are taking steps to mitigate them—mainly by setting aside pools of extra capital in case they get their sums wrong—divining what the world will look like in 40 years' time must be more art than science. Given the perilous state of a great number of corporate pension funds and the firms that stand behind them, many pensioners may be better off in the hands of well-capitalised and -regulated insurers, especially as official compensation is more generous if an insurer fails to honour its obligations than if a company goes bust leaving an underfunded pension scheme. But if insurers in the heat of competition get their bets wrong, thousands of octogenarians may find themselves outliving their means.

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Perks for Parliament

To the manor elected

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MPs' plush pensions could be the next controversy

Illustration by Claudio Munoz

ONE of the requirements for a firm to list on the stock exchange is that it make its pay deals with senior management available for shareholder scrutiny. Rumblings of discontent have recently threatened to derail generous pay packages at both GlaxoSmithKline, a pharmaceutical company, and Royal Dutch Shell, an oil firm.

On May 23rd investors in Britain plc won the same right, when Michael Martin, the speaker of the House of Commons, lost a three-year legal battle with the *Sunday Times* to prevent the details of 14 MPs' expense claims from being published under freedom of information laws. Journalists fell upon the lists with glee. Taxpayers learned that their munificence had paid for, among other things, a satellite-TV subscription for the prime minister as well as thousands of pounds' worth of showers, kitchens, garden plants and the compulsive cleaning of windows (one MP, married to a millionaire, claimed £1,600 for window-cleaning in 2003-04).

These details have been made public just as the broader topic of MPs' remuneration is due to hit the headlines. A bewildering array of committees and reviews are due to report into various aspects of it in the next few months. Indications are that one of those committees—headed by Mr Martin himself—is considering sweeping expenses under the rug again by replacing the accountable second-home allowance with an automatic block grant of £23,000 or an increase in salaries that currently start at £61,820.

MPs' pensions have received less scrutiny so far. That should change. With their generous annual accrual (one-fortieth of final salary for each year worked rather than the one-sixtieth of average salary that is more common in private schemes), uncapped inflation-proofing and government guarantee, they are widely regarded as the best in the land. Officially, the cost to the taxpayer is only 18% of an MP's salary. But John Ralfe, an independent pensions consultant, reckons that using private-sector accounting rules, taking the government guarantee into account and incorporating modern life-expectancy numbers boost that cost to around 50% of salary.

Such lavishness, Mr Ralfe suggests, is in part a relic of the days when many MPs started as stars in the private sector, leaving the prospect of a long career and handsome pension for public service. But the days when most firms offered most workers anything like this sweet a deal are long gone, and other public-sector schemes too are much less cushy.

Many MPs argue that their perks are legitimate. Daily commuting to London is impractical for many, and two homes a necessity. Their basic pay is far from flashy.

In any event, there is some political pressure for reform. Gordon Brown, for one, wants to take away MPs' power to vote on their own salaries. Until April many items worth less than £250—far more than the benefits an unemployed person receives each week—were considered too trifling to require formal accounting for; that limit has fallen to £25.

Mr Martin's determination to keep expenses secret is unlikely to go down well with ordinary workers. They can only dream of new kitchens and plasma-screen TVs while reviewing their defined-contribution pensions and nervously eyeing the stockmarket. And the timing of the various reviews will do MPs no favours either, as rising food, oil and electricity bills frighten and irritate their constituents.

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Bagehot

The Norwegian gambit

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A Churchillian lesson on loyalty for Gordon Brown

Illustration by Steve O'Brien

AN ADMIRAL in full dress uniform denounced the government. So did David Lloyd George. “In the name of God, go!” enjoined a Conservative backbencher, quoting Cromwell. Instead Neville Chamberlain bared his teeth, cried “I have friends in the House” and accepted Labour's challenge to what was, in effect, a vote of confidence. He was howled out of the Commons and replaced by Winston Churchill two days later.

The circumstances of the so-called “Norway debate” in Parliament in May 1940 do not, on the face of it, have much in common with the petty political furore—all unattributable briefing and ill-disguised posturing—that has engulfed Gordon Brown. The standard of political oratory is now rather lower. The perils faced by the nation were then rather graver (while pondering how he came to be prime minister unopposed, future historians may also wonder how Mr Brown became so unpopular so quickly, when so little actually happened). But the 1940 crisis is highly relevant in one important way. As well as altering the course of world history, it was the supreme drama of parliamentary loyalty—with salutary lessons for Mr Brown.

Mythical men in grey

Perhaps the most important concerns the ostentatious loyalty of rivals. As a member of the government, Churchill supported Chamberlain in the epochal debate (indeed, he was partly responsible for the defeat in Norway that precipitated it). He thus confirmed an ancient rule of politics: if you want to wear the crown, abjure the knife—and its modern equivalents, the resignation letter and leadership challenge. Michael Heseltine proved that rule again in 1990 when he stood against Margaret Thatcher: she lost, but so did he. So it ought to be little comfort to Mr Brown that his most plausible rivals—David Miliband, the foreign secretary, and Alan Johnson, the health secretary—have been among his stoutest defenders since the Tories' by-election win, on March 22nd, in the once-safe-Labour seat of Crewe.

As with Churchill's swashbuckling defence of Chamberlain, this theatrical loyalty has a double benefit: it distances the “loyalists” from plots and coups while at the same time, if done well, advertising their political skills. Mr Johnson's very unChurchillian but winningly colloquial style, for example, makes Mr Brown's droning automation sound even worse—even if Mr Johnson deploys it in the prime minister's defence. Mr Johnson, it is true, has forcefully denied that he wants the top job. But since the two main tasks for any emergency prime minister would be to reassure a griping and pinched public, and to soothe a fractious party, some Labour MPs may hope that, with his affable reasonableness, Mr Johnson reconsiders. Every time Mr Miliband answers a question, meanwhile, it seems an implicit reminder that Mr Brown rarely does.

Conversely, the most wounding attacks on Mr Brown have come from people with no realistic prospect of replacing him. That includes the old Blairite “ultras”, some of whom are seething with off-the-record fury at Mr Brown's failings. It is only a mild exaggeration to say that the more overtly loyal an MP is, the more authentically dangerous he is too.

The second Norwegian lesson is that victory is not always enough. Chamberlain won that Commons vote, but enough of his usual supporters switched sides or abstained to make his position almost untenable. Likewise, Mrs Thatcher beat Mr Heseltine in the first round of voting in 1990, but too narrowly: sometimes, only overwhelming loyalty will do. Specifically, leaders can lose their authority as much through their allies' silence as their enemies' vitriol. That is why the invisibility of Jack Straw, the justice secretary, in the first few days after Crewe was ominous for Mr Brown (he reappeared on May 27th). Mr Straw has a long record of backing winners, including Mr Brown himself last year. His is a litmus-test loyalty. Like many kingmakers, he may also have higher ambitions of his own.

The third key lesson is that sometimes the worst thing an imperilled prime minister can do is put his party's loyalty to the test. Chamberlain's invocation of his “friends” helped to finish him; something similar might happen to Mr Brown if, for example, he allowed a vote on his terrorism legislation to become a referendum on him. John Major, of course, submitted himself to a party-election contest in 1995. But if Mr Brown did the same, he might well lose. His fate depends on persuading his MPs that, like it or not, their fates are intertwined with his.

There is an encouraging corollary: if he avoids a showdown, he will probably survive. Labour's mechanism for an official challenge to him is off-puttingly cumbersome. Westminster is humming with talk and even alleged sightings of “men in grey suits”—senior ministers supposedly poised to whisper in Mr Brown's ear and put his premiership out of its misery. But the men in grey suits are, so far, entirely mythical beasts. No modern prime minister has been forced out by such a delegation of doom. The cabinet encouraged Mrs Thatcher to go, but she had already been challenged (twice) and weakened by resignations.

Still, it is not inconceivable that the grey men will materialise—if enough MPs conclude that Labour has a chance but Mr Brown doesn't; that even if he had anything to say, the public has stopped listening; that they need to act quickly to avert disaster. Labour would look both desperate and undemocratic if it installed another unelected prime minister. But plots need seem reasonable only to the plotters: it is a mark of how febrile and introverted many Labour MPs have become that some names being mooted as successors are virtual unknowns.

If so, the Norway debate may offer a final warning. It is that for all its arcane affectations and rituals, Parliament can be a murderously brutal place. When power starts to ebb, it can disappear in a rush, and loyalty in a puff of smoke.

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Economist.com WORLD INTERNATIONAL

Corporal punishment

Spare the rod, say some

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In rich countries at least, parents and teachers are steadily losing the right to discipline children by force

Alamy

"AS PART of their daily lives, children across Europe and the world continue to be spanked, slapped, hit, smacked, shaken, kicked, pinched, punched, caned, flogged, belted, beaten and battered in the name of discipline, mainly by adults whom they depend on." But in some places, it happens less than before, and there is a chance to stop it altogether.

That is how the Council of Europe, a 47-country body that is supposed to promote civil liberties from Dublin to Vladivostok, explains its campaign to abolish physical punishment—to be launched in Croatia in mid-June with a flurry of debates, puppet shows, television spots, pamphlets in many languages and stirring calls to "raise your hand against smacking".

As is often the case with such worthy efforts, the council's rhetoric seems torn between stressing the horrors of the present day and promising that things can easily improve if everybody tries a bit harder. And in a world where children face such horrors as forced labour, sex trafficking and military conscription, devoting energy to outlawing parental smacks may strike some people as the wrong emphasis. But a consensus against hitting children is clearly gathering momentum in the developed, law-governed parts of the world. Also growing is the belief that a light parental cuff and serious forms of child abuse are points, albeit quite far apart, on the same spectrum. Some parents may still insist that their right to dissuade a toddler from doing very dangerous things is also worth protecting; but they are losing the argument.

Only 23 countries (18 of them European) have banned corporal punishment completely. But there are 106—including many places where it was common only a generation ago—which have put a stop to corporal punishment in schools.

Countries where teachers still use force include the United States, where a Supreme Court ruling in 1977 (concerning two pupils whose beatings with a wooden paddle caused medical harm) found that a constitutional ban on "cruel and unusual punishment" applied only to judicial proceedings. That left individual states to decide; in 22 of them, corporal correction in schools occurs in at least some districts.

Elizabeth Gershoff of the University of Michigan, an expert on (and opponent of) physical correction, says the practice remains common in American classrooms and homes. Most American children have been corporally punished at home by the time they reach adolescence, and in a recent year, nearly 300,000 were physically punished at school.

In Europe, by contrast, smacking has nearly vanished from schools (even in Britain and Ireland, where it was rife) and the movement to stop parents and other adults hitting children is gaining ground. In 1979 Sweden became the first country to outlaw all violence by adults on children. It was controversial at the time, but after a two-year drive to publicise the law and the thinking behind it, which included putting advice on milk cartons, smacking itself, and belief in its value, declined fast.

Just over a year ago New Zealand became the first English-speaking country to ban smacking. A lobby group, Family First, is agitating to reverse that change, saying at least half the population supports the right to smack. But few people expect the ban to be overturned. The police were reassured when they won the right to apply the law with discretion, and there have been no silly prosecutions. Some of New Zealand's pro-smackers lost support because their religious rhetoric—talk of loving corrections, followed by prayers—sounded weird.

A smack of desperation

In recent years, several European countries (Greece and Portugal, for example) have quietly abolished parental smacking after a Swiss-based lobby group challenged them for being in breach of the European social charter, a Council of Europe treaty. Three Latin American states (Chile, Uruguay and Venezuela) joined the non-smackers last year. Although nobody expects corporal punishment to vanish soon from traditional homes in Africa or the Middle East, the United States could soon stand out in the Americas, and among rich countries, as a refuge for the spanker.

Indeed, it is the only country, along with Somalia, which has failed to ratify a United Nations convention on children's rights, which since 1990 has protected children from “all forms of physical or mental violence”. American officials helped draft the document, but it faces stiff opposition in some quarters of the United States.

Some Americans regret this. In a paper last year, Ms Gershoff and Susan Bitensky, of Michigan State University, said their country should bow to the combined pressure of a growing world consensus against smacking and scholarly evidence that it is useless or harmful. Summarising scores of studies, they conclude that smacking fails in one of its main aims: to make a child see that some things are wrong, and change its long-term behaviour.

Lots of studies, however, find a correlation between corporal punishment and aggressive, delinquent behaviour. It is hard to prove that the smacks cause the behaviour, rather than vice versa, but Ms Gershoff insists that by rigorously combing the data, one can show that parents are most to blame for this vicious circle.

Other scholars, such as Robert Larzelere of Oklahoma State University, defend the role of smacking in disciplining younger children, though he agrees that it is counter-productive for older ones.

Still, for countries wanting a halfway house, defining the permissible is tricky. In Britain parents can strike, not bruise; in Canada children aged 2-12 can be struck, but not with objects or on the head: “minor corrective force of a transitory and trifling nature” is allowed. And regardless of the law, social changes seem to be making parents in rich countries cautious about smacking. Many Americans who oppose a ban on corporal punishment say they don't consider the practice desirable.

But diehard American spankers may take comfort from defying the latest piece of Utopian dottiness from the UN: a campaign to end the corporal punishment of children, all over the world, by 2009. Whatever the merits of a ban on smacking, this wildly unrealistic goal is hardly the top priority for an organisation that has failed to crack down on far worse forms of abuse by its own blue-helmeted soldiers (see article).

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Economist.com WORLD INTERNATIONAL

Peacekeeping and sex abuse

Who will watch the watchmen?

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The harm that is done by people sent to do good

EPA

A tainted banner

Get article background

ORGANISATIONS that send peacekeepers and aid workers to dangerous places are usually concerned about their envoys' physical safety. But an uglier concern has recently surfaced: how to ensure the moral integrity of people who are supposed to be helping others.

A report this week by the British branch of Save the Children, an aid organisation, underlines the problem. In a study carried out last year in three places with a strong international presence—southern Sudan, Haiti and Côte d'Ivoire—the charity said it had found widespread sexual abuse of children, some as young as six, by aid workers and, above all, by UN peacekeepers. More than half the 250 boys and girls aged 10-17 it interviewed said they knew of such cases. But the abuse remained "widely underreported", it said, because most children were too frightened to come forward.

Sadly, the report tells a familiar tale. The UN in particular has been plagued by sex scandals among its peacekeepers in recent years. After a particularly shocking series of rapes by Nepalese blue-helmets in Congo in 2003, Kofi Annan, then UN secretary-general, set up a committee of inquiry. Its damning findings of "repeated patterns" of rape and other sexual abuse by peacekeepers prompted Mr Annan to announce three years ago a policy of "zero tolerance" for such crimes for all the 200,000 or so personnel, civilian and military, who are employed by the UN and its agencies around the world.

The world body has always banned its staff in the field from having sex with prostitutes or anyone under the age of 18. It also "strongly discourages" sexual relations even with consenting adults in the host population. "Conduct and discipline" teams have now been set up in each of the UN's 17 peacekeeping missions, along with an overarching special unit at its headquarters in New York, to help eradicate the scourge. In addition, since 2005 all new peacekeepers have been required to undergo training to prevent sexual exploitation before being sent to the field.

But the abuse continues, seemingly unabated. Following the scandal in Congo, there have been serious incidents of alleged rape of civilians by blue-helmets every single year—in Burundi (2004), Sudan (2005), Haiti (2006), Liberia (2006) and Côte d'Ivoire (2007). Last year the UN received 748 allegations of misconduct by its peacekeepers, 127 of which involved sexual exploitation and abuse. Most, if not all, will be investigated. But few are likely to lead to convictions or sanctions.

For when it comes to its blue-helmets, the UN finds itself in a bind. Although it can, and does, investigate any serious complaints against them, it has no jurisdiction over the alleged culprits. Only their home states have the authority to try and punish them. Most peacekeeping troops come from the developing world—Bangladesh, Pakistan, India, Jordan, Nigeria, Nepal and Ghana are the biggest contributors—and many prefer to sweep such incidents under the carpet. All the UN can do is to dismiss them and recommend their repatriation. As all peacekeeping troops enjoy absolute legal immunity, the host country cannot do anything either.

Civilian police attached to such missions are a different matter. Like other non-local UN civilian staff in the field, they enjoy only qualified immunity—for actions committed in the course of their official functions. Rape and the abuse of minors would not fall into that category, of course. So such crimes could, in theory, be prosecuted locally. In practice, however, this is unlikely, as the kind of countries to which blue-helmets are sent have either appalling justice systems, or non-existent ones. Besides, finding witnesses willing to speak and assembling sufficient evidence are often virtually impossible in such chaos.

Aid agencies and other NGOs are subject to different laws again. Their foreign-based workers have no immunity in the host country. If they come from civil-law countries, like France, they may be prosecuted—though with great difficulty—back home. Citizens of common-law states, like Britain and most old Commonwealth states, cannot usually be prosecuted at home for crimes committed abroad, but they can be for sex offences.

Most NGOs have codes of conduct, under which the purchase of sexual favours, let alone actual abuse, is strictly banned. But the toughest penalty they can impose is dismissal. Save the Children UK recently sacked three workers for having sex with girls of 17, which, though not illegal, breached its code.

The charity now wants an international watchdog to tackle abuse. How it can succeed where the UN has failed is unclear. One of the biggest problems is not just the unwillingness of victims to complain, but their ignorance of their basic rights. What is needed, suggests Françoise Hampson, a professor of international law, is a campaign to inform the locals of their rights, along with an easily accessible complaints procedure. But in a huge, chaotic place like Congo, that's a tall order.

Another way to improve the present system, she says, would be to require heads of mission to investigate any allegations of wrongdoing at the first whisper, rather than waiting for a formal complaint. She also proposes that the agreements drawn up between the UN and troop-contributing nations be modified to oblige the state at least to tell the UN what it has done to punish wrongdoers.

The UN has been trying to strengthen its procedures. Under a revised “model memorandum of understanding” adopted last year, governments are now explicitly required “to bring the full force of their legal sanctions to bear” to enforce the UN's standards of conduct. What that will mean in practice has yet to be seen. But at least investigation procedures have improved. Upon notification of a case of serious misconduct, the UN now not only informs the country concerned, but also invites it to investigate the incident in co-operation with its own Office of Internal Oversight Services. The new arrangement was applied for the first time to alleged abuse by Sri Lankan peacekeepers in Haiti last year. Over 100 soldiers now face court-martial.

Deeming the new report “deeply disturbing”, Nick Birnback, the UN's spokesman for peacekeeping, said it was impossible to ensure “zero incidents” in such a big organisation. “What we can do is to get across a message of zero tolerance, which for us means zero complacency when credible allegations are raised, and zero impunity when we find that there has been malfeasance,” he said. That would indeed be a useful start.

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Trade in wildlife

Just let them get on with it

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Poor people who rely on nature's gifts should be helped to help themselves

NaturePL

Yes, trade in me—but sensibly

CONSERVATIONISTS and animal-welfare types please take note: trade in wildlife products, as long as it is properly managed, is an indispensable boon for the poor. And what is more, it's big business, worth around $300 billion in 2005—chiefly in timber and fisheries.

That is the message of a new report* from TRAFFIC, a group based in Cambridge, England, which monitors the commerce in undomesticated animals, freely growing plants and their products. It also notes that some countries have a large domestic trade in wildlife, unreported by statistics. Estimates of how many people depend on the wildlife trade for at least part of their income vary from 200m globally to a billion in Asia and the Pacific alone. And a new report due to be released at the Convention on Biological Diversity in Bonn says damage to nature could halve living standards for the poor.

For these people, wildlife provides not only cash but food and health care (in the form of natural medicines). That is particularly important for the world's poorest people, in marginal agricultural areas. As the report points out, many poverty-reduction efforts depend on the survival of natural wildlife. Wildlife trade also provides cash that helps children go to school.

Brimming with bounty

Take Uganda's lake fisheries, which yield fish worth over $200m a year while employing 135,000 fishermen and 700,000 small operators in processing, trade and associated industries. The fisheries also generate $87.5m in exports and contribute fully 2.2% of GDP. The report also highlights the wild-meat trade in seven countries in east and southern Africa: the victuals consumed are the equivalent of up to 40% of household monthly income.

Well-managed trade, as exists in species such as seahorses, humphead wrasse and certain ornamental fish, not only promotes these species' own conservation but can also help the preservation of other important animals and plants. But the report laments that far too much of the harvesting of, and trade in, wild products is poorly supervised, with the result that habitats are degraded and stocks depleted.

One important point: allowing for the secure ownership of wildlife resources by a clearly defined group of poor people is essential for sustainable harvesting. If no public authority is able to offer secure tenure of land or resource rights to a reasonable number of people, there is little incentive to invest in long-term sustainability. This, for example, accounts for the over-collection in central Africa of rattan, a climbing plant that is used to make wicker furniture. Nobody owns the forest or wilderness where rattan usually grows—and as a result it is increasingly scarce.

Establishing such property rights is hard; it may mean the exclusion of “outsiders”, often other poor people or even refugees, from using wildlife resources. But it is necessary: many of the problems involved in the marine aquarium trade in wild fish in Indonesia and the Philippines, for example, are caused by migrant fishermen. In Gabon the government is considering giving village associations a legal monopoly on selling bush meat to outside traders.

One recommendation in the report is to establish wildlife farms; another is certification schemes that help poor people to advertise the sustainability of their wares. The wildlife trade is rarely high on official agendas, and those who rely on it are often the weakest groups in society. It makes sense to treat them, and their business, as a solution, not a problem.

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* “Trading nature”, by Dilys Roe, TRAFFIC, 2008

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Economist.com **SPECIAL REPORTS**

In the nick of time

May 29th 2008
From The Economist print edition

If the recent entry of 12 new EU members had been delayed much longer, it might never have happened, argues David Rennie (interviewed here). That would have been an historic error

IN ITALY'S recent general election, voters in the north of the country were greeted by posters showing a Native American chief in feathered headdress (pictured above). The caption read: "They suffered immigration, now they live on reservations." The posters were the work of the Northern League, a regionalist grouping that blames immigrants and globalisation for many of Italy's ills. The party struck a chord: it almost doubled its share of the vote. Silvio Berlusconi, the overall winner, chimed in, declaring that Italy should close its borders and open camps so police could track down jobless foreigners.

Italians knew whom he was talking about: an estimated half a million Romanians living in Italy, many of them gypsies (Roma), who are blamed for a spate of violent crimes. Romania, along with Bulgaria, joined the European Union at the beginning of last year, giving its citizens the right to travel freely all over their new club. Many duly went west. Mr Berlusconi's oddly precise promise to round up jobless foreigners was no accident. One of the few legal grounds for expelling foreigners from another EU nation is to show they have no means of support. To show that they have a criminal record is not enough: EU citizens may be deported only if they gravely threaten public order.

The arrival of Bulgaria and Romania completed what Eurocrats call the "fifth enlargement" of the union, begun in May 2004 with the admission of ten new members, from Estonia in the north to Cyprus in the south. In under three years the EU grew from 380m people in 15 countries to half a billion in 27.

This report will argue that enlargement has been a force for good. Freedom of movement is a founding principle of the European Union and one of its greatest strengths. Successive waves of enlargement have injected new life into societies and labour markets across old Europe that were in danger of sinking into elegant, arthritic decline.

Freedom to trade has also brought huge benefits. The most recent enlargement added a dozen mostly fast-growing, unusually open economies to the single market, providing a big boost to anaemic EU growth rates. Dan Hamilton, an American academic, calls Europe's eastern fringes "the China next door".

The accession process that began more than a decade ago provided an historic incentive for reforms. Yet the expansion of the club has been jarring for citizens of older member countries (for example, Italy) who have discovered that their national governments are no longer in full control of their borders.

Many people in older EU member countries believe that enlargement has triggered a wholesale exodus of jobs from west to lower-paid east. According to a 2006 Eurobarometer poll, three-quarters of EU citizens think that enlargement speeds the transfer of jobs to countries with cheaper labour. Yet according to the European Restructuring Monitor, an official survey, only 8% of EU jobs lost to restructuring between

2003 and 2006 involved offshoring.

Globalisation started long before enlargement, but enlargement has crystallised public fears about it, often setting one corner of Europe against another. Nokia bosses were heavily criticised earlier this year when they announced the closure of a mobile-telephone factory in the German city of Bochum and the transfer of the work to Cluj in Romania. A German minister demanded assurances that EU funds would not be used to subsidise the move.

In truth, EU firms have been investing heavily in central and eastern Europe since soon after the Berlin Wall came down, and Italy was home to about 350,000 Romanian migrants before Romania joined the union. Yet public fears about Polish plumbers and other bogeymen are real enough. Even though German exporters have flourished by selling to the new member states, 63% of Germans, according to Eurobarometer, think that enlargement is making Europe as a whole less prosperous.

Some of the newcomers have not helped their cause since joining. Nasty populists have done well in elections in several countries, and Romania, Bulgaria, Slovakia and the Czech Republic have shown prejudice against the Roma too. But then prejudice, bad government, corruption and organised crime are not the exclusive preserve of the new members. Some existing members have been setting a bad example for them.

Nor was the fifth enlargement a simple matter of countries governed by former dissidents accepting the democratic embrace of the West. Plenty of ex-communists smoothly relabelled themselves and hung on to power across the block. Brussels is full of talk about “backsliding” to describe the way that politicians in the new member countries forgot, or actively undermined, reforms that the EU demanded during accession negotiations. Corruption and organised crime blight many of the newcomers. Parliaments and ministerial suites shelter too many bad men.

All this has led some to suggest that enlargement happened too soon, and that many of these problems could have been avoided by waiting until the accession countries were better prepared. This report will argue the opposite: that enlargement came in the nick of time. Inside the candidate countries the first victims of further delay would have been reformers who for years had been pushing painful changes as vital for achieving EU membership. Had the public started to doubt that entry was fairly imminent, the drive for reforms would have been undermined.

For the existing member countries, three big reasons would have made enlargement far more difficult if it had come any later than it did. These can be summarised as migration, money and Moscow.

The m-words

First, migration. Immigration from the east to the EU accelerated with the 2004 enlargement, though it had been going on for years before that. As the Italian example shows, if any one of the 12 new members, especially Romania and Bulgaria, were still queuing to enter the EU, there would now be a heated debate about immigration, and the EU keystones of free movement of people, capital, goods and services might soon be under attack.

Second, money. During the long years of entry negotiations, many European economies were doing pretty well. Now, with the world looking bleaker, the older members might be feeling a lot less generous. Back in 2002, 66% of the French supported the coming EU enlargement. By early 2006, France’s then prime minister, Dominique de Villepin, was blaming enlargement for the French rejection of the EU constitution in a referendum the previous summer. “France did not say no to Europe,” Mr de Villepin told an EU meeting in Salzburg; rather, Europe did not adequately prepare the ground for the enlargement of 2004.

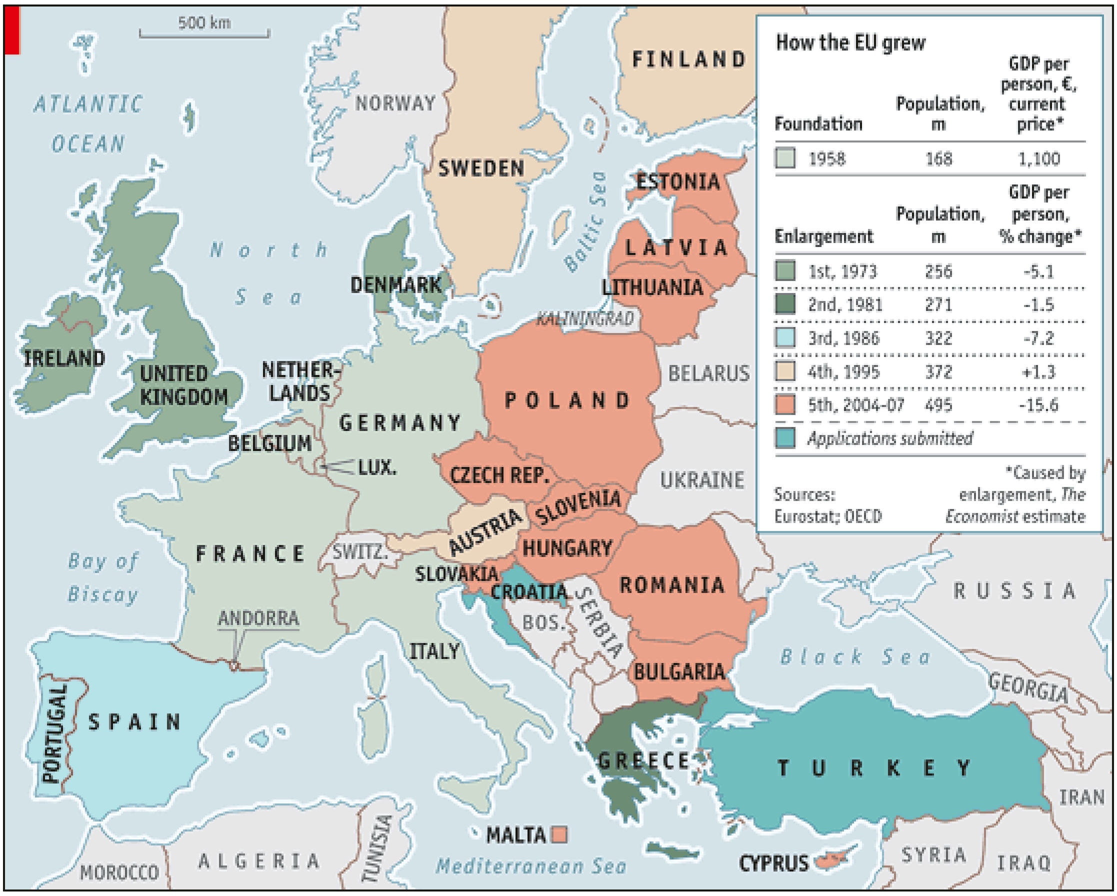
The European Commission ordered an opinion poll in France immediately after the “no” vote in 2005 which identified three main reasons why French voters rejected the constitution: it would shift jobs out of France; the document was overly liberal and pro-market; and the economy was ailing. (A similar poll carried out after Dutch voters said no in their own referendum, days later, found that only 7% of respondents were worried mainly about the loss of jobs overseas. The most common explanations were “a lack of information” and concerns about national sovereignty.)

Money worries would play a bigger part if the latest round of EU enlargement were still being debated now. Poorer countries have been admitted before. When Greece joined in 1981, its GDP per person stood at 58% of the then European Community average (at purchasing-power parity). When Spain and Portugal came in five years later, their income was around 70% and 56% of the EU average respectively.

But the newcomers are in a different class of poverty. For Poland, the figure at entry in 2004 was about half the EU average. When Bulgaria and Romania joined last year, theirs were 38% and 40% respectively.

The newcomers are different in other ways too. Romania, which added 4.5m farm holdings when it joined, now accounts for a third of all the farms in the union. (It also brought several thousand wild bears, more than doubling the EU's bear population overnight.) The newcomers have changed established views of EU history, which had long concentrated on the West and Franco-German reconciliation. As one official puts it, they are full of people for whom 1945 was not a "magic year" but the start of a new occupation.

That occupation was ordered from Moscow, and Russia's increasing assertiveness is the final reason to believe that enlargement happened just in time. EU enlargement brought dramatic changes in Russia's backyard and reduced the country's sphere of influence. Yet Russia did not block the eastern expansion of the EU.



How the EU grew

Foundation	Population, m	GDP per person, €, current price*
1958	168	1,100

Enlargement	Population, m	GDP per person, % change*
1st, 1973	256	-5.1
2nd, 1981	271	-1.5
3rd, 1986	322	-7.2
4th, 1995	372	+1.3
5th, 2004-07	495	-15.6
Applications submitted		

Sources: Eurostat; OECD

*Caused by enlargement, *The Economist* estimate

In reality, Russia's then president, Vladimir Putin, raised only two big concerns ahead of the event, recalls Günter Verheugen, a former EU enlargement chief. One was to protect the status of the Russian language and the rights of non-citizens in Estonia and Latvia. The second, and trickier, one involved Kaliningrad, a chunk of Russian territory sandwiched between Poland and Lithuania (see map). To the horror of eastern European governments, Mr Putin proposed linking Kaliningrad with the rest of Russia by a railway corridor drawn across Lithuanian territory. At a summit in 2003, Italy (then, as now, led by Mr Berlusconi) backed Russia's plan, with encouragement from France. Britain, Sweden and Germany opposed it. Residents of Kaliningrad now travel through Lithuania on a simplified visa. It is not hard to imagine Russia playing even tougher today than it did five years ago.

Earlier this year Mr de Villepin, now safely out of office, told a Belgian newspaper that enlargement was proof of Europe's "genius" for getting along with others. Had it, he mused, been in Europe's interest to open its doors to the nations of the east? "No. But Europe had no other choice but to hold out its hand."

This report would not dispute that Europe had no choice, but it will also contend that enlargement was very much in the union's interests. It will describe an enlarged Europe that is changing fast, in terms of globalisation, infrastructure or efforts to resolve the remaining legacies of communism. It will ask why EU membership has so far failed to end the frozen conflict in Cyprus, and whether that is about to change. On all these fronts, it will argue, it is a good thing that half a billion Europeans are now in this together.

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The dark side of globalisation

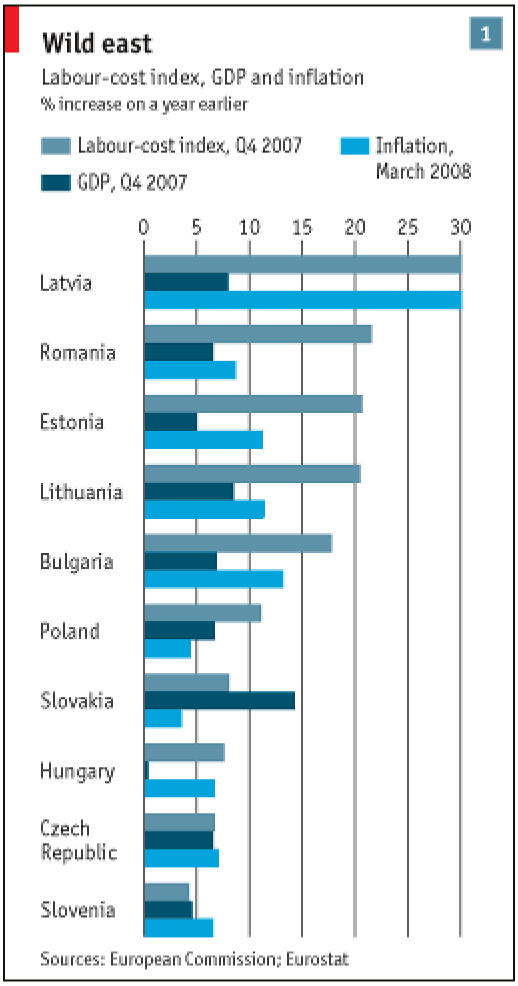
May 29th 2008
From The Economist print edition

Jobs come, but they soon go again

A DECADE ago, Samorin—a small town in western Slovakia, on the banks of the river Danube—was one of many good places in which to watch the effect of globalisation on central Europe. The town was full of cheap, experienced workers in need of jobs, with unemployment at 20%. Foreign investors duly arrived, notably Samsonite, an American luggage-maker, which set up a factory there in 1997. The town's location helped, near a four-way border where Slovakia, Hungary, Austria and the Czech Republic meet in a cat's cradle of big roads and railway lines. There are scores of similar towns across the region that attracted jobs from higher-cost, more highly regulated labour markets farther west.

Workers, trade unions and politicians in old Europe mourned each factory moving east. But, as a European Commission official explains off the record, such shifts were fully expected: offshoring "was the whole idea of enlargement". The process, though wrenching to some, made the European Union as a whole more competitive and spread the benefits of global trade to every corner of Europe.

So far, so familiar. But things have moved on in Samorin. Even though new investment and jobs are still arriving in Slovakia, and proximity still counts, this river town has already lost a factory to offshoring. Samsonite closed its plant in 2006, shedding all 350 staff and shifting production to China.



Like its neighbours, Slovakia has seen wages rising fast as new jobs arrived and many of its own people headed west. In most of the new member countries, unemployment rates are lower than at any time since early 2000.

But rising labour costs are only part of a more complicated story. Slovakia is still cheaper than the Czech Republic. In Samorin, unskilled workers might earn 12,000-15,000 crowns (€380-480) a month. Labour costs have risen faster in other new EU members too. In overheating Latvia, pay in the fourth quarter of 2007 was 30% up on a year earlier (see chart 1).

Samorin is a witness to the way that globalisation is fragmenting as supply chains break into ever smaller parts, sending jobs in all directions. The European Restructuring Monitor (ERM), an EU outfit that tracks globalisation, has analysed about two dozen cases of offshoring from new members of the EU, often involving complex moves. In one example, a German lighting company shed 400 jobs in Slovenia and sent the manufacturing end jobs back to Germany. In another, a Hong Kong-owned textile-maker shut up shop in Latvia, citing a "lack of workforce" in the region, and shifted production to Macedonia and Vietnam.

Citizens of the world

Slovakia is currently a European cheerleader for open markets and free trade. In a Pew Global Opinion survey last year, Slovaks were more enthusiastic than Americans, Swedes or Britons about multinational companies, with 72% agreeing that big foreign companies were good for their country, a European record (55% of French respondents thought foreign firms were bad for them, setting a record in the opposite direction). But will Slovaks remain so upbeat if the jobs stop coming in?

Vladimir Osvolda, the former boss of Samsonite's Samorin factory, thinks his fellow Slovaks have no choice. Western Europeans over 40 remember a working life that was "very comfortable", he says: the iron curtain shielded them from competition in central and eastern Europe, China did not yet present a threat and strong trade unions guarded their interests. East Europeans never had that comfortable life, he says, and never will.

Mr Osvolda lost his own job when Samsonite left; he now runs a factory for an Italian firm. He suspects that not all his staff understood that they lost their jobs to globalisation. All they knew was that they were made redundant five times before, in the tough years that followed the collapse of state socialism, so they felt resignation rather than shock.

Mr Osvolda managed Samsonite’s startup in 1997. He recalls that Samorin felt like a mirror of a Samsonite factory in the Belgian town of Turnhout. "They would lay off 100 staff, we would take on 100." His employers had to deal with three trade unions when shedding staff in western Europe. "Here, there was no trade union."

Not that the Americans were ruthless, he says. They rather overpaid people in Samorin. Labour costs were higher than in Asia, but location trumped cost advantage. The factory’s role was to manage peak demand for the highest-priced products. What killed his plant was the effect of higher labour costs on suppliers, who one by one moved to Asia. By the end, the factory was having to fly in materials to fill urgent orders at great expense.

"Samsonite was in Belgium 30 years before they decided the perfect solution was to invest in Slovakia," notes Mr Osvolda. The company’s Samorin business model lasted just nine years. "Everything is getting faster and faster."

Not all east Europeans are as philosophical as Mr Osvolda. The big test will come if (or when) growth rates in the ex-communist block slow to match those in old Europe and pay falls in real terms. Companies with strong trade unions—mostly former state concerns—have already seen strikes over pay. Romanian workers recently downed tools at a Renault subsidiary that makes the Logan, a low-cost car (see article).

Nils Muiznieks of the University of Latvia says his country is too small to dream about keeping out foreign threats. For those who are not happy with their prospects, he says, "the policy option here is not protectionism, it’s emigration."

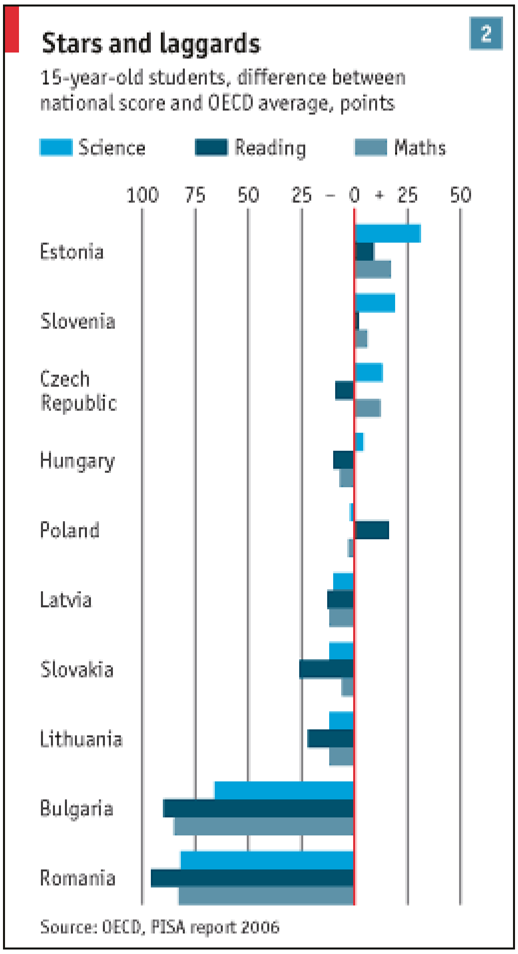
Meglena Kuneva, the Bulgarian member of the 27-strong European commission, draws a dividing line, not between old and new Europe but between "lazy and zealous Europe". The new members will thrive as long they do not become lazy, she says.

To date, the newcomers’ governments have remained fairly liberal on matters such as flexible labour markets and tax policies (their support for free trade is spottier). Slovakia’s prime minister, Robert Fico, won office as a fiery left-wing populist, for example, but was then careful to leave in place business-friendly policies like a flat tax, devised by a previous government.

Günter Verheugen, now EU commissioner for enterprise and industry, has been touring some of the new member countries, urging governments to prepare for rising labour costs. The newcomers’ success was based on three things, says Mr Verheugen: cheap labour, skilled and motivated workers, and an existing industrial base. Now costs are rising but productivity is growing painfully slowly, from a low base. The newcomers face the same problem as Spain and Portugal did on entry: relying too heavily on foreign investors to bring technologies and jobs, rather than creating indigenous centres of research and development. In the longer term, if new EU members "cannot compete on costs, they have to compete on quality and innovation", says Mr Verheugen.

The cliché that eastern Europe is crammed with highly educated boffins and poetry-spouting intellectuals has long been disproved. In the OECD’s latest PISA survey of educational standards in science, reading and mathematics, only young Estonians and Slovenians performed above the OECD average in all three.

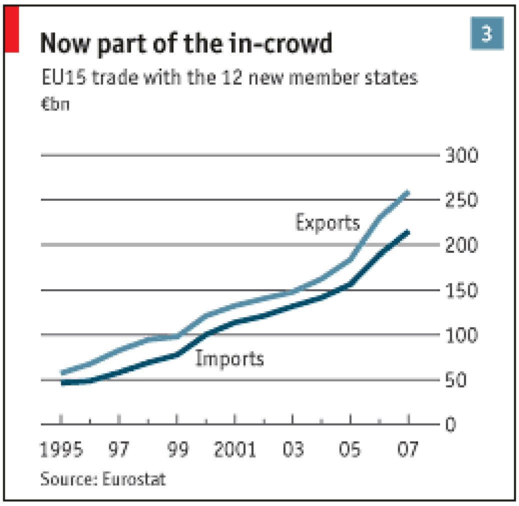
Young Bulgarians and Romanians were way below average (see chart 2).



Body-shopping

Alarmingly, the idea has taken hold across central and eastern Europe that the most pressing crisis is a shortage of people. Every day, newspapers report plans to ship in Vietnamese textile-workers, Ukrainian road-builders or Moldovan waiters to fill vacancies. There may well be some immigration, but it will not be the cure-all some seem to expect.

In sleepy Samorin, the "migrant workers" are from the poorer east of Slovakia, a few hours' drive away, but the locals see even eastern Slovaks as a race apart. They get drunk and sometimes fight, says Irvin Sarmany, a municipal official. Some blame the newcomers for a rash of burglaries.



Miroslav Beblavy, director of the Slovak Governance Institute, a think-tank, argues that the newcomers' governments should start by improving their policies at home. Employment rates in Slovakia, Hungary and Poland hover at or below 60% of the working-age population, compared with Denmark's 77%. "You can't complain about labour shortages when so many people are not working," he says. Across the region, governments have failed to keep people over 55 in the workforce, an urgent problem because ex-communist populations are greying fast. Millions of Roma are widely seen as "unemployable". Large numbers of young people now go to university. Too many are studying fashionable things like social sciences rather than engineering or computing.

Small, mundane changes would help. In some countries workers who have taken early retirement would lose their pensions if they went back to work. Bulgaria has no laws covering temporary work. At his new factory in Samorin, Mr Osvolda has started recruiting toolmakers and other specialist workers from eastern Slovakia. But he notes that once he has persuaded skilled workers to uproot themselves and move 300-400km westward, some of them will keep going to Britain or Ireland to earn two or three times more.

Everything is becoming more mobile, making life more complicated. But many central and eastern European workers remember the days when they were not free to move. They are a tough, flexible bunch and do not think the world will stop for them. The EU is lucky to have them.

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Economist.com SPECIAL REPORTS

The logic of the Logan

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From The Economist print edition

Success on four wheels

AFP

Cheap and cheerful

As the pace of globalisation quickens, the vocabulary of its European critics is failing to keep up. Search the French internet for the Logan, a low-cost car made in Romania that is a surprise hit for Renault, and the word *délocalisation* crops up a lot. But the ugly word misses an interesting point. True, French sales of the Logan grew by almost 75% last year, despite boxy styling and a minimal marketing budget. But Renault never planned to build or even sell the Logan there. Nor is it an old model of some west European car, given a second life in the east. For the French, it was never local.

Renault's idea was to produce a robust new car with few gadgets from scratch and sell it in emerging markets such as eastern Europe, Turkey and north Africa. The Logan was designed to meet European Union norms because some of the target markets were due to join the EU, but to sell at a much lower price than standard models. Cheap labour was part of the plan. The car "would not make sense paying French or Spanish wages", says a Renault boss, Gérard Detourbet. But a bigger factor was proximity to customers: cars are expensive to ship over long distances.

Production began in 2004 in Romania, where Renault had bought a local carmaker, Dacia. Low Romanian salaries were only the "cherry on the cake", says Mr Detourbet, who heads the Logan project. That is just as well, because the firm's salaries in Romania have been rising ever since. Last year they jumped by 20%, to an average of about €450 a month. A three-week strike at the Dacia plant ended in April with a pay award of 28%.

Months after the Logan's launch, Renault learned of unofficial imports into France from Romania, prompted by press coverage of the car, so it rushed to organise distribution in western Europe, beginning with France. Last year nearly 80,000 Logans were sold in western Europe.

Mr Detourbet remembers a time when Western carmakers kept quiet about their factories in the ex-communist east. That changed as Western buyers became less interested in who built their car and more concerned about the brand name and the manufacturer's guarantee. The Logan brand is even harder to pin down. In the EU and north Africa the car is badged as a Dacia but sold by Renault dealers. Most French buyers know that it is made in Romania (hence the price of €7,600 for the basic model), but "they don't really think it's a Dacia," says Mr Detourbet: they think it is a Logan, meaning a Renault.

In France the Logan's main competition is secondhand cars. Its buyers range from people without much money to better-off customers who resent spending hefty chunks of their income on a car. In Romania the Dacia name has a positive image and the car is not seen as cheap. In the rest of eastern Europe people remember the brand from communist times, but with a shudder, so Renault has had to reassure buyers that this car is different. The company's profit margin on the Logan is over 6%, double that on the full-price Renault range. Production has now spread to Russia, Morocco, Colombia and Brazil, and to Indian and Iranian joint ventures.

As labour costs converge across new and old Europe, will the Logan remain a European car? Certainly more and more suppliers will leave the EU. There will be more robots and fewer workers in east European car plants in future. But given the cost of hauling cars to customers, production in the EU will not vanish.

For all the talk about *délocalisation*, perhaps the Logan is distinctively European in a way that harks back to the first years of post-war motoring. A cheap, odd-looking car that takes cobblestones and potholes in its stride: what could be more French than that?

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No love lost

May 29th 2008
From The Economist print edition

The two halves of Aphrodite's island remain at loggerheads

AFP

A new take on the Green Line

FOR a restaurant built in ten days flat and opened only five days before your correspondent's visit, the Corado kebab house in Nicosia grills a pretty good chicken. The restaurant lies a few metres north of the Green Line that has been separating the Greek-speaking majority from the Turkish-speakers in the north for more than 40 years, cutting the island of Cyprus into two. On a recent spring evening business was humming as kebabs were rushed to tables in the alley outside its open-fronted kitchen. Four other restaurants opened nearby in the space of a week.

This mini-boom was prompted by increased freedom of movement. Politicians and security chiefs from both sides agreed to open a new crossing-point round the corner from the Corado on April 3rd. The opening followed the election defeat of the island's hardline president, Tassos Papadopoulos. The new president, Demetris Christofias, and the northern Cypriot leader, Mehmet Ali Talat, know each other well: they are comrades from the pan-Cypriot trade-union movement. This has sparked cautious optimism about fresh peace talks launched in March.

It has been possible to cross the Green Line in a few places since 2003, but after the initial enthusiasm the number of people making the journey dropped sharply. This latest crossing, on Ledra Street, the old commercial heart of the capital, is different. Crossing elsewhere takes planning; at Ledra Street, you can cross on a whim. After the bland modernity of Greek-speaking Nicosia, the Turkish side offers a jumble of crumbling mansions and scruffy bazaars, mosques of honey-coloured stone and weed-filled ruins.

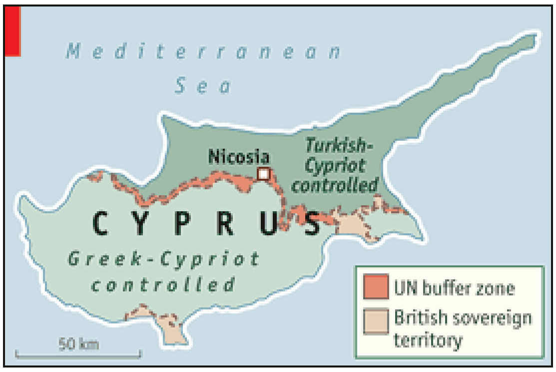
Numbers of those crossing northward nearly doubled to some 55,000 in the week after Ledra Street opened, with crowds of Greek-Cypriots joined by the odd sunburnt tourist. Staff at the Corado thought their new customers were attracted by the low prices. Greek-Cypriots said curiosity was a bigger lure. Either way, being able to cross at Ledra Street feels long overdue. The Republic of Cyprus, which in legal terms means the whole island, joined the EU in 2004, and Cypriots on both sides of the Green Line are citizens of the union. Yet the frozen conflict has only partly thawed. Around the corner from the new crossing, with its tubs of flowers and smart awnings, the old barrier still snakes its way through the city, guarded by troops.

The first four years of Cypriot membership amount to a failure for the EU's enlargement policy. Turkey does not recognise the Republic of Cyprus, even though it is itself a candidate to join the club of which Cyprus is now a member. Turkish-Cypriots were promised access to all the familiar instruments of European soft power. Direct trade with the EU was to be encouraged, and €259m was to be spent on things like scholarships, waterworks and projects to foster links between the two Cypriot communities. But progress has foundered on Turkish-Cypriot demands for direct trade and Greek-Cypriot blocking of any project that implies recognition of the authorities in the Turkish north. A deadline for using the cash promised in 2004 is drawing near, yet by March 2008 only 5% of it had been spent.

All or nothing

In Brussels, Cypriot diplomats' obstruction of EU projects designed to end the isolation of the north cause anger. Many say Cyprus should never have been admitted as a divided island. In truth, the EU had no choice. Greece made it clear that it would not approve any new expansion of the EU unless it included Cyprus.

Cypriot officials often have the law on their side. The European Commission admits, for example, that it is hard to plan infrastructure projects in the north when an estimated 78% of private land there belongs to Greek-Cypriot families. But insisting on those legal rights has costs. Free movement of goods, people and services is not just a technical aspect of life in the EU: the EU's transformative power is based on economics.



It was never likely that western Europe stopped warring and borders disappeared because Europeans became kindlier or more prepared to observe international treaties. Clearly, prosperity made sharing easier and cross-border trade made all participants better off. But in Cyprus, the past four years have offered a demonstration of what happens when politics blocks that economic alchemy: peace stalls.

Strictly speaking, EU law is "suspended" in the north, home to about 30,000 Turkish troops who never left after invading the island in 1974 and driving a third of the Greek-speaking population from their homes. In the Turkish telling of it, their troops came to bring peace after inter-communal violence and a military coup in the south aimed at uniting Cyprus with Greece. Since 1983 the northern side has called itself the Turkish Republic of Northern Cyprus, an isolated non-state recognised only by Turkey.

In the eyes of Greek-Cypriots, the occupation must be ended by a peace settlement under which all Turkish troops leave and stolen Greek-Cypriot property is returned or proper compensation paid. A week before Cyprus joined the EU, Greek-Cypriot voters rejected a United Nations peace plan that they felt did not offer enough on either front (but Turkish-Cypriots voted yes).

Official figures show two-way trade across the Green Line to be worth less than €500,000 a month, with black-market trade perhaps five times as large. Turkish-Cypriot goods are unwelcome in the south. Turkish-Cypriots themselves—or at least the 82,000 or so who hold Cypriot ID cards—come to the richer south for shopping and free medical care. Greek-Cypriots head north for beaches, casinos and brothels. But although workers are in short supply in the south, thanks mainly to a property boom, only 6,000 Turkish-Cypriots commute to work in the south.

A recent study by a Norwegian group, the Peace Research Institute of Oslo (PRIO), suggests that a reunified Cyprus could gain €1.8 billion a year from increased tourism and freed-up trade with Turkey. Manthos Mavrommatis, head of the Greek-Cypriot chamber of commerce, notes that Greek-Cypriot businessmen are a swash-buckling lot, investing in tough spots from Russia to Syria, yet Turkey is seen as off-limits even though it is the biggest market in the region. Turkey's refusal to open its ports and airports to Cypriot ships and airliners (despite a promise to do so) is driving away more and more shipping business to rivals such as Malta.

Right or might?

Yet politicians rarely make an economic case for peace. At his (legally non-existent) presidential palace, the northern leader, Mr Talat, asked how he would try to persuade Greek-Cypriots to back a future settlement, does not mention free movement of people or goods. Instead, he issues a warning that

Turkish-Cypriot opinion has become disenchanted with the EU in the past four years and there is a real threat of permanent partition. "In Cyprus, the economy is a secondary issue," he says. He does concede that the recent adoption of the euro in the south solves one problem that has caused rows in the past: how to merge currencies in a united Cyprus.

In his (much larger) palace on the southern side, Mr Christofias offers just one reason for the failure of EU policies to promote free movement and trade. The "so-called isolation" of the north is "a result of the invasion and the occupation by the Turkish army of this part of the island of the Republic of Cyprus," he says.

The largely unseen presence of that huge Turkish garrison is enough to dampen the optimism of many Greek-Cypriots. Mr Talat is widely dismissed as an incidental figure, with mainland generals seen as the real powers in the north.

That points to another lesson Cyprus offers about EU enlargement. The EU's structure—which pretends that all member states, of whatever size, are equally important—does not fit well with the hardheaded business of relations with big, powerful neighbours. In the EU's calculation of how hard to push Cyprus and Turkey respectively, Cyprus has EU membership, as well as the law, on its side, whereas Turkey can muster big strategic arguments. For a union that swears by the rule of law but has big strategic ambitions, that is an unacknowledged dilemma.

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Largesse while it lasts

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From The Economist print edition

Lots of EU money is flowing to Poland and the rest. It must be spent fast

The daily grind

IN APRIL, the red-and-white trains of the Warsaw metro finally made it to Slodowiec in the north of the Polish capital, adding an 18th station to the city's single-line underground system. It had taken 25 years of stop-start tunnelling to get there.

This summer a contract will be awarded for a second metro line, running from east to west. The tender says a main central section must be built and open to passengers in 46 months, in time for the Euro 2012 football tournament which Poland is co-hosting. That startling change of pace will require two things: lots of money and a wholesale change in official thinking.

The money is there. Outside Slodowiec station stands a large billboard bearing the European Union's blue-and-gold flag which explains that more than a third of the 858m zloty (€251m) cost of the new station came from EU funds.

Not counting farm subsidies, estimated at €14 billion between now and 2013, Poland's slice of gross EU payments will come to more than €80 billion, or €2,000 for every Pole. There is €13.2 billion for "rural development" (say, tourism or light industry in country areas), €734m for fishermen and a staggering €67 billion for "cohesion" policies that help poorer parts of the union catch up. Cohesion funds pay for things like job training, cleaning up polluted rivers and, above all, roads, bridges, sewers and other infrastructure.

Poland struggled, as newcomers always do, to spend even the limited funds on offer during its first years of membership. Since 2007, the start of a new seven-year EU budget period, the money taps have been wide open. EU cash must be spent within a few years or it will be taken back, so governments across the region have to get organised, and Poland's more than most.

Slovenia and Slovakia have some good motorways. Riga has a gleaming airport. The Czech "Pendolino" train from Prague to Bratislava is so impressive that it was featured in a James Bond film, "Casino Royale", albeit disguised as a train from Montenegro. But Poland has only about 500km of motorways, and most big cities are still linked by perilous, lorry-choked two-lane roads. It can take five hours to drive the 300km from Warsaw to Kraków. High-speed trains remain few and far between, and even Warsaw airport's new terminal, opened this year, has been a saga of delays and money rows.

That is where the second change comes in. Polish ministers say they have at last woken up to the need to move faster, sort out their creaking public-procurement system and generally play the EU game. Polish plans call for 1,200km of new motorways to be built in the next six years, and for the railway network to triple in length.

The foreign construction and engineering companies pouring into Warsaw are sceptical it will all happen on time. They say that successive Polish governments have quarrelled and dithered over every public project. Incoming administrations have scrapped plans that their predecessors had agreed to. The bosses of government agencies seem unable to take decisions, says a foreign executive. The law allows firms that lose tenders to appeal endlessly. Last but not least, officials betray a widespread lack of knowledge of environmental issues, and about how seriously the EU takes them.

Elzbieta Bienkowska, appointed regional-development minister by the centrist government of Donald Tusk last November, agrees that her country's record has been poor. A new public-procurement law is needed, she acknowledges, and promises one is on the way: "In Poland a company that loses a bid can appeal and appeal—and then the funding disappears." The public-procurement rules were drawn up by "members of parliament with a control-freak attitude", says a senior Polish official. Much of the red tape can be seen as a reaction to the "wild capitalism" of the 1990s, "when anything was possible".

How not to spend it

EU money can create the conditions for economic transformation, clearing infrastructure bottlenecks and the like. But that is only the start of it. Portugal and Greece are routinely held up as cautionary tales against squandering the benefits of EU entry. Portugal built some fancy roads but struggled to make its economy more competitive. Greece's income per person in its first decade of membership actually fell relative to the rest of the club.

Worryingly for the Poles, it may be harder for big countries to get this right. In a small country a dose of EU funding can have outsize effects, says José Ignacio Torreblanca, a Spanish expert on EU affairs: "You just need one good motorway to take all your goods out."

Spain—with a population of about 40m people, close to Poland's—is often cited as a model of how to use EU money well. In a study for the Elcano Royal Institute, Mr Torreblanca found that in the two decades after joining the EU in 1986 Spain received net transfers of €93.3 billion (at 2004 prices), the equivalent of an extra 0.83% of GDP growth each year for 20 years.

The new member countries suspect they will not be getting the 20 years of generous assistance enjoyed by Spain and other southern European countries. Enlargement is an expensive business, and old Europe is not in lavish mood.

Vaira Vike-Freiberga, a former president of Latvia, describes ex-communist members as being caught in a nasty pair of scissors. On the one hand, they have to catch up on 50 wasted years. On the other, she is not sure that "older members have been as generous with the new members as they have been to each other at various times."

Is enlargement being done on the cheap? It is a common charge, but comparisons are difficult. All member countries contribute to the EU kitty and get money back. Rich ones contribute much more than they get back and poor ones draw out more than they pay in. What really counts is net transfers. In the first three years of its membership Poland did much better than Spain in the equivalent period, landing about €6 billion in net transfers against Spain's €2 billion (at 2004 prices).

Spain's payments from the EU reached full speed around 1990. In the seven years that followed, the country received some €30 billion (at 2004 prices) in net transfers. It is too early to say what Poland will get in the seven years from 2007 to 2013, but it will do at least as well as Spain.

The big difference may come later. The EU sent large sums to Spain well into its second decade of membership, but few people think that EU cash will keep flowing to central and eastern Europe for that long. Lope Seco Gonzalez, who heads the Polish office of Sener, a Spanish engineering firm, says Poland is going through the same experience as Spain two decades ago, except that "this is going to be much, much faster."

The gain for Spain

Several of the building firms most actively chasing Polish infrastructure work are Spanish-owned. Slodowiec metro station was built by Mostostal, a Polish firm 49.9% owned (and in effect controlled) by Acciona of Spain. Four of the five consortiums bidding for the second Warsaw metroline are headed by Spanish or Spanish-owned companies.

Austrian, Portuguese, Greek and even Chinese firms are also sniffng around the honeypot of EU money. But Spanish firms do not just bring knowledge of EU funding rules, says Mr Gonzalez; they spent much of the 1990s investing heavily in Latin America, where many had a rough time. Spanish firms say they are tougher than rivals from countries such as France or Germany, slightly cheaper, and unfazed by convoluted bureaucracy. “We are a little bit four-wheel drive,” Mr Gonzalez suggests.

Foreign contractors and their Polish partners are going to need all the traction they can get. In some countries, EU funding may be something of a “resource curse”, says Andre Wilkens of the Open Society Institute, a group financed by George Soros, a veteran financier. Mr Wilkens is alluding to the disruptive effects of oil or mineral wealth cascading into fragile states. The next decade will see a lot of concrete poured in central and eastern Europe. The newcomers need to ensure it is poured to good ends.

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Toxic legacy

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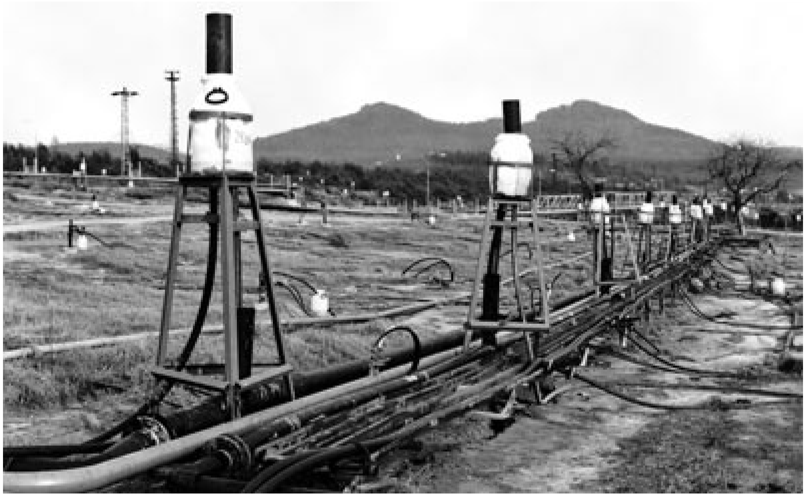
What communism left behind



A mine that failed the acid test

TWICE a symbol of foreign oppression, the disused Czech airfield of Hradcany, a couple of hours' drive from Prague, is now a happily disorganised sort of place. On a recent spring afternoon its concrete expanses, first built by Nazi invaders, attracted a learner-driver bunny-hopping past deserted bunkers that used to hold Soviet fighter jets. On another taxiway a woman on rollerskates led two small girls on bicycles. At weekends, cyclists mingle with kite-flyers and microlight pilots.

The air of subversive freedom is fitting. Since the Velvet Revolution, the image of the Czech Republic's governments has been set by ex-dissidents, not the sleek reformed communists who clung to power in some neighbouring states. The Czechs made a better job than most of opening the archives of their communist-era secret police and trying to keep ex-spooks away from high office (see article). Prague does not just look as rich as any Western city, it is rich: in terms of GDP per person, it is wealthier than any region of France outside Paris.

And yet here in Hradcany the toxic legacy of communism persists. Under the birch and pine trees of the airfield, black pipes and hoses snake across the sandy soil before disappearing into small well-heads. An oily tang in the air offers a clue: this cheerful place is the site of an environmental disaster caused by Soviet forces.

The occupiers left some 7,000 tonnes of kerosene in the soil around the airbase from where it began draining into a nearby river. Some jet-fuel leaked from shoddy pipework and storage tanks. Other spills were deliberate. Czech workers from the airfield have said that sometimes fuel-supply trains would arrive before the base had room to store more kerosene. When that happened, the newly arrived fuel was poured on the ground.

When the cleanup first began, a well dug anywhere within an area of a dozen hectares (30 acres) around the airstrip would reveal several centimetres of kerosene on top of the natural groundwater. "We used it as fuel," recalls Jirina Machackova, a scientist working for a company called Earth Tech who has been helping to clean up the site for 11 years. Locals would steal fuel recovered from the cleanup for use in their tractors. The job is due to be finished about 2012, by which time it will have cost the Czech state more than €17m. Even then, the ground will be too contaminated to build on.

By an unhappy coincidence, the Czech Republic's worst ecological disaster lies just a few miles away, at the site of a uranium mine that once supplied the Soviet Union with fuel for warheads. As at Hradcany, the trouble is underground. From 1974 to 1996, Soviet and Czech technicians carried out what they called “chemical mining” for uranium below the town of Straz pod Ralskem. Over the life of the mine, more than 4.3m tonnes of sulphuric acid and other toxic chemicals were pumped deep underground to leach out the uranium. The acid mix was pumped back up and the uranium separated out.

Acid mining is used in the West too, and with the right local geology need not be dangerous, says Ludvik Kaspar, a young engineer from Diamo, a state mining and mine cleanup firm which now runs the site. Unfortunately, he says, this is a terrible place for the method, and communist-era miners botched their work. They injected more acid than they pumped out, so the solution flowed sideways, away from the mine. In theory, a thick layer of rock kept the toxic stew away from an important aquifer, closer to the surface, that provides the region with drinking water. But the miners perforated that protective layer with 15,000 injection wells, causing massive contamination.

Today, Diamo must work night and day, pumping clean water into the ground through a line of wells to form a hydrological barrier that uses water pressure to keep the worst poisons penned in. At the same time the old acid is pumped up for treatment. If Diamo stopped all this pumping, acid waste from the mine would contaminate the North Bohemian Cretaceous Basin, explains Mr Kaspar. Asked who relies on that basin for water, he replies: “For example, Prague.”

The poison cannot be sealed off with a physical wall—there is too much of it, too far down. Instead, Diamo must keep pumping, controlling the invisible menace with what EU experts call “dynamic containment” while slowly treating the worst contaminants. Diamo executives say the site should be stabilised by 2035, but it will never be clean: under their plan, more than a million tonnes of contaminants will be left underground.

The twin environmental catastrophes of Hradcany and Straz are a fair metaphor for the legacy of communism. To a tourist or a business traveller, the Czech Republic, Hungary or Latvia, and especially their smart capital cities, may look like any corner of the Western world. But decades of communism left poisons that linger on.

The old system’s environmental abuses cannot be separated from other crimes committed in the name of state socialism. The Czech environment minister, Martin Bursik, notes that ecological protests preceded the Velvet Revolution of 1989 as citizens of the industrial “Black Triangle” near Poland and Germany demanded to know what was in their choking air.

The coming of democracy brought a flurry of environmental legislation. But it was the prospect of EU entry that gave such laws teeth, says Ladislav Miko, a Czech environmental official who now works at the European Commission in Brussels. Inspectors could exert pressure on large firms to fit clean technology because it would become mandatory once the country joined the EU. (Many small firms kept old, filthy factories open until EU accession, then declared bankruptcy.) The EU has budgeted €5.78 billion for environmental work in the Czech Republic between 2007 and 2013, but the problems dwarf the sums available.

Much Western media attention has been concentrated on communist-built nuclear power plants. Bulgaria and Slovakia had to promise to shut plants down before joining the EU. Lithuania, which produces 72% of its electricity at a single nuclear power station, must shut it on EU orders by next year. Nuclear power plants are easy to see and fret about, but there are plenty of less visible nasties. Old landfills across the region, for example, could take tens of billions of euros to clean.

Yet there are also some bright spots. Water quality in the new members, except in Hungary, Romania and Bulgaria, is approaching EU standards, says Mr Miko. Four years ago, at the time of the big-bang enlargement, their water quality was “like the West in the 1970s”.

Poison of the mind

The picture is just as complex when it comes to ideological legacies. Famously, the sweeping away of old hierarchies was followed by spells of wild capitalism in which too many gains were ill-gotten. Yet those years also saw a big infusion of fresh thinking as clever, often foreign-educated reformists became government ministers at a young age, and still do. In capitals across the region, those young reformists draw very similar conclusions about the legacy of communism.

Corruption is a huge problem, says Henrik Hololei, who used to be Estonia’s economics minister and is now a senior Eurocrat in Brussels. “In Soviet times, cheating the state was like freedom-fighting.” He points to the contrast between Estonia and Finland, which share very similar histories and cultures. But Finland was spared Soviet occupation and now enjoys top billing, jointly with Denmark, as the least corrupt country on earth, in an index compiled by Transparency International, a pressure group. Estonia comes 28th. “That is a good result for a new member state,” says Mr Hololei, “but without the Soviet legacy Estonia might be in the top five.”

Mr Bursik, the Czech environment minister, says ex-communist societies not only distrust their elites, they also lack confidence in their own civic strength. A senior official in Warsaw complains that the low quality of the civil service holds his country back, but nobody cares enough to change it. “One of the most popular tabloid stories here is that bureaucrats are paid too much,” he sighs. “And of course the opposite is true.” The salaries are miserable, he says, and administration wretchedly bad. “There is a lack of recognition in Poland that an efficient civil service is a big benefit.”

Such reformers welcome the EU as a source of rules and rigour. But even new EU laws can be subverted by the genius of ex-communist citizens for finding loopholes, says Mr Miko, the environmental official. When transposing EU directives into national laws, local lobbies will often push for some ambiguous wording to be used. “Sometimes you can work out what is behind it: aha, these people want to shoot wolves.” Sometimes the effect of a loophole emerges only later.

As in the poisoned soil and water of Hradcany and Straz, communism left mental and political legacies that cannot be walled off. But nor are they safe to be left alone. Dynamic containment will be needed for years to come.

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Bury your hatchets

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...or grind your axes?

Reuters


The Kaczynskis got vetting

DOES it matter if the European Union's top echelons include men who have done wrong in the past or who prospered under nasty regimes? Look round the table at the governing council of today's 27-strong union, and more than half the heads of government have experience of life under dictatorship—not all of them on the right side.

The EU has admitted young democracies before. In fact, nearly two decades after the fall of the Berlin Wall, the ex-communist nations have a longer period of free elections behind them than Greece, Spain or Portugal did when they joined in the 1980s. Often the effect has been positive, bringing in people who do not take freedom for granted. The union's current foreign-policy chief, Javier Solana, was an underground Socialist in Franco's Spain. The president of the European Commission, José Manuel Barroso, was an 18-year-old Maoist when revolution came to Portugal (and did his bit by setting fire to his university rector's car). The German chancellor, Angela Merkel, grew up in former East Germany, and no dark shadows were revealed when her Stasi files were made public.

In the first years after 1989 most of the ten ex-communist newcomers passed laws committing them to opening their secret-police archives, as was done in the former East Germany. Some countries went further, establishing "lustration" policies (the word comes from the Latin for ritual purification) that vetted senior public servants, politicians, judges and the like with the help of secret-service files. But such laws were often watered down or undermined, and results have been mixed.

Officially, the EU takes no interest in the political or moral records of national leaders as long as their actions do not breach the law. Prospective member countries have been ordered to reform their legal systems and create independent anti-corruption agencies. But the opening of secret-police files or the banning from office of ex-spooks has never been made a condition of EU entry. War criminals are different, with future membership for Croatia, Serbia and others formally linked to their governments' full cooperation with the international war-crimes tribunal for former Yugoslavia.

For citizens of the new member countries the dividing line between corruption and secret-police links is blurred. The oligarchs who benefited from the early years of privatisation were widely believed to have had, at the least, good links with the old regime's intelligence services.

What does all this imply for the EU? Some say nothing, arguing that after 20 years it is too late to revisit the past. The big fish, it is argued, ensured long ago that their files vanished from secret-police archives, and today's calls for lustration are mainly about score-settling and factional fights. Besides, who can be sure that the files had got things right?

One good argument against lustration is that the privatisation era is now largely finished. Former agents long ago turned their secret-police connections into wealth and forms of influence that do not involve public office and thus cannot be touched by lustration, says Georgi Stoytchev, head of the Bulgarian branch of the Open Society Institute, a think-tank.

Others note that ex-communist countries are not the only ones to send bad men to ministerial gatherings in Brussels or to be slow to tackle the past. For example, it took more than 50 years for Maurice Papon, a French budget minister in the 1970s, to be convicted of organising the wartime deportation of French Jews. And there are well-established links between the Mafia and Italian politics.

A slow excavation

Yet there is a hunger for greater transparency. In March four officials in the Czech interior ministry were asked to resign over links with the old secret police. The Czech press has recently developed a taste for combing the files of celebrities and entertainers. Generally, the Czechs made a pretty good job of opening their files. Shortly after Czechoslovakia split in 1993, the Czechs opened their archives to those who had been spied on and in 2003 published a list of 75,000 agents and informers. Thousands have been banned from public office under a lustration law.

In Slovakia, led by the autocratic Vladimir Meciar for much of the 1990s, it took until 2004 for files to be properly opened. Slovenia quietly “buried” its communist past after splitting from Yugoslavia, its foreign minister, Dimitrij Rupel, said last year, putting national unity ahead of examining past wrongs.

The Baltic states, as former parts of the Soviet Union, saw most of their KGB files vanish to Moscow, and there have been wrangles ever since about opening the bits left behind in Latvia, Estonia and Lithuania. A band of former KGB agents took Lithuania to the European Court of Human Rights, complaining about a law banning them from both public and private employment. The court conceded that although the public ban should stand, they should be allowed private-sector jobs.

In Hungary, it took until 2004 for a law to be passed to open the state security archives fully. Even then, it allowed names to be kept secret to protect modern-day “national security”.

Poland’s first formal lustration law, in 1997, was “very, very weak”, says Andrzej Paczkowski, a governor of the country’s Institute of National Remembrance, fuelling the public’s suspicions that plots and shadowy networks were responsible for the ills of post-communist life, from high unemployment to botched privatisations. When the centre-right party of Lech and Jaroslaw Kaczynski came to power in 2005, those pent-up suspicions exploded. A new lustration law sought to vet as many as 700,000 Poles, including journalists, local councillors and high-school teachers. Its scope was sharply reduced by the constitutional court, but as many as 100,000 people are still being investigated.

In Romania it was not until 2006 that key Securitate files and a master index were handed over to an independent institute. This year the government had to issue an emergency decree to keep that institute open after a court judgment ruled its work unlawful and threatened to annul thousands of investigations already carried out.

The campaign to open files in Bulgaria has been equally laboured, says Hristo Hristov, an investigative journalist and author in Sofia. “Lustration is usually a popular topic among politicians when they are in opposition,” he notes. Bulgaria’s various spy archives have still not been handed over to an independent commission (implausibly, the government says it is still trying to find a building big enough). Names have trickled out, though. In March a parliamentary report said that one in five of all ministers in office since 1990 had a past as a collaborator with the communist secret services. Bulgaria’s president, Georgi Parvanov, was named as a collaborator last year. He says he was approached to edit a book and did not realise he was dealing with spooks.

The passage of time may have helped. In Slovakia delays in opening the archives meant that the truth came out “at a moment when we could deal with it,” suggests Mr Beblavy of the Slovak Governance Institute. It made the evil of that time “tangible” for a new generation. Those named as informers need not be hated, he says. But after reading someone’s file, he adds: “It is very hard to respect them.”

As far as the EU is concerned, the best argument for pressing on with opening communist archives in the union’s newest members may be a back-to-front one. It surely says something troubling about the security services and politicians in a member country if they block the release of secret-police files from a defunct dictatorship. And member countries now have to place much more trust in each other’s security and legal systems than before, thanks to ambitious new EU instruments in the field of criminal justice. For example, a European arrest warrant issued by a judge in one country must be enforced more or less automatically in other EU nations. That requires a big leap of faith. Just how big is the subject of the next article.

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Trust me

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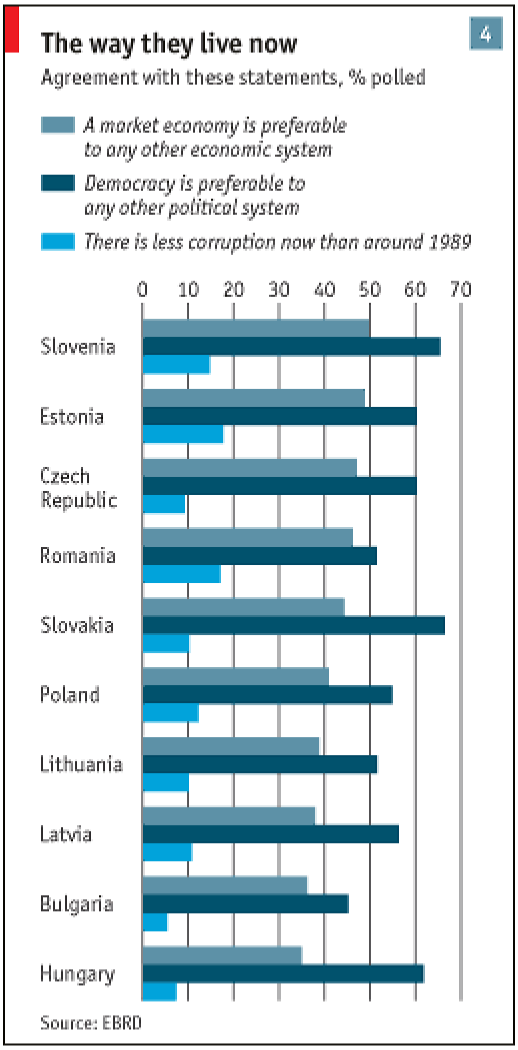
The theory and the practice of the rule of law

IN THE European Union, rhetoric often precedes reality. From earliest days, its founders followed the principle that where fine words led, with a bit of luck facts would follow. Sometimes, though, the gap between what the EU declares and what its citizens sense in their guts grows dangerously wide—and that is when the union gets into some of its worst jams.



Take the rule of law in the enlarged EU of 27. Officially, all members of the club are assumed to be equally committed to upholding Europe's legal rules (as defined by the 80,000 pages of Euro-law that new members must adopt), as well as the woollier virtues of "European values". But does anyone believe Bulgarian judges, as a group, are as determined to crack down on organised crime as, say, their Swedish counterparts? Since 2001 there have been an estimated 120 contract killings in Bulgaria, and not one of them has been solved.

This summer the European Commission will publish reports on the justice systems in Bulgaria and Romania (both of which are on probation until the end of 2009). Interim reports in February were not kind. Bulgaria, the commission found, had not produced convincing results in fighting high-level corruption and organised crime. Of a sample of ten high-profile Mafia cases registered between 2000 and 2007, only one had been concluded. Ordered to clamp down on corrupt officials at border posts, the customs service had suggested annual checks.

Romania's report uncovered less blood but more cynicism. "Procedural errors" had blocked criminal probes into corruption by serving or former ministers. Romania's parliament had made significant changes to a criminal-investigation law, including a demand that suspects be informed in advance if their telephone was going to be tapped, and the downgrading of embezzlement worth less than €9m to a "minor" offence. Under heavy EU pressure the parliament is currently taking a second look at this law.

The commission has already suspended tens of millions of euros in funds for Bulgaria, for fear of fraud. Barring a dramatic change, the next report may well recommend freezing billions of euros. The EU also has the power to suspend Europe-wide recognition of court judgments in Bulgaria and Romania. That would be serious.

The EU principle of mutual recognition means that many civil rulings can be enforced across borders. A European arrest warrant can send Italian police to pound on doors in Rome at the request of officers in London, and can secure a suspect's swift extradition.

But few expect the sanction to be invoked. EU officials acknowledge the contradiction involved in asking people to trust the new member states even as they issue devastating reports about them. But the officials also say that very little would be gained by suspending mutual recognition. Crooked judges "will just laugh at us", argues one official, whereas reformers trying to change the system from within would lose ground.

Romania, Bulgaria and several other countries admitted to the EU since 2004 started sliding away from the rule of law almost as soon as they entered. The case is put forcefully by Alina Mungiu-Pippidi, a

Romanian academic, who calls the EU admission process a “nearly miraculous” incentive for governments to clean up their act. But the effect wore off the day they were in, “like a short-term anaesthetic”. The EU enlargement process is aimed at integrating new members into the web of EU standards, rules and subsidies, not at transforming its political rulers, says Ms Mungiu-Pippidi. So as long as islands of excellence within national bureaucracies were able to churn out what the invigilators in Brussels wanted, the accession process trundled happily along.

Her evidence makes depressing reading. For example, with accession safely accomplished, the Slovene parliament voted to close down an EU-inspired anticorruption commission, which had to be saved by the country’s constitutional court. In Latvia the prime minister tried to fire the head of his country’s anticorruption agency until a public outcry stayed his hand. In Romania the justice minister, Monica Macovei (revered in Brussels as the country’s most effective sleaze-buster), was sacked three months after EU entry, accused by her prime minister of failing to uphold “government solidarity”.

This March it was the turn of the Bulgarian interior minister, Rumen Petkov, to lose his job, this time under heavy pressure from Brussels. A leaked intelligence report said a drug gang had received top-secret documents from officials in his ministry, and Mr Petkov admitted to having met suspected organised-crime bosses, though he says he was trying to stop contract killings.

All this murk is having an effect on the EU’s ability to push ahead with closer cooperation in justice and home affairs. Enthusiasm for strengthening Europol, a pan-EU police agency, and Eurojust, which brings together European public prosecutors, has been diminished, says a senior official. “On the other hand,” he adds, “if you want to combat serious organised crime, you need to work with the Bulgarians.”

The broader rule of law has also come under strain. Populists, of both the buffoonish and the sinister variety, have done alarmingly well in elections across the new member countries since 2004. In Slovakia, Vladimir Meciar, who led his country away from the democratic path in the 1990s, returned to office as a junior member of the current ruling coalition. The current Slovak government recently introduced a worryingly broad press law that allows those criticised by the newspapers the right to a prominent rebuttal.

After their countries joined, voters in Romania and Bulgaria sent a clutch of hardline nationalists to sit in the European Parliament. In Hungary, violent street protests broke out after the prime minister admitted to lying about the state of the economy to win re-election. Poland’s first years as an EU member saw a string of political crises as Lech and Jaroslaw Kaczynski, identical twins, shored up their conservative coalition government with radical nationalists and populists.

Why the time was right

Do such antics add up to proof that enlargement was premature? Defenders of the EU accession process say no, offering various arguments to support their claim. The most widely used and least convincing is that the accession process was extremely rigorous. The new members underwent far tougher scrutiny than previous entrants, says one senior commission official: Bulgaria and Romania faced detailed questions about the treatment of prisoners, for example, and in Cyprus domestic violence was a big issue. “There are old member states that would not pass that degree of scrutiny,” the official adds. But complying with benchmarks does not prove a country is ready. It might simply mean that the EU had set the wrong benchmarks.

It is also true that foreigner-bashing populists have done well at recent elections across old Europe: just look at voting patterns in France, Belgium, the Netherlands, Denmark and Austria. But pointing to flaws in long-standing member countries is a double-edged argument: if EU membership is an inherently civilising process, as many Eurocrats claim, why is it that half a century in the club has not yet made Italy a model of good governance?

Ironically, one force that may have stunted political development in the new members is the process of enlargement itself. With the best of intentions, EU officials and Western diplomats emasculated governments in the ex-communist block, hemming them in with action plans and targets so that it barely mattered which party was in office, since all were committed to achieving EU membership. Ivan Krastev, a Bulgarian academic, has written that for ordinary voters the accession era felt like a powerless time when they could “change governments but not policies”.

Perhaps a better argument for defending enlargement is a more modest one: that EU membership has proved more useful than the pessimists think, despite its limits. EU rules put a lid on the havoc that nationalists can wreak, for instance. They make it unlawful to discriminate against ethnic minorities in the job market or close borders to a neighbour's goods. Bulgaria's Mr Petkov was doubtless a flawed interior minister, but he did resign in the end. His departure was hastened by an independent body founded two years ago at the EU's urging, the National Security Agency.

Vaira Vike-Freiberga, the former Latvian president who steered her Baltic republic through the accession process, describes EU membership as a gradual process that does not end on the day of accession: "It is not like being a born-again Christian, where supposedly the Holy Ghost descends on you and from then on you are a different person."

In Bulgaria, Georgi Stoytchev of the Open Society Institute says the EU can never mobilise society against organised crime from the outside. To many ordinary Bulgarians, smuggling gangs mean "cheap cigarettes and cheap alcohol. If gangsters shoot gangsters, it is one way of dealing with the problem." The government, he predicts, will act only if it is leant on by legitimate business lobbies.

The best argument for letting in countries like Bulgaria and Romania sooner rather than later is the most modest of all: waiting a few more years would not have done any good. A whole generation of corrupt old judges will have to leave office before things change, says an EU official. "My only hope is the younger generation wants to do it differently." Reformers in that younger generation need protecting, both for the sake of their own country and of Europe as a whole. A look at the rest of the western Balkans suggests that this is more easily done inside the EU than outside.

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Give and take

May 29th 2008
From The Economist print edition

Enlargement enriches old as well as new members

AFP

Go forth and multiply

THIS report has looked at some of the ways in which the EU has changed the 12 new members. But the newcomers have also changed the EU in many ways. Here are some of them.

An expansion to 27 members would cause institutional gridlock, it was forecast. That turned out to be spin to justify streamlined voting rules contained in the Lisbon treaty. Not only is there no gridlock, but with 27 countries represented round the table there is less waffle than before.

Big deals have been concluded, notably an agreement to cut 20% off EU emissions of greenhouse gases by 2020. Fears of becoming too dependent on Russia played a big part in persuading the new entrants to sign up to the EU's climate-change deal (which also stresses energy security). They remain worried by their big neighbour to the east, and their presence has made EU debates on Russia more hardheaded.

The European Commission is recruiting a whole generation of Eurocrats from the new members who are slowly changing the place. For one thing, they speak English, not French. More fundamentally, the EU institutions were originally designed on French lines, and older officials still take the quasi-Cartesian view: I regulate, therefore I am. But many of the newcomers have already pushed through liberal reforms at home, perhaps during spells as junior ministers, which makes the best of them impatient when told that the EU is too hard to reform.

The Vatican has done well out of the latest enlargement, comments an official. It is not just Poland that brings Roman Catholic values to Brussels. Courts in Malta, an island nation of 400,000 people, do not issue divorces, and abortion is illegal there. Various forms of gay partnerships and marriage have sprung up across the EU. That would normally have prompted the European Commission to propose mutual recognition of such unions, to avoid muddle when couples move. But with Malta and Poland in the club, it is "not worth putting it on the table at the moment", says the official.

How many more?

The new members are generally keen on further enlargement of the union. Many would like to bring next-door neighbours into the fold. Poland, for example, is a tireless advocate for Ukraine. But the going is slow now because the easier cases are already in the club. Croatia is not really ready to join, if only because of organised crime, but the EU wants to stabilise the western Balkans, so it will get in around 2010. For the same reason, everyone wants to encourage Macedonia, Bosnia-Herzegovina, Montenegro and Albania to keep on the path towards membership (Albania is going to take a while). Serbia, for its part, has to choose if it wants to stay on the democratic path or head into self-imposed isolation, officials say. Depending on its choice, it could achieve formal candidate status quite quickly or be out in the cold for years.

The hardest case of all is Turkey. Its membership bid is currently in a form of suspended animation. Entry negotiations have been partly frozen to punish Turkey for its refusal to open its ports and airports to traffc from Cyprus. The French president, Nicolas Sarkozy, remains publicly opposed to Turkish membership but has agreed to put high-level EU debate on the subject on hold until 2010, when a report on the future of the EU by a "group of the wise" (which was Mr Sarkozy's idea) is due to be delivered. Turkey has serious problems of its own, starting with a court case that threatens to outlaw the ruling Justice and Development (AK) party for threatening the country's secular order.

Will Turkey ever join the union? There is no shortage of strategic arguments in favour of its accession. It is a large, secular Muslim democracy. It controls the Bosporus, as well as gas or oil pipeline routes that would allow Europe to become less dependent on Russia for its energy supplies. Such arguments mark Turkey out as important. But many Europeans clearly feel that is not the same thing as saying it should join the EU. Any enlargement of the club must be agreed on by all existing members. The most recent Eurobarometer poll on enlargement found that 69% of Germans, 54% of French and a striking 81% of Austrians were opposed to Turkish entry.

Olli Rehn, the EU's current enlargement chief, likens the EU accession process to a journey that matters as much as the destination. Europe wants Turkey to become more modern, democratic and stable because Turkey has strategic importance as "an anchor of stability and a benchmark of democracy for the wider Muslim world", he says. The best way of achieving those changes is the process of becoming an EU member. So to him, "importance and membership are inseparable."

If membership is ruled out as a destination, the journey cannot continue. But a clause in the French constitution (a sop for the anti-Turkey camp from the previous president, Jacques Chirac) obliges France to hold referendums before approving new accessions after Croatia's. Given French voters' views, the clause makes Turkish entry talks pretty pointless. Back in April Mr Sarkozy was arguing for the clause to be scrapped. After a parliamentary outcry he is now wavering.

Turkey itself, meanwhile, seems rather disillusioned. When Eurobarometer pollsters asked Turks whether membership was mainly in their interest, the EU's interest or in the mutual interest of both, the largest block of respondents (34%) thought the main beneficiary would be the EU. Perhaps surprisingly, some senior EU figures agree. "We need Turkey more than Turkey needs us," says Mr Verheugen.

Such statements may shock Europeans, but they need to hear them. They are too used to seeing enlargement as a charitable gift from a rich West to its poorer neighbours. It is hard work for both sides. But it is also an almost magical tool for stabilising a whole continent, creating new markets and letting free trade and free movement build ties of interdependence.

For these reasons and more, Europe's most recent expansion was not just a good idea. In retrospect, it will be seen as one of the EU's most significant achievements. It reunited a continent divided by Soviet oppression and brought into the European fold nations that had previously hovered on the edges of the West. If it were tried now, it would be far harder to pull off. Europeans everywhere should be glad it happened just in time.

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Sources and acknowledgments

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Offer to readers

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Corporate governance in Japan

Power struggles

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As Japanese businesses and bureaucrats block outsiders, domestic forces vie to open the country further

Illustration by David Simonds

“ZIMBABWE” is the comparison that Michael Connors of Hermes, a British pension-fund manager, mockingly draws when describing Japan's shareholder democracy. Hermes is the principal adviser of the pension schemes for many large companies, including BT and Royal Mail, and oversees billions in Japan. But corporate governance as opaque as the politics of an African dictatorship, Mr Connors grumbles, costs shareholders dear.

In recent months, corporate Japan has done an excellent job of fending off foreign investors. Peter Mandelson, the European Union's trade commissioner, calls it the most closed market in the industrialised world. Rare victories do take place: on May 29th a shareholder vote led by Steel Partners, an American activist investor, prompted the removal of six directors and the boss of Aderans, a wigmaker. But last year Steel's attempt to acquire Bull-Dog Sauce, a venerated condiment brand, was rebuffed. Bull-Dog's poison-pill defence was successfully defended all the way to the Supreme Court. Steel has since quietly sold its stake in Bull-Dog.

Then there is the case of the Children's Investment Fund (TCI), a British hedge fund. In mid-May, the trade and finance ministries blocked TCI from doubling its 9.9% stake in J-Power, a big electrical utility. Although the ministries put their decision down to unspecified national-security concerns, it looks as if they feared that TCI would siphon off J-Power's cash as dividends and dash away, leaving the company ill-prepared to pay for building a nuclear power-plant and investing in its network. TCI responded by buying shares in companies that hold cross-shareholdings in J-Power, to press for change indirectly. And it vowed to kick up a stink when J-Power holds its annual shareholder meeting in June.

The Bull-Dog and J-Power squabbles are merely the latest and most visible conflicts between the Japanese business and political establishment and foreign investors. More than a quarter of Japanese shares are owned by foreigners, who account for more than 60% of the trading. Meanwhile, the stockmarket value of more than half the firms on the market's first tier is below their book value. In other words, they are worth more broken up and sold than they are as going concerns.

Things are so dire that eight big international investment funds, including Hermes—which together hold billions of dollars in Japanese equities—have called for sweeping reforms and greater shareholder democracy. They want Japanese firms to take on independent directors, refrain from introducing poison-pill defences, unwind defensive cross-shareholdings and unload their cash by increasing dividends, among other things. More than 600 firms had adopted poison-pill defences by 2007, twice as many as in 2006. And cross-shareholdings increased in 2006 and 2007, having fallen for almost a decade.

Yet the metaphor of shareholder democracy is misplaced, quips one government official, since Japan is barely a functioning political democracy: the ruling Liberal Democratic Party has been in power nearly continuously since 1955. Besides, he continues, Japanese managers treat all stakeholders equally: they do not only ignore shareholders, but everyone else too. As Alex Emery of Permira Advisers, a large British private-equity fund, puts it: “Japan is not just closed to foreigners—it's closed to everyone.”

Foreigners have been calling for change for years, to little effect. But lately there have also been calls for change within Japan. In May the Council on Economic and Fiscal Policy, an influential group appointed by the prime minister, put forward a series of proposals, the boldness of which is a strong rebuke to the insular ministries and their managers.

The first reform, devised by a group on foreign direct-investment (FDI) associated with the council, proposed making takeovers of Japanese firms easier, to attract more foreign capital. (Japan's cumulative FDI in 2006 was around 3% of GDP, compared with 14% in America and 45% in Britain.) The group also recommended reducing the tax burden. Japan's corporate-tax rate, at almost 40%, is one of the highest among rich countries.

Second, the council called upon the Tokyo Stock Exchange to establish new rules to discourage anti-takeover defences. Third, it proposed dividing Japan's $1.44 trillion public-pension scheme, the world's largest, into smaller funds and placing them in the hands of external fund-managers rather than retired bureaucrats. The idea is to revitalise the stockmarket, increase accountability and diversify risk, says Takatoshi Ito, an economist at Tokyo University who is on the council.

Investors are also taking action. Japan's Pension Fund Association (PFA), which invests $120 billion on behalf of 27m members, has startled Japanese bosses by voting against the renomination of directors at firms that earn a return on equity (ROE) of less than 8% for three consecutive years. (The average in Japan is around 9.5%, compared with 19% in America and Europe.)

Tomomi Yano, the director of the PFA, notes that the fund, around 65% of which is invested in Japan, produces a return of just 4%; in four years in the past decade it posted negative returns. That is a big problem in Japan, which has a shrinking workforce and a growing cohort of retired people. Of the 1,000 firms the PFA invests in, almost half did not make the grade and the PFA either voted down the directors or told them to improve their performance. “It needs to be a dialogue,” says Mr Yano.

Most promisingly, Japanese institutional investors are starting to hold bosses to account. In May Nikko Asset Management said it would oppose reappointing directors in cases where ROE falls below the industry average and the company does not present a plan to fix things. Daiwa has issued guidelines advising big firms not to list subsidiaries without placing outside directors on their boards, and Nomura and Nissay have developed guidelines covering ROE and takeover defences respectively. These moves are modest by Western standards, but in Japan they represent a big and welcome shift.

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Japan's business lobbies

Jockeying for influence

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Who speaks for corporate Japan?

SINCE it was founded in 1946, Japan's Keidanren, or “Business Federation”, has been one of the country's most powerful institutions. It was the mouthpiece of business interests and it told hands-on bureaucrats what was best for industry. In the same year, however, a second organisation formed: the Keizai Doyukai, or “Association of Corporate Executives”. It stayed in the shadow of its larger rival.

But lately its stature has been increasing. Japan's policy for cutting carbon emissions after 2012, for example, was based on the position of the Keizai Doyukai. As well as becoming more influential, the former underdog is also more progressive than the Keidanren. Rather than lobbying to prevent foreign takeovers, for example, the Keizai Doyukai favours foreign investment.

The reason for the divergence is partly organisational. The Keidanren's members are companies, and tend to take a cautious line. The Keizai Doyukai's members are individual executives, who are freer to take more progressive positions, since they do not represent their employers. Even their headquarters symbolise their differences: the Keidanren has its own building, a cement box from the 1960s; the Keizai Doyukai's modest office is in a chic, modern tower, and resembles a nightclub's VIP lounge.

The Keidanren's chairman is Fujio Mitarai, the head of Canon, a consumer-electronics giant. The Keizai Doyukai's chairman is Masamitsu Sakurai, who leads Ricoh, its rival. Mr Mitarai ran into controversy a few years ago over Canon's use of part-time employees, which pushed the limits of the law. Mr Sakurai, meanwhile, champions the rights of temps and part-timers, arguing that they should be paid the same as full-time employees for the same work.

Indeed, Mr Sakurai goes even further, calling for the end of Japan's seniority-wage system (in which salaries are based on length of service rather than performance). “It is important to maintain competitiveness among employees,” he says. It would also let Japanese firms compete for global talent, he says.

To be fair, some of Keidanren's policies are progressive, such as its call for greater competition in telecoms. Perhaps the Keizai Doyukai's rise indicates a growing appetite for competition, rather than consensus, in Japanese business.

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Mobile telecoms

Halfway there

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How to promote the spread of mobile phones among the world's poorest

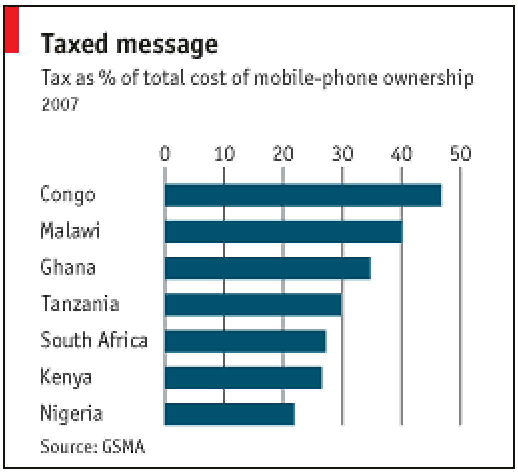
SOMETIME in the next few months, the number of mobile phones in use will exceed 3.3 billion, or half the world's population. No technology has ever spread faster around the globe: the mobile phone took less than two decades to reach this degree of penetration. But the ever-restless wireless industry has already set its sights on getting the other half connected. Two recent reports analyse how to add the “next billion” to the subscriber list.

In practice, that means finding ways to make mobile phones more affordable to people in the developing world, since most people in the developed world already have phones. The single largest barrier for would-be mobile subscribers, according to a report by Portio Research, a market-research firm, is the cost of a handset. So the industry has been doing its best to cut prices, with Motorola, an ailing American equipment-maker, taking the lead. Its cheapest phones now cost less than $30. John White of Portio believes that prices for simple, voice-only handsets could fall to $10 in five years.

But affordable phones are only part of the picture. Operators in developing countries have been inventive in their efforts to reach rural customers. In Bangladeshi villages “telephone ladies” rent out their handsets, one call at a time. China Mobile, the world's largest operator by subscribers, offers rural customers an agricultural-information service alongside the ability to make calls. Smart Communications, an operator in the Philippines, sells text messages for as little as $1.80 per 100 messages, and allows subscribers to pass airtime to phone “buddies” at a cost of less than $0.03 per minute.

For operators to make a profit at such low prices, network infrastructure must be cheap to install and operate. That is prompting innovation in base-stations as well as handsets. Operators have found ways to share network infrastructure to cut costs; equipment-makers have developed small, low-cost base-stations specially for use in the developing world.

There are also new business models, such as having a local entrepreneur run a base-station and provide services, including billing and handset maintenance. This is the idea behind “Village Connection”, a project launched by Nokia Siemens Networks, an equipment-maker. Ericsson, a rival company, meanwhile, has teamed up with Idea Cellular, an Indian operator, to use biofuel to power base-stations.



Yet even as the industry strives to make handsets and services cheaper, governments keep adding costs—mainly by levying taxes and customs duties. And these are particularly high in sub-Saharan Africa, according to a report released this week by Frontier Economics, a consultancy, at the behest of the GSM Association (GSMA), an industry lobby. The average ratio of tax payments to operator revenues is 30%. On average the mobile industry, which accounts for 4% of GDP, contributes 7% of national tax revenue.

This enthusiasm for taxation is easy to explain: governments have to tax something, and mobile phones are an easy target, since operators' billing systems do all the hard work. But treating mobile phones as a cash cow is shortsighted, says Gabriel Solomon of the GSMA, because mobile-specific taxes reduce demand. If governments did away with them and charged only VAT, tax revenues from the mobile industry would be around 3% higher by 2012, the report found, and the average penetration rate would increase from 33% to 41%. (Studies have found that in a typical developing country, an increase in mobile penetration of 10% boosts GDP growth by around one percentage point.)

Whether or not finance ministers are not convinced by such calculations, operators seem to be. Some have offered to guarantee tax revenues if mobile-specific levies are scrapped.

Even without this sort of measure, Portio predicts that global mobile penetration will reach 75% by 2011. A device that was a yuppie toy not so long ago has now become a potent force for economic development in the world's poorest countries. But more can be done to exploit it. Most governments say they are in favour of economic growth and broader access to communications. By cutting back on mobile-specific taxes and tariffs, they can help to promote both of those things.

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Economist.com BUSINESS

Telecoms in China

Rewired

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The long-awaited reorganisation of China's vast telecoms industry begins

BY ANY measure—revenues, employees, customers—it is the largest industrial reorganisation ever. And, reflecting how business is done in China, it was announced in the most modest way, with a posting on a government website on May 24th. The country's telecoms industry, with nearly 600m mobile subscribers, 360m fixed-line customers and $244 billion in revenue, will be reconfigured. Six companies will be collapsed into three, each spanning mobile, fixed and broadband services.

China Mobile, the world's largest mobile operator by subscribers, will merge with China TieTong, the smallest fixed-line operator. China Telecom, the country's biggest fixed-line operator, will acquire one of the mobile networks run by China Unicom, which will merge its remaining mobile operations with China Netcom, another fixed-line operator. A sixth operator, China Satcom, will be taken over by China Telecom.

The reorganisation had been expected for years, but rumours of an imminent decision swept the Hong Kong and Shanghai markets on May 23rd, provoking a panic that continued until May 27th. The shares of China Telecom, China Unicom and China Netcom were suspended, and those of China Mobile fell in value by 10%, or $31 billion. (The other two operators are unlisted.)

The main purpose of the plan is to create a more competitive industry—which means, in practice, taking China Mobile down a peg or two. It will gain a fixed-line arm, but that is no recompense for what it will give up: its lock on the massive mobile market, encompassing two-thirds of Chinese customers and an even higher share of new subscribers. Under the new rules, which have yet to be spelled out, it will face regulatory pressure to allow rivals into its market.

China Mobile is also likely to be hobbled in another way. The reorganisation will at last allow the Chinese government to grant licences for “third generation” (3G) mobile services, after years of delay. 3G gives operators more capacity and makes possible whizzy mobile-data services. But the government has delayed issuing the licences so that China's home-grown but long overdue 3G technology, called TD-SCDMA, can be used for at least one of the country's three networks. (The other two networks will use foreign standards which are already widely deployed elsewhere.) It is expected that China Mobile will be forced to adopt TD-SCDMA, an immature standard for which there is only a limited selection of handsets and equipment.

The reorganisation is the fourth since China first opened its telecoms industry to limited, state-orchestrated competition. Each time the government has arranged things to mirror the outcome produced by market forces in the West. The process has worked well in many ways: fees are low, access is broad and growth is strong. But will China's pursuit of industrial-policy goals now hamper the industry's progress?

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Economist.com BUSINESS

Retailing in India

Unshackling the chain stores

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India needs a supermarket revolution

IN THANE, a suburb of Mumbai, shoppers can enjoy the wide aisles and well stocked shelves of the HyperCity hypermarket, which offers food imported from Waitrose (a British supermarket chain), a demonstration kitchen, a cricket net for testing out a new bat or pads, and 30 cash registers that ring from 11am to 10pm, seven days a week. Customers can also savour the rare privilege of pushing their own trolleys and serving themselves from the shelves. They can, in other words, shop like people in most other countries.

But “organised retail”, such as hypermarkets, supermarkets and department stores, is still rare in India, accounting for just 4% of the country's $322 billion market. Most Indian shopping still takes place in millions of independent grocery shops, or *kirana* stores, manned by the owner and perhaps a put-upon assistant or two. And people hand-pick their fresh fruit and vegetables from hand-cart hawkers and pavement vendors.

What is holding the supermarket chains back? The government bars foreigners from investing in retailing, except for single-brand stores, in which they can own a 51% stake. This means Reebok can open a vast shop selling its shoes in Hyderabad; but Carrefour, a French supermarket giant, cannot set up shop. Worse, organised retailers must leap over as many as 33 regulatory hurdles, from signboard licences to anti-hoarding measures, before they open their doors. If they want to move goods out of some states, they must pay an exit tax. If they want to bring goods into others, they must pay an entry tax. Sometimes they must pay taxes, called *octroi*, even to move goods within a state.

India's small shopkeepers, often slow at the till, have been quick to man the barricades in defence of their turf. One of the larger protests drew some 20,000 traders, vendors and shopkeepers to central Mumbai in October. There is much strange talk about “retail dictatorship” and “corporate hijacks”. Is this all paranoia?

Stung by the protests, the government asked the Indian Council for Research on International Economic Relations (ICRIER), an independent think-tank, to measure the impact of organised retail on the disorganised sort. It unveiled its findings this week. When an organised retailer opens nearby, small retailers typically lose about 23% of their sales in the first year, the report finds. But after five years they are more or less back to where they started.

Only a tiny fraction of stores (1.7%) close down each year, and some even hire more people to improve their home-delivery service. Even five years from now, traditional retailers will control 85% of the market, the report projects. Retail dictatorship remains some years off.

The institute offers a number of suggestions to help independent retailers hold their own. The *kiranas* should gang up into co-operatives so that they can buy in bulk from suppliers. The government should also encourage banks to lend to them. Syndicate Bank, for example, allows small businesses to open so-called “pygmy” accounts, into which they pay their daily takings and against which they can borrow 25,000 to 150,000 rupees ($600-3,600).

And what about the shoppers? Surprisingly, households that earn less than 10,000 rupees a month save the most when organised retailers open up nearby, shaving about 10% from their shopping bills. They seem to cherry-pick the loss leaders and discount items in the supermarkets and discount stores, relying on smaller retailers for everything else. The rise of organised retail will save Indians money, even if it adds a little anomie.

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Chief executives

How to get to the top

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New research reveals the most popular routes into the executive suite

Illustration by Claudio Munoz

MARKETING used to be the route to the chief executive's chair, but the world has changed. Now, says Monika Hamori, professor of human resources at Instituto de Empresa in Madrid, it is finance chiefs who are most likely to get the top job, though experience in operations—running parts of the company—is also essential. CFO Magazine (a sister publication of *The Economist*) found in 2005 that one-fifth of chief executives in America were former chief financial officers, almost double the share of a decade earlier. The importance of quarterly financial reporting, and closer scrutiny since the imposition of the Sarbanes-Oxley corporate-governance act, have put CFOs in the limelight—and given them the chance to shine.

Another factor in reaching the top is whether you stay with the company you joined as a youngster. Ms Hamori's research (with Peter Cappelli of the Wharton School in Philadelphia) looked at companies in the S&P 500 and the FTSEurofirst 300. She finds that “lifers” get to the top in 22 years (in America) and 24 years in Europe. “Hoppers” who jump between four or more companies, by contrast, take at least 26 years on average to become chief executives. Insiders get promotions that reflect their potential, because their bosses have enough information to be reasonably confident about their ability. When executives switch from one company to another, however, they tend to move less far up the hierarchy, the researchers found.

The time taken to reach the top is falling. The average time from first job to chief executive fell from 28 years in 1980 to 24 in 2001. Successful executives are spending less time than they used to in each intermediate job—an average of four years—and they fill five posts on the way up, down from six. One reason for this acceleration is that company hierarchies are flatter than they used to be. Another important shift is the advent of female chief executives. In 2001 women accounted for 11% of bosses at leading American companies, according to the Hamori/Cappelli survey; in the early 1980s there were none.

Transatlantic differences

America is usually regarded as the home of raw capitalism, with youthful managers hopping from firm to firm and pushing their way to the top. But the Hamori/Cappelli study and another by Booz & Company, a consultancy, show that Europe is a more dynamic and harsher environment than America or Japan for chief executives. For a start, European chief executives are younger, with an average age of 54, compared with over 56 in America. The Hamori/Cappelli study shows that 26% of American bosses were lifers, compared with only 18% in Europe.

The Europeans also have a harder time once they get to the top. Booz & Company's annual survey of chief-executive succession shows that 17.6% of European bosses moved on last year, compared with 15% of Americans and 10% of Japanese. Chief executives, the survey found, last longer in America: the average tenure over the past decade was just over nine years. But in Europe the average tenure over the same period was less than seven years.

Moreover, a whopping 37% of changes at the top in Europe were more or less firings, according to Booz, compared with only 27% in America and 12% in Japan. Booz puts this down to the more recent tightening of corporate governance in Europe. Another Booz finding is common to both sides of the Atlantic: looking back over recent years, board disputes and power struggles lie behind a third of chief-executive firings. In short, shareholder activism is making its presence felt, putting pressure on bosses to perform.

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Eco-manufacturing

Get your green pants here

May 29th 2008 | COLOMBO
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A Sri Lankan firm says it has the world's first carbon-neutral clothes factory

AT A SPANKING new lingerie factory in Thulhiriya, a short drive from Colombo, Sri Lanka's capital, senior managers wear T-shirts. This is not because MAS Holdings, the country's biggest apparel company, which recently opened the factory, is a dress-down sort of a firm. It is because the factory has no air-conditioning. Instead it uses evaporative cooling, which leaves the workplace around four degrees hotter than air-conditioning would—but uses much less energy.

The factory has many energy-saving features. Its carefully designed windows provide enough natural light for workers stitching bras. Its turf roofs provide a cooling shade. Overall it uses 40% less energy than an ordinary factory of the same size. And the electricity it uses is from renewable sources: 90% from a hydro-power plant and 10% from on-site solar panels. MAS reckons it has built the world's first carbon-neutral clothes factory.

It was built at the instigation of Britain's biggest clothier, Marks & Spencer (M&S), which contributed £200,000 ($400,000) towards the cost of the solar panels and design. The “green” underwear that MAS is now making at the factory for M&S will reach British high streets in June, and will cost no more than existing garments.

For MAS, which had revenues of $700m last year, the “eco-factory” began as a branding experiment. Sri Lanka's textiles firms, which account for 67% of the country's industrial production, have higher costs than others in Asia, so they pick niches. MAS, for example, has grown by 20-30% a year over the past two decades by concentrating on complicated, high-value garments, such as lingerie for Victoria's Secret, an American apparel brand. In addition, MAS sells itself as an “ethical” employer—it certainly employs no children to stitch racy smalls for Victoria's Secret. Similarly, the eco-factory helps to tie in an image-sensitive client.

It is also good economics. The factory cost $7m to build, around 25% more than its traditional equivalent. That is partly due to a lot of fancy touches included to meet M&S's demand for an “iconic” factory. Stripped to its basic design, it would have cost about 15% over the odds. The factory's power also costs extra. But in a country that generates 65% of its electricity with imported oil—and saw power-price inflation of 30% in March—the extra costs are offset by energy savings. MAS expects the higher construction costs to have paid for themselves in less than five years.

For M&S, all this is part of “Plan A”, a five-year drive to become carbon-neutral and generally more “ethical” by 2012. M&S initially said this scheme would cost £200m, which it would recoup through higher sales. But the retailer said in May that in the current financial year Plan A would be “cost-neutral”—that is, the scheme has generated savings equal to the investments it requires. Next year the company expects it to be profitable.

It is not all glorious. M&S has had to shelve a plan to run lorries on biofuels because of worries that they are not as green as they seem. Nonetheless, the firm says it has reduced carbon-dioxide emissions from its British operations by 9%, despite opening 103 new stores. It has bought a fleet of 140 tear-shaped trailers, which use 10% less fuel and provide 16% more space than their less aerodynamic forebears.

“It's a very good brand investment for us, and it's not actually costing us any money,” says Mike Barry, M&S's head of corporate responsibility. For all that, he will not say how much M&S is actually investing in its green scheme. It would be interesting to know.

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Private equity in Austria

Fending off the locusts

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Will an American private-equity firm buy Vienna's Ferris wheel?

“HANDS off our Viennese giant wheel,” says Heinz-Christian Strache, the combative boss of the far-right Austrian Freedom Party. On May 20th Merlin Entertainments, a British amusement-park operator owned by Blackstone, an American private-equity company, said it was in talks with the owners of the giant Ferris wheel in the *Wurstelprater*, an amusement park in the centre of Vienna. The wheel, built in 1897 to commemorate the 50th anniversary of the accession of Emperor Franz Joseph I to the Habsburg throne, is one of Vienna's best-known landmarks. It must stay in Viennese hands, says Mr Strache, otherwise it will only be a short step to renting out the Hofburg Imperial Palace to the French.

Despite an outcry from Austria's populist politicians and the local media, Merlin and Blackstone have not said anything about their plans for the Ferris wheel. Peter Petritsch, one of its owners, said he was happy to talk to Merlin, but would prefer to rent the wheel rather than sell it outright. Merlin, the owner of the Legoland theme parks, the London Eye (another Ferris wheel) and Madame Tussauds, a group of wax museums, has yet to invest in Austria.

Private equity in the Alpine republic is still in its infancy, but has become big business in neighbouring Germany over the past decade. So far private-equity investment has not caused much controversy in Austria, with the exception of the takeover in 2006 of BAWAG, a troubled bank, by Cerberus, an American outfit. But public opinion towards private equity in Germany is much more hostile, after a fierce debate in 2005 over whether hard-nosed private-equity investors—branded “locusts” by a politician—were good for the country.

Blackstone and its subsidiary are keen to avoid an Austrian locust debate, and are gauging public opinion before deciding on their next move. Meanwhile Mr Strache continues to issue dark warnings about Merlin's plans to put pictures of London's Tower Bridge and Big Ben into the wheel's gondolas. Perhaps the xenophobic party boss should read up on his city's history. Vienna's wheel was designed by Walter Bassett—a Briton.

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Face value

Ringing off

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Arun Sarin has seen off his critics and is leaving Vodafone in good shape

AP

WHEN Arun Sarin took over in July 2003 as chief executive of Vodafone, the world's largest mobile operator by revenues, there was general agreement about what needed to be done—and that he was the right man to do it. His swashbuckling predecessor, Sir Christopher Gent, had transformed Vodafone from an obscure British firm into a global giant through a series of daring acquisitions, most famously the hostile takeover of Mannesmann, a German operator, in 2000. After all this empire-building, the theory went, Vodafone needed an administrator to come in and quietly fit the pieces together. The industry was also on the verge of launching its much-hyped “third generation” (3G) services, which would require a steady hand, attention to detail and operational rigour.

Mr Sarin, who had a reputation for this sort of thing from his days as chief operating officer at AirTouch, an American operator that Vodafone had bought in 1999, seemed the perfect choice. But things did not quite work out as expected. Mr Sarin, who announced on May 27th that he intends to stand down as chief executive in July, has had a bumpy ride. But he will leave the company in good shape, and his reign has been a success—just not in quite the way that people originally anticipated.

Things began as expected. When Mr Sarin took over, the clear priority was to get Vodafone's local affiliates working as a whole. “We had not done that, and frankly it was quite a sore point,” he says. So he started by revamping the organisation, binding the companies together and untangling the backroom spaghetti to simplify and standardise operations—and reduce costs.

But after a year or two it became clear that quietly fitting the pieces together would not be enough. Vodafone's shares were doing worse than those of its rivals, and repeated attempts to turn things round at its troubled Japanese unit had failed. Investors also wanted Mr Sarin to sell the company's stake in Verizon Wireless, a big American operator. It used a different wireless technology, so there was little scope for exploiting scale economies in purchasing; nor could Vodafone, as the minority partner, exploit its brand in America. Along with the problems in Japan, this highlighted the limits to Vodafone's global ambitions.

Mr Sarin's most difficult period came in mid-2006, “when people were calling for his head”, says Damien Chew, an analyst at ING, an investment bank. There was infighting on the board worthy of a medieval court, and it ended only when Mr Sarin purged his predecessor's lieutenants. Some 10% of shareholders voted against his reappointment at the firm's annual meeting. Vodafone's mobile-only model, which once seemed visionary, began to look outdated, as the industry embraced “convergence” between fixed-line, mobile, broadband and television services. And 3G was not yielding the expected returns in Europe.

It was a close-run thing. In retrospect Mr Sarin's problem was that he had chosen the right new strategy—reducing Vodafone's dependence on developed markets, and moving instead into high-growth emerging markets—but it was not what unhappy investors wanted to hear. He began the shift in mid-2005, taking control of operators in the Czech Republic and Romania and then acquiring Telsim, a Turkish operator, in December. Many investors were livid: Vodafone's acquisition spree was supposed to be over, and Mr Sarin was accused of paying far too much for Telsim. But if he had spelled out his new ideas in early 2006, says Mr Chew, “there would have been a lot of scepticism”.

For a while Mr Sarin's survival was in doubt, but he soothed his critics by selling Vodafone's ailing Japanese unit and toughed it out until the strong growth of Vodafone's new divisions in eastern Europe and Turkey had demonstrated his new strategy's potential. He also switched from a “mobile-only” to a “mobile-plus” approach, offering fixed-line services in some markets. His strategic shift was crowned by the acquisition of Hutchison Essar, an Indian operator, in February 2007. Vodafone swiftly integrated the company and successfully exploited its scale and operational expertise to provide cheap handsets and expand coverage. It was partly down to luck, but Mr Sarin's survival ultimately proved to be in shareholders' long-term interests. Had he given in to short-termists who wanted to sell Vodafone's American unit, he says, there would have been pressure to sell off other assets, and “Vodafone would not exist as a company today.”

Out of India

It seems fitting that it was the acquisition of an Indian firm that sealed the turnaround in Mr Sarin's fortunes. Born and raised in India, the son of a well-to-do military officer, he took an engineering degree at the Indian Institute of Technology, before moving to California, where he did a further degree and an MBA and became an American citizen. Mr Sarin's Indian roots were an asset during the fight for Hutchison Essar. And in retrospect, having an Indian-American running Vodafone was exactly the right choice for a company that is now trying to bridge mature and developing markets. This week the group reported strong financial results, and it recently reported that it now has more customers outside western Europe than within it.

Mr Sarin's successor will be his deputy, Vittorio Colao, an Italian who runs Vodafone's European operations. As well as continuing today's strategy with further acquisitions in Africa and Asia, says Mr Sarin, Mr Colao must work out how to compete and co-operate with industry giants such as Nokia, Google and Microsoft as the internet goes mobile, and new mobile-advertising markets open up. “His big challenge is to figure out that bit,” says Mr Sarin. He thinks Mr Colao's experience in the media industry will prove an asset. For his part, Mr Sarin says he has not decided what to do next. But having seen off his critics and fixed Vodafone's new course with an acquisition in the country of his birth, it clearly seemed like a good moment to ring off.

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Energy

Double, double, oil and trouble

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AFP

Is it "peak oil" or a speculative bubble? Neither, really

AFTER oil hit its recent record of $135 a barrel, consumers and politicians started to lash out in every direction. Fishermen in France have been blockading ports and pouring oil on the roads in protest. British lorry drivers have paraded coffins through London as a token of the imminent demise of the haulage industry. In response, Gordon Brown, Britain's prime minister, is badgering oil bosses to increase production from the North Sea, while Nicolas Sarkozy, the president of France, wants the European Union to suspend taxes on fuel.

In America, too, politicians are haranguing oil bosses and calling for tax cuts. Congress has approved a bill to prevent the government from adding to America's strategic stocks of oil, and is contemplating another to enable American prosecutors to sue the governments of the Organisation of the Petroleum Exporting Countries (OPEC) for market manipulation.

But the most popular scapegoats are "speculators" of the more traditional sort. OPEC itself routinely blames them for high prices. The government of India is so sure that speculation makes commodities dearer that it has banned the trading of futures contracts for some of them (although not oil). Germany's Social Democratic Party proposes an international ban on borrowing to buy oil futures, on the same grounds. Joe Lieberman, chairman of the Senate's Homeland Security Committee, is also mulling regulation of some sort, having concluded that "speculators are responsible for a big part of the commodity price increases". The assumption underlying such ideas is that a bubble is forming, and that if it were popped, the price of oil would be much lower.

Others assume the reverse: that the price is bound to keep rising indefinitely, since supplies of oil are running short. The majority of the world's crude, according to believers in "peak oil", has been discovered and is already being exploited. At any rate, the size of new fields is diminishing. So production will soon reach a pinnacle, if it has not done so already, and then quickly decline, no matter what governments do.

As different as these theories are, they share a conviction that something has gone badly wrong with the market for oil. High prices are seen as proof of some sort of breakdown. Yet the evidence suggests that, to the contrary, the rising price is beginning to curb demand and increase supply, just as the textbooks say it should.

Stocks, bonds and barrels

Those who see speculators as the culprits point to the emergence of oil and other commodities as a popular asset class, alongside stocks, bonds and property. Ever more investors are piling into the oil markets, the argument runs, pushing up the price as they do so. The number of transactions involving oil futures on the New York Mercantile Exchange (NYMEX), the biggest market for oil, has almost tripled since 2004. That neatly mirrors a tripling of the price of oil over the same period.

But Jeffrey Harris, the chief economist of the Commodity Futures Trading Commission (CFTC), which regulates NYMEX and other American commodities exchanges, does not see any evidence that the growth of speculation in oil has caused the price to rise. Rising prices, after all, might have been stimulating the growing investment, rather than the other way around. There is no clear correlation between increased speculation and higher prices in commodities markets in general. Despite a continuing flow of investment in nickel, for example, its price has fallen by half over the past year.

By the same token, the prices of several commodities that are not traded on any exchange, and are therefore much harder for speculators to invest in, have risen even faster than that of oil. Deutsche Bank calculates that cadmium, a rare metal, has appreciated twice as much as oil since 2001, for example, and the price of rice has risen fractionally more.

Investment can flood into the oil market without driving up prices because speculators are not buying any actual crude. Instead, they buy contracts for future delivery. When those contracts mature, they either settle them with a cash payment or sell them on to genuine consumers. Either way, no oil is hoarded or somehow kept off the market. The contracts are really a bet about which way the price will go and the number of bets does not affect the amount of oil available. As Mr Harris puts it, there is no limit to the number of “paper barrels” that can be bought and sold.

That makes it harder for a bubble to develop in oil than in the shares of internet firms, say, or in housing, where the supply of the asset is finite. Ultimately, says David Kirsch of PFC Energy, a consultancy, there is only one type of customer for crude: refineries. If speculators on the futures markets get carried away, pushing prices so high that refineries run at a loss, they will simply shut down, causing the price to fall again. Moreover, speculators do not always assume that prices will rise. As recently as last year, the speculative bears on NYMEX outweighed the bulls.

There is, admittedly, a growing category of inherently bullish investment funds that seek to track commodity-price indices, in which oil is usually the biggest component. Politicians have begun to denounce these “index funds”, since they make money for their investors only if prices rise. According to Mr Lieberman, they have grown in value from $13 billion to $260 billion over the past five years. This surge of investors betting on rising prices, many observers contend, has become a self-fulfilling prophecy, helping to push prices ever higher and thus attract yet more investment.

But Bob Greer, of PIMCO, an asset-management firm, argues that even index funds make unlikely suspects. For one thing, they too invest in futures, rather than in physical supplies of oil. So every month, they must trade contracts that are about to fall due for ones that will not mature for several months. That makes them big sellers of oil for prompt delivery.

What is more, their growth is not as impressive as it first appears. Paul Horsnell of Barclays Capital, an investment bank, puts the total value of index funds and other similar investments at $225 billion. That is less than half the market capitalisation of Exxon Mobil, he points out, and a tiny fraction of the $50 trillion-odd of transactions in the oil markets each year. Although index funds have grown quickly, that growth stems in large part from the rise in value of the futures they hold, rather than from fresh investment flows. He estimates that index funds swelled by $13 billion in the first quarter of this year, for example, of which all but $2 billion derives from the rise in commodity prices.

Back to basics

Mr Harris of the CFTC, for one, believes that the oil price is still a function of supply and demand. For the past few years, the world's production capacity has grown only sluggishly. Meanwhile, demand, especially from the developing world, has been growing faster. So there is hardly any slack in the system. Only Saudi Arabia and the United Arab Emirates are thought to be able to increase their output from today's levels, and even then, there are doubts, since Saudi Arabia, in particular, is secretive about the state of its oil industry.

That leaves the oil market at the mercy of even small disruptions to supply. Prices tend to jump each time militants sabotage an oil pipeline in Nigeria, bad weather threatens production in the Gulf of Mexico, or political clouds gather over the Persian Gulf.

The problem is exacerbated by a growing mismatch between the type of oil being produced and the refineries that must process it. The most common benchmark prices, including the one used in this article, refer to “light” crude, the least viscous sort, which produces the most petrol and diesel when refined. “Heavy” oil, by contrast, yields more fuel oil, which is used mainly for heating.

At the moment, diesel is in short supply and there is a glut of fuel oil. That makes processing heavy oil unprofitable for some refineries, since the gains from diesel are outweighed by losses on fuel oil. As refineries turn instead to lighter grades, it pushes their prices yet higher. The discount on heavier crudes has risen to record levels. But even then, points out Ed Morse, of Lehman Brothers, another investment bank, Iran is having trouble selling the stuff. It is storing huge quantities of unsold oil on tankers moored off its coast.

Presumably, Iran and other heavy-oil producers will eventually be obliged to drop prices far enough to make processing the stuff worth refiners' while. In the longer run, more refineries will invest in the equipment needed to crack more diesel out of heavy oil. Both steps will, in effect, increase the world's oil supply, and so help to ease prices.

But improving an existing refinery or building a new one is a slow and capital-intensive business. Firms tend to be very conservative in their investments, since refineries have decades-long life-spans, during which prices and profits can fluctuate wildly. It can also be difficult to find a site and obtain the right permits—one of the reasons why no new refineries have been built in America for over 30 years. Worse, new kit is becoming ever more expensive. Cambridge Energy Research Associates (CERA), a consultancy, calculates that capital costs for refineries and petrochemical plants have risen by 76% since 2000.

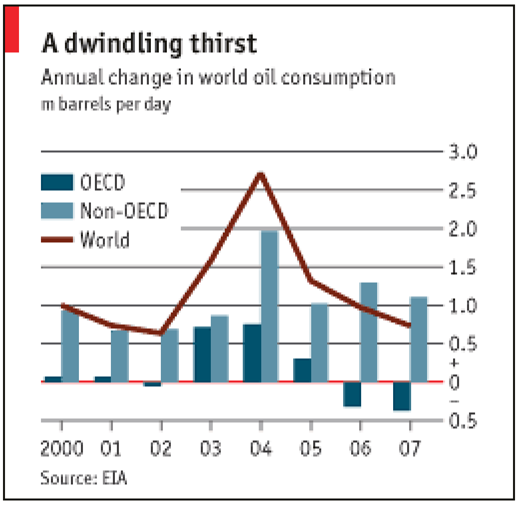
Much the same applies to the development of new oilfields. CERA reckons that the cost of developing them has risen even faster—by 110%. At the same time, oilmen remain scarred by the rapid expansion of output in the late 1970s, in response to previous spikes in prices, that led to a glut and so to a prolonged slump. Exxon Mobil claims that it still assesses the profitability of potential investments using the same assumptions about the long-term oil price as it did at the beginning of the decade, for fear that prices might tumble again. Environmental concerns are also an obstacle: America, for one, has banned oil production off most of its coastline.

Increasing nationalism on the part of oil-rich countries is adding to the difficulties. Geologists are convinced that there is still a lot of oil to be discovered in the Middle East and the former Soviet Union, but governments in both regions are reluctant to give outsiders access. Elsewhere, the most promising areas for exploration are also the most technically challenging: in deep water, or in the Arctic, or both. Although there have been big recent discoveries in such places, they will take longer to develop, and costs will be higher. The most expensive projects of all involve the extraction of oil from bitumen, shale and even coal, through elaborate processing. The potential for these is more or less unlimited, although analysts put the costs as high as $70 a barrel—more than the oil price this time last year.

Nonetheless, PFC Energy has examined projects that are already under way, and concluded that global oil production will grow by over 3m barrels a day (b/d) over the course of this year and next. In particular, it expects production outside OPEC to grow by about 500,000 b/d both years—a marked increase from the near stagnation of recent years.

Meanwhile, the high price is clearly beginning to crimp demand. The growth in global consumption last year was barely a quarter what it was in 2004 (see chart); this year, it is likely be even lower. In rich countries (or at least among the members of the Organisation for Economic Co-operation and Development (OECD), a rough proxy), the effect is even more pronounced. Consumption has been falling for the past two and a half years.

Poorer countries' demand for oil is still rising, albeit at a slowing pace. That is partly because their economies are growing faster, and partly because their consumers are shielded from the rising price through subsidies. But the increasing expense of such measures is forcing governments to water them down or scrap them altogether (see article). That, in turn, should further sap consumption.



Oil pique

China's growing thirst for oil is often put forward as one of the main factors behind today's higher oil prices. Demand for diesel there, for example, rose by over 9% in the year to April. But Mr Morse argues that such growth might not last. The government has ordered oil firms to increase their stocks of fuel by 50% to be sure there are no embarrassing shortages during the Olympics. It is also planning to run some power plants near Beijing on diesel rather than coal, in an attempt to reduce pollution during the games. These measures are helping to boost China's demand for diesel, but the effect will be transitory.

In the short run, neither demand for nor supply of oil is very elastic. It takes time for people to replace their old guzzlers with more fuel-efficient cars, or to switch to jobs with shorter commutes, or to move closer to public transport. By the same token, it can take ten years or more to develop an oilfield after its discovery—and that does not include the time firms need to bolster their exploration units.

Gary Becker, an economist at the University of Chicago, has calculated that in the past, over periods of less than five years, oil consumption in the OECD dropped by only 2-9% when the price doubled. Likewise, oil production in countries outside OPEC grew by only 4% every time the price doubled. But over longer periods, consumption dropped by 60% and supply rose by 35%. The precise numbers may be slightly different this time round, but the pattern will be the same.

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Fuel subsidies

Crude measures

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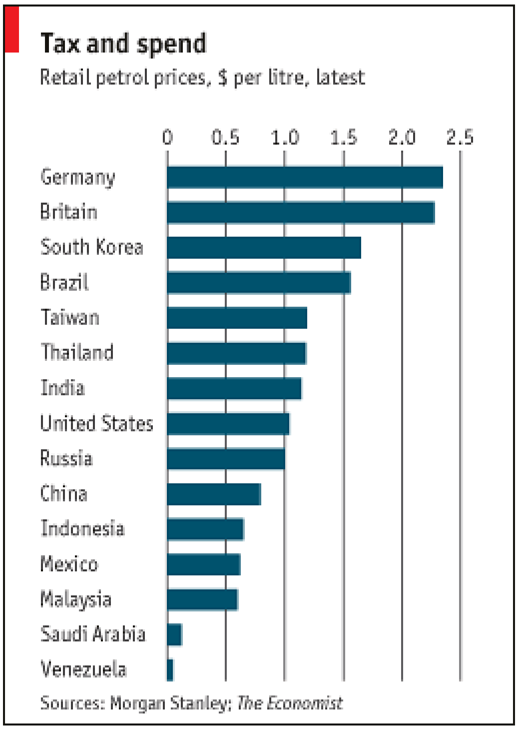
Not everybody is paying higher prices for oil



HALF of the world's population enjoys fuel subsidies. This estimate, from Morgan Stanley, implies that almost a quarter of the world's petrol is sold at less than the market price. The cheapest petrol is in Venezuela, at 5 cents per litre. That makes China's pump price of 79 cents seem expensive, but even this is a bargain compared with $1.04 in the United States and $2.35 in Germany (see chart).

As the gap has widened between soaring international prices and fixed domestic prices, so has the cost of subsidies. Indeed, budgetary strains are now forcing some governments to lift prices. On May 24th Indonesia raised fuel prices by around 30%. This was the first increase since 2005, but it still leaves petrol too cheap at 65 cents a litre. Dearer oil is likely to push up inflation from 9% to 12%. But without the increase, the government's subsidy bill was heading for an alarming 3% of GDP this year. In the past week Taiwan has also raised petrol prices by 13% and Sri Lanka has lifted them by 24%.

Malaysia has one of the biggest fuel-subsidy bills in the world, estimated at as much as 7% of GDP this year. By holding down the price of petrol, Malaysia now has the lowest inflation rate of all the 32 emerging economies tracked by *The Economist*. But the government is expected to allow prices to rise soon to curb its widening budget deficit.

In theory, rising crude-oil prices should reduce global demand. But if domestic prices are capped, then emerging economies will continue to guzzle oil, pushing world prices still higher. Emerging economies accounted for more than the whole increase in world oil consumption last year—because demand in the rich economies fell. But recent price increases will make little difference to global consumption unless China and India follow suit.

India's state-owned oil companies face mounting losses, as they are forced to sell fuel at fixed prices below cost. Petrol prices are actually slightly higher in India than in the United States, because Indian motorists pay much higher fuel taxes, but diesel is about 40% cheaper than in America. The oil firms are partly compensated by bonds which the government issues to them—a trick which allows the government to keep the subsidy off its books. At today's prices, the total subsidy (including the full losses of oil companies) could be as much as 2-3% of GDP this year. Morgan Stanley estimates that the government's total budget deficit (central and state governments and all off-budget items) is running at 9% of GDP in this fiscal year. The government must hold an election by May next year, so it is reluctant to raise fuel prices by much. It is thought to be considering a modest rise combined with a cut in excise duty.

In early 2008 Chinese motorists paid roughly the same for their petrol as Americans did. Whereas the pump price in America has since jumped by 33%, Chinese prices have remained fixed, swelling the losses of state-owned refiners. According to Dragonomics, a Beijing-based economic research firm, the retail price for diesel is about 40% below that in America. To cut their losses, oil firms have reduced supply, causing shortages at some petrol stations. However, China is less likely than other countries to lift prices soon. Oil subsidies are estimated at less than 1% of GDP, and its budget surplus and small public debt mean that the government can afford to keep prices down for some time. Most likely, it will delay increasing fuel prices until food-price inflation has eased.

Across the emerging world, governments fear that lifting fuel prices will hurt the poor and so trigger social unrest. Yet fuel subsidies are an inefficient way to protect the poor: they mainly benefit the richer owners of cars and air-conditioners, and favour energy- and capital-intensive industries, rather than those that create most jobs. An IMF study of five emerging economies found that the richest 20% of households received, on average, 42% of total fuel subsidies; the bottom 20% received less than 10%. That money would be better spent on health, education and infrastructure. Not only would this benefit the poor, but higher prices would also help to dampen global oil consumption, and hence the price of oil.

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Stock exchanges

The battle of the bourses

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Illustration by Satoshi Kambayashi

Exchanges have gained from merger speculation and rising trading volumes. But competition from whizzy new markets is starting to spoil the party

"ARGUABLY, there's never been a better time to be an exchange business," enthused Clara Furse, chief executive of the London Stock Exchange (LSE), on May 22nd after unveiling record profits. The past few years have been a golden era for the world's bourses: their own share prices lifted on a wave of mergers; trading volumes, already rising smartly, sent into orbit as investors sought to profit from the volatility triggered by the credit crunch.

But Ms Furse's joy is not unconfined. The LSE's share price has fallen by half since January. NYSE Euronext, which runs New York's exchange and several European markets, is down by 30%. Since March the volume of trading it handles has tumbled, even as the overall market has surged. NASDAQ, its cross-town rival, has seen turnover drop to its lowest level since 2004. Why is this happening?

The main culprit is competition. In America electronic upstarts have been nipping at the exchanges' heels for years. They got a fillip last year with the introduction of Reg NMS, a rule that forces trades to be sent to the venue offering "best execution". (The European Union's new MiFID directive does much the same.) The old exchanges' share of the market is rapidly eroding: in America it stood at 73% in April, down from 86% a year before.

The competition comes in two forms. The first is electronic markets that aspire to become full exchanges. In America BATS and DirectEdge are the trail-blazers, having grabbed a combined 13% of all matched trades at last count. The leader in Europe is Chi-X, launched in March 2007, and the closest thing to a pan-European electronic market. At times its share of British and German trades tops 13% and 6% respectively. Other platforms, such as the much-hyped Turquoise, are preparing for their launches.

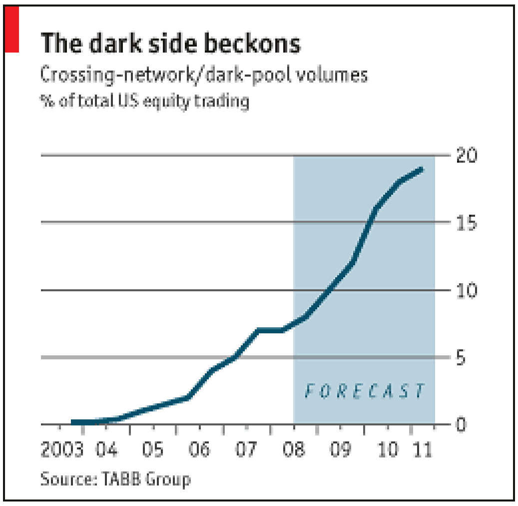
These networks are typically backed by consortia of banks that were once in bed with the established exchanges as their member-owners. By stimulating competition, the banks hope to force the exchanges to cut their fees. These remain particularly expensive in Europe, where the cost of trading is, on average, three times higher than in America.

The new lot tout several advantages. With no legacy technology weighing them down, their platforms are ultra-fast. Chi-X, for instance, can complete trades at up to ten times the speed of older rivals, and more reliably. This appeals to high-frequency algorithmic traders at hedge funds and specialist brokers, an increasingly important constituency for whom a millisecond is an aeon.

They are cheaper, too, not least because they have been offering generous rebates to “liquidity providers” that post quotes. Chi-X has gone a step further, offering slivers of equity to its heaviest users. Such user-friendly tactics are hard for the exchanges to match without angering their shareholders. “They're still struggling to figure out how much liquidity is sticky and how much price-sensitive,” says Larry Tabb of TABB Group, a consultancy.

Speed and price are not everything, however. In August and January the share of trades done electronically on NYSE fell from 90% to as low as 60-70%. At times of stress “people realise milliseconds don't matter”, argued Duncan Niederauer, the exchange's boss, in a recent speech. “It's better to get it right.”

The second type of competition comes from “crossing networks” and “dark pools”, two forms of private market used to trade large blocks of shares away from the glare of the exchanges. Some investors like them because they conceal the buyer's identity and the price, reducing the risk of the market moving against them as others react. Dozens of these markets are up and running. In America they are expected to account for one-fifth of all share-trading in three years' time (see chart).



Although this free-for-all provides sought-after anonymity, the market as a whole may suffer from the fragmentation of liquidity. Banks are starting to address the problem. This month Goldman Sachs, Morgan Stanley and UBS agreed to offer each other access to their pools, using computer programs that roam from network to network looking for matching buy and sell orders. “Technology is solving the problem of splintered liquidity as it arises,” says one participant.

Full mergers among dark pools may be next. Some see parallels with the late 1990s, when the first generation of electronic-trading networks consolidated, or were bought by exchanges looking to get ahead in the technological arms race. Both NASDAQ and the NYSE are cutting deals with dark pools. Mr Niederauer sees an opportunity to “reaggregate” markets.

Some exchanges are even quietly creating dark pools of their own, buried within their main market. Their reluctance to publicise this is understandable: although it helps them to hold on to business, it irks some of their big customers, whose own bids may be trumped by the service. Other counter-attacking measures are less surreptitious. Some bourses, such as Deutsche Börse and NASDAQ, have bought options exchanges, which enjoy bigger margins than pure stockmarkets. NYSE Euronext, which already has Liffe, a futures exchange, is looking to expand its business in derivatives (though it also needs to realise the transatlantic market it promised when it formed in 2006, and to plug gaps in its global network).

The exchanges have two more cards up their sleeves. One is to launch markets that the upstarts cannot. NASDAQ, for instance, has PORTAL, a marketplace for “144a” securities, which only sophisticated investors may trade. The other is to develop listings—the business in which brand counts most—by, for instance, offering in-house research for smaller stocks.

In America the battle between newcomers and old guard is already firmly joined. Across the Atlantic horns are only just starting to lock. As the head of trading at one Wall Street bank puts it: “Some incumbents, particularly in Europe, have had it their own way for so long that they still don't understand what's coming.”

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Economist.com FINANCE & ECONOMICS

Buttonwood

Not so vigilant

May 29th 2008
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The puzzle of low Treasury-bond yields

Illustration by Satoshi Kambayashi

THE yield of Treasury bonds is arguably the single most important indicator in financial markets. Since the American government is unlikely to default, the bond yield sets the risk-free rate against which other assets are measured. It also serves as a barometer of investors' feelings about economic variables like inflation and recession.

But precisely because it does so many things, the Treasury bond can send out conflicting signals. Consumers have been grumbling about the inflationary impact of higher oil and food prices for a while. But bond investors have only recently taken fright, pushing the yield on the 10-year Treasury bond above 4% on May 28, for the first time since the start of the year. Even now, however, the breakeven inflation rate (the difference between yields on conventional and inflation-linked bonds) on five-year Treasury issues is just 2.4%, within the range it has occupied for the past four years; compare that with the 7.7% inflation rate that American consumers expect over the next 12 months.

One possibility is that the "bond-market vigilantes" have been asleep. "We sometimes wonder if Treasury-bond investors enjoy losing money," muses Tim Bond, a strategist at Barclays Capital, as he ponders the logic of owning ten-year Treasuries yielding close to 4% when headline inflation is heading (on his view) for more than 5% by August.

Bill Gross of Pimco, a bond-market investor, argues that inflation is understated in the official American figures because of statistical adjustments made over the past 25 years. The result may be that investors have been fooled into buying Treasury bonds on unrealistic expectations of real (after-inflation) yields.

Another possibility is that breakeven rates are not an effective measure of investors' inflation expectations. That is the view of Jack Malvey, a strategist at Lehman Brothers. He argues that yields on inflation-linked bonds have been distorted over the past decade by demand from pension funds, which see the bonds as an ideal way to match their liabilities.

A third option is that bond investors think today's inflation rates are a blip. "Inflation may be an issue now but it likely won't be over the next ten years," says Pavan Wadhwa, head of European rates strategy at JPMorgan Chase. Optimists argue the anti-inflation credibility of central banks is stronger than in the 1970s. And they note that high oil prices, although they push up inflation in the short term, ultimately tend to act as a tax on growth.

The credit crunch may also be having lingering effects. Bond yields reached their low in mid-March when the Bear Stearns crisis was in full swing. At that point, the ten-year Treasury bond yielded just 3.31%, the lowest level in five years. Investors were fleeing the riskier debt of bank and other corporate borrowers for the safety of government paper.

Yields have moved up by more than half a percentage point since then, as investors have started to move money out of government bonds and back into the equity market. But recessionary fears still linger, especially when investors are bombarded with statistics such as the continued fall in American house prices and the decline in consumer confidence. It may still be worth holding Treasury bonds yielding around 4% as a hedge against a sharp economic downturn.

In short, the bond market is caught in an awkward compromise, with worries about the financial and economic outlook balancing concern about inflation.

In the medium term, however, it is hard to argue with Lehman's Mr Malvey when he says that he expects yields in some government-bond markets to rise by two-to-three percentage points over the next two or three years. Although the world may not be about to return to the excesses of the 1970s, the Goldilocks era is tapering off: the trade-off between growth and inflation has deteriorated.

Nor have Treasury-bond investors exactly been coining it in recent years. According to Barclays Capital, the annualised real return since the start of 2003 has been a meagre 1%. Will the Chinese, with a domestic inflation rate of 8.5%, really want to hold bonds yielding 4% in a currency they expect to depreciate against the yuan? Is the anti-inflationary credibility of the Federal Reserve really that convincing when it is clear that its rate decisions can be driven by concern for the health of the banking sector? Indeed does it make sense for German ten-year bonds to yield more than Treasuries when the inflationary rhetoric of the European Central Bank looks much more hawkish?

Veteran investors may recall 1962, when the Treasury-bond yield was less than 4%. Those who bought bonds then earned negative real returns over the succeeding five-, ten- and 20-year periods. They should be very careful about making the same mistake again.

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Latin American equity markets

Samba v Ranchero

May 29th 2008 | MEXICO CITY AND SÃO PAULO
From The Economist print edition

As stockmarkets go public, Mexico struggles to keep up with Brazil

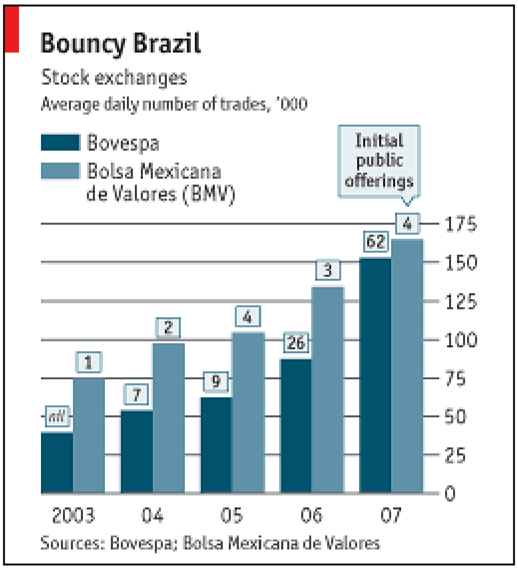
SINCE the Stockholm Stock Exchange paved the way in 1993, the world of bourses has been swept by a wave of “demutualisation”, in which exchanges have become publicly held corporations. Of the world's five largest stock exchanges, only Tokyo is still owned by its member brokerages. Latin America is the latest region to catch the bug.

The Bolsa Mexicana de Valores (BMV), the Mexican exchange, is planning an initial public offering (IPO) for mid-June, and is hoping to raise something like $200m within Mexico and another $200m or so in America. The IPO will not be a full demutualisation—the 19 partners, including a roster of international banks and Mexican financial firms, that now own the exchange will dilute their holding to just over half.

These numbers are dwarfed by a pair of listings that took place in Brazil last year. Bovespa, Brazil's main stock exchange, and the Bolsa de Mercadorias & Futuros (BM&F), Brazil's commodities and futures exchange, both went public in 2007. On May 8th they merged to become the second-largest exchange in the Americas. The size of the Brazilian markets has attracted foreign interest: the merged stockmarket has an alliance with the Chicago Mercantile Exchange, which is a big shareholder. The tie-up allows a trader sitting in London to buy and sell Brazilian securities through Chicago's Globex trading system. Conversely, a Brazilian trader wanting to hedge against swings in the price of soya beans, say, can trade in the biggest futures market in the world.

The Mexican market remains much more limited by comparison. Although Brazil's economy is only 45% larger than Mexico's, firms listed on the Bovespa had a total 2007 market capitalisation (on average) of $1.4 trillion, more than three times the BMV's tally. Look at growth (see chart) and the differences become yet more stark. The BMV had four IPOs in 2007; Bovespa had 62. Trading volumes have been growing faster in Brazil, which is also the more alluring destination for foreign capital. BlackRock, a mutual-fund manager, is not unusual in having 70% of its Latin American portfolio invested in the country.

The extent of these disparities looks odd. Mexico's derivatives market has done well, with more peso futures now traded in Mexico than in Chicago. Corporate debt has also grown healthily on Mexican bond markets. Part of the reason for Mexico's relative weakness is technical: although property is one of the country's growth areas, unhelpful tax rules have impeded listed real-estate investment vehicles.



A bigger problem is the power of near-monopoly firms and large family holdings. It is difficult to reach an exact figure, but one Mexican financial analyst reckons that Carlos Slim, by some accounts the world's richest man, controls close to 50% of the value of shares traded on the BMV. “How can you have an active IPO market when you have these big fat companies that dominate everything and stifle the next generation of companies?” he asks.

Salvation may lie abroad. André Cappon of CBM, a consultancy, reckons that the global exchanges business will eventually by dominated by three or four multinational constellations. Gazing up at them from the gutter will be the small national exchanges that are the norm in most of Latin America. In the middle there will be satellites, like Singapore and Brazil. Mexico's best hope for its markets, reckons Mr Cappon, lies north, in a tie-up with one of the exchanges in America.

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Economist.com FINANCE & ECONOMICS

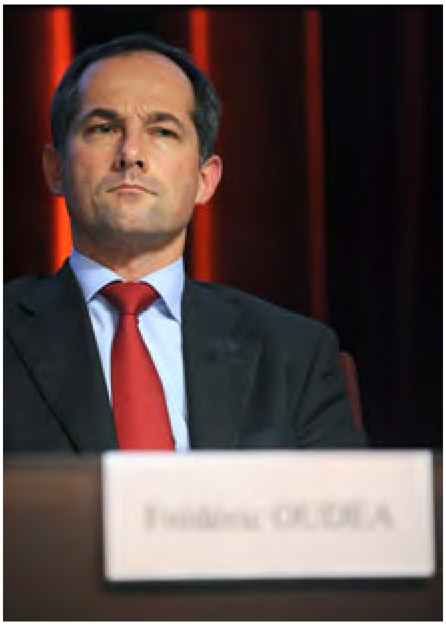
Société Générale

After JK

May 29th 2008
From The Economist print edition

The Kerviel trading scandal was bad. It could have been worse

AFP



SOCIÉTÉ GÉNÉRALE has been the object of much scrutiny and some mockery since news broke in January that Jérôme Kerviel, a lowly trader in an unexciting market, had lost his employer €4.9 billion ($7.2 billion). The French bank has taken its lumps since then—its shares are down by 28% since the start of the year and shareholders gave executives a rough ride at the annual general meeting on May 27th—but it could have been worse. In many ways SocGen has been lucky.

To be fair, the bank has earned some of that good fortune. It was quick to raise new capital, asking shareholders for €5.5 billion in February. It has replaced its chief executive: Frédéric Oudea (pictured) took over from Daniel Bouton, who remains SocGen's chairman, in May. And it has set out to tighten controls with a set of reforms that will cost more than €100m. By the time those changes have taken effect, says Mr Oudea, SocGen will lead the pack in terms of its risk oversight.

There is a lot to fix. A juicily detailed internal report, published on May 23rd, identified more than 1,000 fictitious transactions used by Mr Kerviel to offset actual bets he was making on European futures indices. Direct supervision was either weak or, for a period in 2007, entirely lacking. Alarm-bells that should have rung, such as Mr Kerviel's reluctance to take any holidays, remained silent. Those that did ring failed to trigger a response. The bank now suspects that Mr Kerviel was being helped by a trading assistant who entered some of the made-up trades.

Just how big a governance snafu the Kerviel saga represents is a matter for debate. Mr Oudea rejects the idea of a systemic failure, arguing that the loss was a product of a particular time and place: a period of rapid growth in equity derivatives, which overstretched the bank's capacity to monitor itself, and a peripheral trading desk where people were less jumpy about the risk of fraud.

Clients seem willing to give SocGen the benefit of the doubt. Revenue at the equities division of the investment bank tumbled by half in the first quarter, compared with the same period in 2007, but much of the fall can be put down to reduced levels of proprietary trading as the bank pegged back its trading limits. “The client-driven franchise is where one would expect to see the wound from Kerviel, but it seems to be holding up,” says Guillaume Tiberghien, an analyst at Credit Suisse.

It helps, of course, that other banks are also suffering, which is where SocGen's luck comes in. Risk appetite is down across the board; levels of introspection about risk management are up. Delays in confirming and settling derivative trades, a blind spot exploited by Mr Kerviel, are seen as an industry-wide problem. Not only do clients lack appealing alternatives, but so do employees. With Calyon, the investment-banking arm of Crédit Agricole, shrinking, equity derivatives traders in Paris have fewer suitors than they otherwise might.

That burst of capital-raising looks prescient too: SocGen's Tier 1 ratio of 8% is in line with the new benchmark emerging at European banks. And the chances of a takeover battle are slim when rivals are also nursing wounds, leaving Mr Oudea free to plot a course back to health. The new boss says that risk appetite at the investment bank will be dialled back up again in due course, and that more capital will flow to other businesses such as retail banking in emerging markets, consumer credit and private banking. He will doubtless face many more questions about Mr Kerviel; but this crop could have been much harsher.

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Disclosure in China

Stepping backwards

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Worries about transparency undermine markets in China and Hong Kong

ESTABLISHING credibility has been a hard slog for China's equity markets. All three, Shanghai, Shenzhen, and Hong Kong, are to varying degrees known for government intervention and a clubby opacity. As the profitability and scale of Chinese companies have grown and their shares have rocketed, plenty of effort has gone into making the markets work more efficiently. But there is an awfully long way to go, and Hong Kong and the mainland show worrying signs of backsliding.

AP

Webb in reflective mood

In Shenzhen plans are afoot to create a new exchange for smaller companies with briefer operating histories. The model is America's NASDAQ, a market that has had tremendous success funding innovative start-ups from around the world, including start-ups based in China.

Good luck. NASDAQ's success rests on an approach that is antithetical to China's. Capital-hungry companies deluge potential investors with information in an effort to create demand for their shares. The government is there to ensure that the information is accurate. However, in China disclosure remains wretched, the result of a censored press, poorly enforced laws and a history of conflating information with propaganda. Regulators tightly control which companies can go public and when shares can be sold, based on perceptions of what is good for the overall market. (For instance, the Chinese government has reportedly stepped in to cap the amount that two state-owned banks can bid for Wing Lung Bank, a listed Hong Kong lender.) Nothing about the new Chinese market will change this state of affairs, except that the companies permitted to list will have even less information to disclose than those on the existing small-company bourse already operating in Shenzhen.

Hong Kong's stock exchange has thrived in recent years on the premise that it is a well governed alternative to Shenzhen and Shanghai. But even here disturbing signs have emerged. May 15th saw the resignation of David Webb, a writer and former investment banker known for his independent views as a member of the exchange's board of directors. Mr Webb resigned, citing policy decisions made “through the back door” by government officials and the exchange's unwillingness to provide critical information.

Mr Webb's criticisms about all manner of abuses inflicted upon investors, from layers of transaction fees to ignored proxy votes, made him something of a hero to Hong Kong's numerous punters. He also gained a huge, if less voluble, fan base within big global financial institutions.

In the fracas after his departure, it emerged that the exchange and Hong Kong's government were having quiet discussions about creating a new set of listings, known as a “professional board”, with fewer disclosure requirements. The Hong Kong exchange already demands less frequent disclosure than other big Asian markets. Even so, more opacity is thought to appeal to the tycoons in charge of Hong Kong's sprawling business empires, because they would like a way to transfer profits between operations without having to reveal the details to minority shareholders.

Going up against the establishment in Hong Kong is not easy. In April Mr Webb backed another candidate with heavyweight financial credentials for a seat on the exchange's board but the government put its voting muscle behind a candidate who had only recently headed the audit committee of a firm that collapsed. The hope is that China's mainland bourses are dragged up to the level of Hong Kong; the fear, that all slither down.

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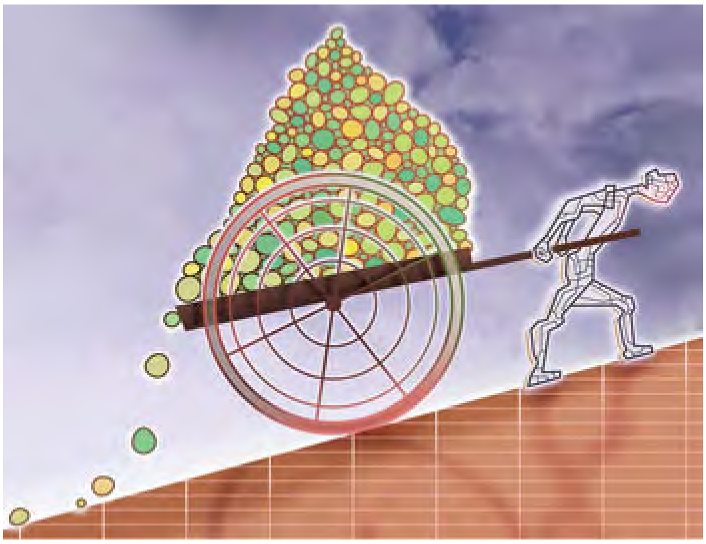
Economics focus

The Doha dilemma

May 29th 2008
From The Economist print edition

Does freer farm trade help poor people?

Illustration by Jac Depczyk



THE global food crisis has shone a harsh spotlight on the consequences of government meddling in agriculture. Poor people go hungry, in part, because Americans pay their farmers to divert crops from food to fuel. But in at least two areas, the crisis has emboldened those who are sceptical of free markets in food.

The first is “food security”. Politicians in rich and poor countries have seized on recent price spikes as proof that free farm trade is a risky business and self-sufficiency a worthy goal. The second area concerns the poor. For years reformers have advocated freer trade on the grounds that market distortions, particularly the rich world's subsidies, depress prices and hurt rural areas in poor countries, where three-quarters of the world's indigent live. The Doha round of trade talks is dubbed the “development round” in large part because of its focus on farms. But now high food prices are being blamed for hurting the poor (the topic of a big United Nations summit in Rome starting on June 3rd).

The argument for self-sufficiency is easiest to counter. Anyone who believes autarky is the route to food security should look at starving North Korea. In world markets trade barriers, not the lack of them, have exacerbated the mess. The commodities that have seen the biggest price spikes are those which tend to be traded least. Only 6% of global rice production, for instance, flows across borders. Unilateral export restrictions, such as those imposed by Vietnam and India, have made matters worse. Global supply is disrupted and domestic farmers discouraged from producing more. The route to deeper, less volatile markets lies through freer trade and fewer distortions. The notion that free trade precludes food security is plainly wrong-headed.

The links between trade, food prices and poverty reduction are more subtle. Different types of reform have diverse effects on prices. When countries cut their tariffs on farm goods, their consumers pay lower prices. In contrast, when farm subsidies are slashed, world food prices rise. The lavishness of farm subsidies means that the net effect of fully freeing trade would be to raise prices, by an average of 5.5% for primary farm products and 1.3% for processed goods, according to the World Bank.

These effects are still much smaller than recent food-price spikes, but would they, on balance, help or hurt the poor? In crude terms, food-exporting countries gain in the short term whereas net importers lose. Farmers are better off; those who buy their food fare worse. Although most of the world's poor live in rural areas, they are not, by and large, net food sellers. A forthcoming study* of nine poor countries by M. Ataman Aksoy and Aylin Isik-Dikmelik, two economists at the World Bank, shows that even in very rural countries, such as Bangladesh and Zambia, only one-fifth of households sell more food than they buy. That suggests the losers may outnumber winners.

But things are not so simple. The authors point out that net food buyers tend to be richer than net sellers, so high food prices, on average, transfer income from richer to poorer households. And prices are not the only route through which poverty is affected. Higher farm income boosts demand for rural labour, increasing wages for landless peasants and others who buy rather than grow their food. Several studies show this income effect can outweigh the initial price effect. Finally, the farm sector itself can grow. Decades of underinvestment in agriculture have left many poor countries reliant on imports: over time that can change.

The World Bank has often argued that the balance of all these factors is likely to be positive. Although freer farm trade—and higher prices—may raise poverty rates in some countries, it will reduce them in more. One much-cited piece of evidence is a study† by Thomas Hertel, Roman Keeney, Maros Ivanic and Alan Winters. This analysis simulated the effect of getting rid of all subsidies and barriers on global prices and trade volumes. It then mapped these results on to detailed household statistics in 15 countries, which between them covered 1 billion people. Fully free trade in farm goods would reduce poverty in 13 countries while raising it in two.

A question of numbers

But lately the bank seems to be taking a different line. Robert Zoellick, the bank's president, claims that the food-price crisis will throw 100m people below the poverty line, undoing seven years of progress. His figure comes from extrapolating the results of a different study** by Mr Ivanic and Will Martin, another World Bank economist. This study analyses the effects of more expensive staple foods on poverty by examining household surveys in nine countries. In seven cases, higher food prices meant more poverty. (Dani Rodrik, a blogging Harvard economist, was one of the first to highlight the tension between these studies.)

In fact, the bank's results are not as contradictory as they seem. The two studies are based on different sets of countries: only Peru, Zambia and Vietnam appear in both. And the gloomy analysis measures only the effect of pricier staple foods, whereas the other examines freer trade in all farm goods. Such trade brings broader benefits: even if higher prices for staples exacerbate poverty in some countries, at least in the short term, the effect may be outweighed by increased demand for other farm exports, such as processed goods, as rich countries cut tariffs.

These subtleties suggest two conclusions. First, the bank, and others, should beware sweeping generalisations about the impact of food prices on the poor. Second, the nature of trade reform matters. Removing rich-country subsidies on staple goods, the focus of much debate in the Doha round, may be less useful in the fight against poverty than cutting tariffs would be. The food-price crisis has not hurt the case for freer farm trade. But it has shown how important it is to get it right.

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*"Are Low Food Prices Pro-Poor? Net Food Buyers and Sellers in Low Income Countries" by M. Ataman Aksoy and Aylin Isik-Dikmelik. World Bank (forthcoming)

†"Distributional Effects of WTO agricultural reforms in rich and poor countries" by Thomas Hertel, Roman Keeney, Maros Ivanic and Alan Winters. *Economic Policy*, April 2007

**"Implications of Higher Global Food Prices for Poverty in Low-Income Countries" by Maros Ivanic and Will Martin. World Bank Policy Research Working Paper No 4594, April 2008

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Exploring Mars

The Phoenix has landed

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Phoenix has arrived on Mars, in search of places where life might exist. But an analysis of the planet's rocks suggests that there is probably none to look for

THE past few days have brought good news and bad for those who hope to find Martians of some description or other. The good news is that on May 25th *Phoenix*, America's latest mission to Mars, landed successfully where many others have failed. The bad is that an analysis of the results of previous successful missions suggests it is unlikely that life ever got going there in the first place, let alone survived the transition to the harsh Martian conditions prevailing today. The balmy, watery past conjured up in the minds of the eternal optimists who inhabit the exobiology departments of the Earth's universities has been replaced by something more akin to a planet-sized version of the Dead Sea.

To start with the positive, though, *Phoenix*'s landing seems to have been picture-perfect. Literally. The photograph above, which was taken from a spacecraft called *Mars Reconnaissance Orbiter* during *Phoenix*'s descent, shows how it first deployed a parachute to slow itself. It then, in classic sci-fi fashion, fired retro-rockets to make a controlled touch-down on three spindly legs, rather than swaddling itself wimpishly in balloons and bouncing around for a bit before settling, as some previous missions have done.

More pleasingly still, the first images it sent back could have come out of a geography textbook's chapter on arctic terrain. They show a surface broken into polygonal slabs by repeated freezing and thawing of the sort that happens above permafrost. For, unlike any previous successful mission to Mars, *Phoenix* has landed not in the planet's tropics but near one of its poles. And the reason for going there is the same as the reason for the polygonal slabs. It is that the Martian poles are repositories of ice, and the hunt for water on Mars has now become almost obsessive.

Ere the winter storms begin

Phoenix got its name from its precarious beginnings. In 1999 NASA, America's space agency, suffered two failed Mars missions on the trot. One, *Mars Climate Orbiter*, had a particularly humiliating crash, because the fault lay with a group of engineers who, in defiance of common sense, had continued to use imperial units of measurement in their calculations when all around had adopted the metric system. The crash of the other, *Mars Polar Lander* (intended to touch down near the south Martian pole), was not caused by that sort of carelessness; landing things on Mars is inherently hard and mission failures are inevitable. Nevertheless, rather than risk a third consecutive loss, NASA put things on hold. One result was that an unlaunched craft similar to *Mars Polar Lander* was tucked away in a clean room while the agency had a rethink.

The outcome of that rethink was a bid by the University of Arizona to take the mothballed lander, refit it and have another go at visiting a Martian pole (this time the northern one). The idea of naming the craft after a mythological bird that self-immolates and then rises anew from its own ashes was thus irresistible. It was also poignant, because *Phoenix*'s active life is expected to be a mere three months. It will be killed beyond reasonable hope of resurrection not by heat but by the encroaching cold of winter.

Watching that winter arrive will be spectacular. Vastitas Borealis, the area that *Phoenix* has landed in, will be covered in a metre-deep layer of frozen carbon dioxide. *Phoenix*'s main camera will have an impressive view of this happening. The instrument everyone is really concentrating on, however, is not the camera but the digging arm. Measurements from orbit suggest that the Martian permafrost is within half a metre of the surface. If that is correct, the arm, which is fitted with a scoop and a second camera, should be able to dig into the permafrost, photograph its details and bring samples back into the main body of the probe for analysis.

The hope—the one that propels all missions to Mars—is to find a set of conditions that would allow living creatures to survive. Since cold-tolerant microbes do just that in terrestrial permafrost, it is quite possible that appropriate conditions will, indeed, be found. That does not, of course, mean that anything will be living in them. Nor is *Phoenix* equipped to detect micro-organisms, though it will be able to sniff out organic molecules if these are around, and that will be a tantalising clue. It will also examine the general chemistry of the sub-surface layers, to see if it is within the limits tolerable by living things on Earth.

The shore of a poison sea

The importance of those limits is emphasised by the second piece of news, a paper analysing Mars's rocks that was published a few days after *Phoenix* landed. The message seen written in those rocks when they were first examined was of abundant water. Lots of them are layered in ways that indicate they formed at the bottoms of lakes or seas. However, Nicholas Tosca of Harvard University and his colleagues have been looking more closely and, as they report in *Science*, the second glance is not as promising as the first.

Mars's geology (if that is not an oxymoron) has been studied spectroscopically by several satellites, and has also been prodded and probed at a local level by ground-based rovers. The upshot is that the layered rocks do, indeed, seem to have formed underwater. They appear to be sandstones, but with a lot of minerals such as magnesium, calcium and iron sulphates that form when brine evaporates. It is these minerals that concern Dr Tosca.

His calculations suggest that the waters they formed from would have been highly acidic. That is bad enough for those who imagine them brim-full of bacteria. But they would also have been highly osmotic. The dissolved chemicals within them would have served to lock up the water so that it could not take part in biochemical reactions.

The degree to which water is locked up by such solutes is measured by a number called the “water activity” of a solution. Pure water has an activity of 1.0. Seawater's activity is 0.98. The water of primeval Mars, Dr Tosca calculates, was probably between 0.78 and 0.86, and may sometimes have been as low as 0.5. That is far lower than is tolerable by any living thing known on Earth, even from places like the Dead Sea.

This result will probably not dampen the ardour of exobiologists. Living organisms, they will argue, are amazingly adaptable, so why should they not be born in conditions even more extreme than those found on Earth? Like a phoenix, perhaps. But then the phoenix is mythological.

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Education and sex

Vital statistics

May 29th 2008
From The Economist print edition

Girls are becoming as good as boys at mathematics, and are still better at reading

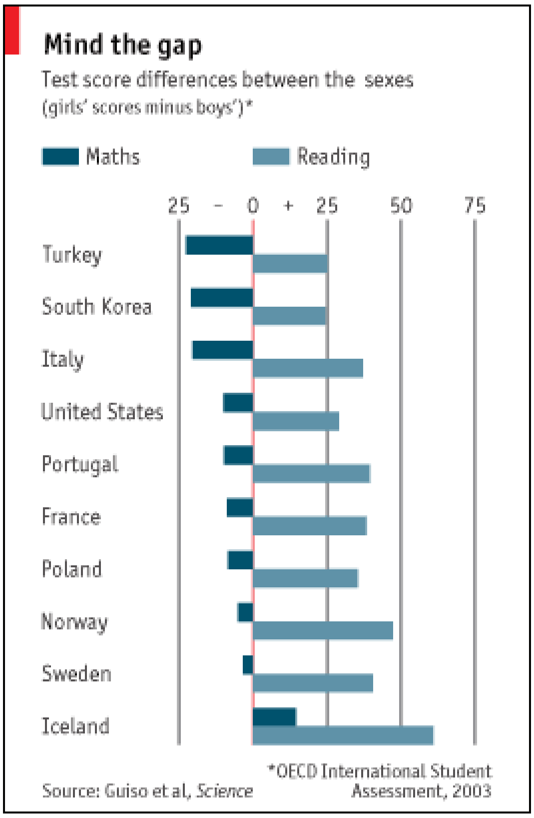
TRADITION has it that boys are good at counting and girls are good at reading. So much so that Mattel once produced a talking Barbie doll whose stock of phrases included “Math class is tough!”

Although much is made of differences between the brains of adult males and females, the sources of these differences are a matter of controversy. Some people put forward cultural explanations and note, for example, that when girls are taught separately from boys they often do better in subjects such as maths than if classes are mixed. Others claim that the differences are rooted in biology, are there from birth, and exist because girls' and boys' brains have evolved to handle information in different ways.

Luigi Guiso of the European University Institute in Florence and his colleagues have just published the results of a study which suggests that culture explains most of the difference in maths, at least. In this week's *Science*, they show that the gap in mathematics scores between boys and girls virtually disappears in countries with high levels of sexual equality, though the reading gap remains.

Dr Guiso took data from the 2003 OECD Programme for International Student Assessment. Some 276,000 15-year-olds from 40 countries sat the same maths and reading tests. The researchers compared the results, by country, with each other and with a number of different measures of social sexual equality. One measure was the World Economic Forum's gender-gap index, which reflects economic and political opportunities, education and well-being for women. Another was based on an index of cultural attitudes towards women. A third was the rate of female economic activity in a country, and the fourth measure looked at women's political participation.

On average, girls' maths scores were, as expected, lower than those of boys. However, the gap was largest in countries with the least equality between the sexes (by any score), such as Turkey. It vanished in countries such as Norway and Sweden, where the sexes are more or less on a par with one another. The researchers also did some additional statistical checks to ensure the correlation was material, and not generated by another, third variable that is correlated with sexual equality, such as GDP per person. They say their data therefore show that improvements in maths scores are related not to economic development, but directly to improvements in the social position of women.



The one mathematical gap that did not disappear was the differences between girls and boys in geometry. This seems to have no relation to sexual equality, and may allow men to cling on to their famed claim to be better at navigating than women are. However, the gap in reading scores not only remained, but got bigger as the sexes became more equal. Average reading scores were higher for girls than for boys in all countries. But in more equal societies, not only were the girls as good at maths as the boys, their advantage in reading had increased.

This suggests an interesting paradox. At first sight, girls' rise to mathematical equality suggests they should be invading maths-heavy professions such as engineering—and that if they are not, the implication might be that prejudice is keeping them out. However, as David Ricardo observed almost 200 years ago, economic optimisation is about comparative advantage. The rise in female reading scores alongside their maths scores suggests that female comparative advantage in this area has not changed.

According to Paola Sapienza, a professor of finance at Northwestern University in Illinois who is one of the paper's authors, that is just what has happened. Other studies of gifted girls, she says, show that even though the girls had the ability, fewer than expected ended up reading maths and sciences at university. Instead, they went on to be become successful in areas such as law.

In other words, girls may acquire an absolute advantage over boys as a result of equal treatment. This is something that society, more broadly, has not yet taken on board. Mattel may wish to take note that among Teen Talk Barbie's 270 phrases concerning shopping, parties and clothes, at least one might usefully have been, “Dostoevsky rocks!”

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Cancer vaccines

Target acquired

May 29th 2008
From The Economist print edition

It may become possible to vaccinate against brain tumours

CERVICAL cancer is caused by a virus. That has been known for some time and it has led to a vaccine that seems to prevent it. Since then, researchers have been looking for other cancers that may be caused by viruses, to see if they too can be prevented. And they seem to have found one—one of the most feared of all. A piece of research expected to be unveiled on June 1st by Duane Mitchell of Duke University in North Carolina, at a meeting of the American Society of Clinical Oncology, hints that glioblastomas, the most lethal form of brain tumour, may also be susceptible to vaccination.

The story began a few years ago when Charles Cobbs of the California Pacific Medical Centre Research Institute in San Francisco found something odd about glioblastomas. He noticed they usually have a form of herpes, called cytomegalovirus, active within them. It is not that catching cytomegalovirus automatically causes a brain tumour—the virus is found, inactive, in about 80% of the population. Nevertheless, there is clearly some connection between virus and tumour, a connection reinforced by Dr Cobbs's discovery that the virus appears to dwell inside the tumour but not in the healthy tissue surrounding it. This led him to speculate that the virus may be creating the tumour as a safe haven to support its own existence.

After learning about Dr Cobbs's work, Dr Mitchell and his colleagues first confirmed the basic findings. They discovered cytomegalovirus in the tumours of more than 90% of those people with glioblastoma whom they examined, but not in healthy brain tissue, nor in non-malignant brain tumours. They then began an experiment on 21 patients who had been diagnosed with glioblastoma.

Their intention was to encourage those patient's immune systems to attack the tumours by training them to recognise the signs of active cytomegalovirus infection. To do that, they drew blood from their patients and exposed the immune-system cells within each sample to bits and pieces of cytomegalovirus, in order to encourage those cells to develop the power to identify the pathogen. The cells were then injected back into the patients they had come from, in the hope that those patients' immune systems would react to cytomegalovirus as if they had encountered it naturally within the body.

The results are encouraging. The normal prognosis for glioblastoma is death within two years, even if a patient is treated with chemotherapy and radiation. Such treatment by itself is reckoned to slow the tumour's growth by between six and eight months. When Dr Mitchell added his crude vaccine to the traditional treatment, this figure rose to more than a year—and in some people the tumours have stopped growing for more than two years, an observation that opens the door to work on a proper vaccine.

Just why active cytomegalovirus is associated with glioblastoma is still unclear. The virus may cause the tumour, as Dr Cobbs suspects, or the tumour may simply provide the virus with a congenial home. From the vaccine-maker's point of view it hardly matters. If a vaccine causes the immune system to destroy infected cells, the cancer will be killed anyway. And that would be very good news indeed.

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Palaeontology

Storking the ancient skies

May 29th 2008
From The Economist print edition

This is an artist's impression of a flying reptile called Quetzalcoatlus eating a small dinosaur. Until recently, Quetzalcoatlus and its relations were thought to have hunted fish from the sea. But a re-analysis of their skeletons, published in the Public Library of Science by Mark Witton (who is also the artist in question) and Darren Naish, both of Portsmouth University, in England, suggests they were more like giant storks. Rather than skimming the sea, they plucked their prey from the ground. At five or six metres high, Quetzalcoatlus could easily have eaten young dinosaurs. Or young humans, had they been around 65m years ago.

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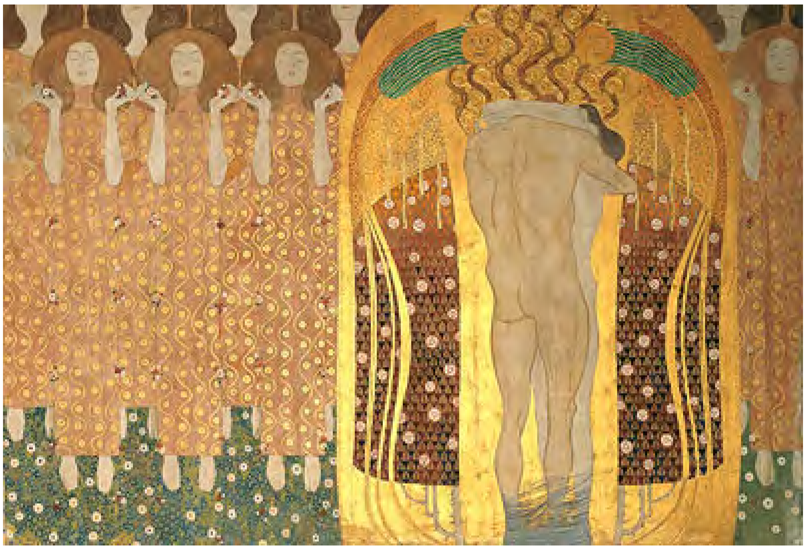
20th-century art

Golden bars of heaven

May 29th 2008
From The Economist print edition

Belvedere, Vienna



The ostentation and eroticism of Gustav Klimt make him as much a painter of this century as he was of his own time, a new exhibition shows

GUSTAV KLIMT was a great portrait painter whose subjects were the prosperous Viennese bourgeoisie at the start of the 20th century. His supporters were mostly young, progressive and Jewish. Together they celebrated the “ennoblement of luxury”. Now Klimt has become the flavour of this decade, not least because his work reflects another period of great prosperity in which ostentation and wealth came back in fashion. For example, a portrait from his golden period of Adele Bloch-Bauer, which is literally decorated with gold leaf and silver, is one of the costliest paintings ever sold. Ronald Lauder, a cosmetics heir and former American ambassador to Austria, is believed to have paid $135m when he bought it for his little Neue Galerie in New York in 2006.

In Britain the Tate Gallery's Liverpool outpost has chosen Klimt for its big show while the city is the 2008 European capital of culture. This is the first, and maybe the last, major Klimt show in Britain. “It's proved much more difficult than we expected it to be,” says Christoph Grunenberg, director of the Liverpool gallery and co-curator of the exhibition. To mount it was a bold decision that caused him sleepless nights. They were worth it.

Klimt was a leader in the revolt against the Vienna art establishment known as the Secession. The idea was to combine painting, design, architecture and music in a *Gesamtkunstwerk* or “total work of art”. The finest example is the “Beethoven Frieze” from the Secession show of 1902. Gustav Mahler provided the musical accompaniment for Klimt's visual representation of Beethoven's ninth symphony. A careful reconstruction of the frieze is a persuasive reason for visiting Liverpool.

It is a monumental piece on three walls, painted on heavy plasterboard, and it tells a simple story of good overcoming evil. A virtuous, gold-plated knight challenges the villainous Typhon, an ape-like figure who is fawned upon by fairly repulsive but beautifully painted women representing sickness, madness and death (Typhon's daughters), and temptations such as lewdness, lust and excess. The style is reminiscent of the *Jugendstil*—or art nouveau—but the decoration comes directly from the Secession itself, for Klimt applies real gilt, coloured glass, curtain rings and mother-of-pearl as well as paint.

The last image is inspired by Friedrich Schiller's “Ode to Joy”, which is also the basis for the last movement of Beethoven's ninth symphony. “The iconography of that climax is complex,” says Mr Grunenberg. Some critics have suggested that the naked figures of a man and woman (pictured above) surrounded by a choir of angels signify the nations of Europe coming together. It actually looks like a more human version of the same thing.

The frieze was to be destroyed at the end of the 1902 exhibition, but it was stored instead, in a shed next to a tram track where it was damaged before its restoration in the 1970s. This version was made in 1984, using Klimt's own techniques and materials. It is a copy, but Mr Grunenberg is unapologetic: “This reproduction is absolutely justifiable because it is of such high quality.” (To see the original requires a journey to Vienna.)

The focus of the show is on Klimt, but the exhibition spreads through galleries designed to illustrate other examples of total works of art. Klimt painted the wives of clients who did up their houses with furniture and decoration made by his friends at the Wiener Werkstätte, who were, in turn, heavily influenced by the British arts and crafts movement. No detail was omitted, down to the lavatory-paper holder and the coal scuttle.

None of the works from Klimt's golden period has travelled to Liverpool, but there are excellent examples of earlier, somewhat less extravagant domestic portraits. The last gallery in the show is titled “The World in Female Form”; it includes his Salome, high-cheeked, black-haired and utterly ruthless, and his Eve, with broad hips, chunky thighs and an expectant smile. In a small room off this gallery are examples of his easy, realistic eroticism. Klimt himself appears in various photographs, wearing a smock and a pointed beard. Although he lived with his mother and two sisters throughout his adult life, when he died there were 14 outstanding paternity suits against him, which might explain his Mephistophelean smile.

“Gustav Klimt: Painting, Design and Modern Life in Vienna 1900” will be at Tate Liverpool from May 30th until August 31st.

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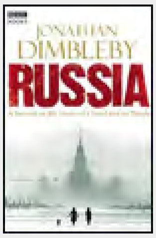
Russia

Horses and vodka

May 29th 2008
From The Economist print edition

SPENDING time in Russia is a bit like taking the psychotropic anti-malarial drug Lariam: anyone with a propensity to anxiety should probably avoid it. Jonathan Dimbleby, an accomplished British broadcaster, was by his frank admission in a state of considerable emotional turmoil when he travelled from the Arctic city of Murmansk to Vladivostok. The overwhelming landscape and the people who were often so rude did not help his mood, but his responses—awe, horror and frustration—were perhaps more acute as a result.

Russia: A Journey to the Heart of a Land and Its People
By Jonathan Dimbleby



BBC Books; 563 pages; £25

Buy it at
Amazon.co.uk

The ugly authoritarianism of Vladimir Putin's Kremlin and Russia's hydrocarbon-fuelled diplomatic bolshiness are now well documented. There are fewer worthwhile accounts of ordinary life across the vast, eccentric Russian continent in the Putin era. Mr Dimbleby's perceptive travelogue is one of them. He describes the spookiness of St Petersburg; the micro-cultures (and pointy shoes) of the Caucasus; the desolation of Beslan; the magic of Tolstoy's country estate; the ludicrously dangerous roads and dreadful hotels. He captures the way Russians are transformed by toasts, the romance of long-distance train rides and the squalor of train stations. He encounters a Karelian witch, a Siberian shaman and wild horses in the Altai mountains. He visits a plush Moscow *banya*. He drinks a lot of vodka.

Along the way he offers lively summaries of some of the key dramas of Russian history, including the exploration of Siberia, the tragic nobility of the Decembrists and the unspeakable siege of Leningrad. He meets the kind of near-saints that only places with so much bad history can produce: suicidally brave journalists in Samara; campaigning environmentalists in the Urals; a heroic AIDS worker in Irkutsk. They vary what might otherwise have become a dismal parade of villainy.

“We steal,” a Caspian sturgeon poacher says, “and we think nothing of stealing because everyone is stealing.” Mr Dimbleby notes the gangsterism of government at all levels, the brazen rackets and the cradle-to-grave corruption that Russians must negotiate to survive. He nicely portrays the fatal combination of savage indifference on the part of the country's rulers and the enraging fatalism of the ruled. He is perpetually baffled by what, to his Western ears, sound like contradictory attitudes: the Russians he meets are sophisticated, acquisitive and yet cynical to the point of hostility towards democracy. “Crypto-fascist” is his label for the system Mr Putin has built.

Mr Dimbleby loves Russian literature, and he hears Tolstoyan and Gogolian echoes as he travels. But he is not a Russia expert (he undertook the journey for a BBC television series), and makes some mistakes and simplifications, over Chechnya and the Yukos affair, for example. That, however, is also his book's main virtue. His novice's eye sees the moral outrage in everyday injustices—the use of malnourished teenaged conscripts as slave labour, say, or the routine persecution of migrant labourers—to which more practised Russia-watchers are too often desensitised. His disgust is mitigated by the fascination that Russia somehow inspires too, even in the most sceptical visitor.

Russia: A Journey to the Heart of a Land and Its People.
By Jonathan Dimbleby.
BBC Books; 563 pages; £25

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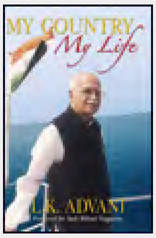
Indian politics

Angry old man

May 29th 2008
From The Economist print edition

My Country My Life
By L.K. Advani

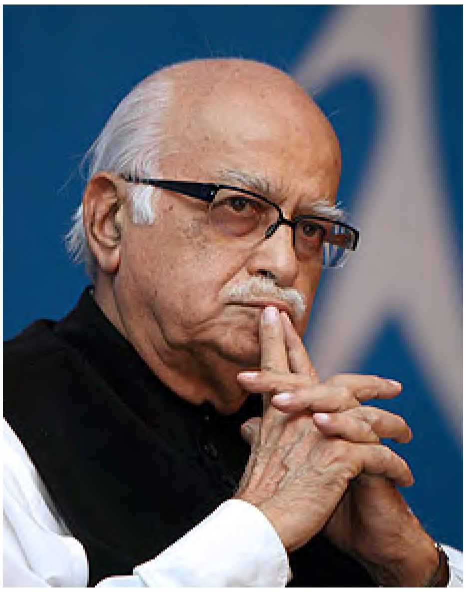


Rupa & Co, Delhi; 1084 pages; $30

Buy it at
Amazon.com

IN THE Indian general election in 1984, a Hindu nationalist group called the Bharatiya Janata Party (BJP) won two seats. In 1996, led by Atal Bihari Vajpayee, it won 161 seats and briefly formed the government. A revered orator, Mr Vajpayee was one of the main architects of this dizzying rise. The other, who will lead the party into an election due by next year, is one of India's most divisive figures: L.K. Advani.

AFP



Musing on power

A hale octogenarian, Mr Advani's political career spans India's independent history. But he is best known for his part in the calamity that helped fuel the BJP's rise: the destruction of the Babri mosque in Ayodhya by Hindu fanatics in 1992. This outrage—which sparked communal massacres in which some 2,000 people died, most of them Muslims—was instigated, at least in part, by a BJP campaign for a Hindu temple to be built on the site of the mosque. The campaign was spearheaded by Mr Advani, who led a *ram rath yatra*, or chariot procession, halfway across India to rally support for the temple. Mr Advani calls this the “most decisive, transformational event” of his career.

Mr Advani has some impressive qualities. He is enraged by the corruption and cronyism that has rotted Congress, India's other national party. But he is astute enough to confess that the BJP's own standards of probity have lapsed. He is justified in boasting of his party's economic policies while running coalition governments from 1998 to 2004. Indeed, the BJP can arguably claim more credit for India's recent 9% growth rate than the current Congress-led coalition government. Mr Advani also offers a candid, if not original, analysis of why these policies nonetheless failed to satisfy the poor Indians who voted the party out in 2004.

To fans of tolerance, however, Mr Advani's views and the prospect of the BJP returning to power are disturbing. Mr Advani says he has no aversion to other faiths: “Some of my best personal friends are indeed Christians.” Yet he believes that India is a Hindu country, defined by a superior Hindu culture which all patriotic Indians must embrace. The BJP government was notorious for rewriting school textbooks to propagate its mythical belief that civilisation began in India.

For those who worry about Mr Advani's role in spreading this message, his book may be doubly alarming. This is a thunderous history of Indian politics, which glories in his triumphs, as he sees them, and offers venomous appraisals of his many foes. A photograph of Mr Advani cuddling a pet white rabbit—captioned “A tender moment”—is a rare, and slightly unsettling, effort to portray the old tub-thumper in a less pugnacious mode.

Another vignette is more interesting. In 2005 Mr Advani and his family were invited on a tour of Pakistan, ending in Karachi, the city of Mr Advani's birth, which he was forced to flee after British India's bloody division, and which he loves more than any other. Deeply moved by an experience that included ample Pakistani hospitality, Mr Advani made some surprisingly generous remarks about Pakistan's founder, Muhammad Ali Jinnah—whom hardline Hindus especially hate.

In the furore that followed, he was forced to quit as the BJP's leader. Mr Advani describes this as “the most agonising moment in my political life”. But what explains his kind words about Jinnah? One possibility, this book suggests, is a refugee's longing for home.

My Country My Life.
By L.K. Advani.
Rupa & Co, Delhi; 1,084 pages; $30

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French films

On-screen confidence

May 29th 2008 | PARIS
From The Economist print edition

New spring for French cinema

THE French film industry is more often given to introspective agonising about American cultural imperialism or the tyranny of the market than to self-congratulation. But this year, unapologetic triumph is in the air. It is not just that for the first time in 21 years the Cannes film festival jury, headed this time by Sean Penn, awarded its top prize, the Palme d'Or, to a French film, Laurent Cantet's “Entre les Murs” (“The Class”). Another homegrown movie, “Bienvenue Chez les Ch'tis” (which will be remade for an American audience as “Welcome to the Sticks”), is set to overtake James Cameron's Hollywood blockbuster, “Titanic”, as the country's all-time top box-office hit.

Apart from their tiny budgets, these two films could scarcely differ more. The first is a gritty documentary-style classroom drama, filmed—like Nicolas Philibert's charming 2002 film, “Etre et Avoir” (“To Be and To Have”)—with real pupils in a real school, this one in a multicultural quarter of Paris. It is adapted from a book by François Bégaudeau, based on his experience as a teacher (he plays a fictionalised version of himself in the film). The second is a slick, warm, redemptive comedy, written by and starring Dany Boon, a French comic, which overturns French prejudices about the beer-drinking, rain-soaked north. Since its release in February, “Bienvenue Chez les Ch'tis” has notched up a staggering 20m cinema tickets in France—just short of the 20.7m that “Titanic” secured—and over €100m ($157.6m) in receipts.

Partly thanks to this hit, French films grabbed a 63% share of all domestic ticket sales in the first four months of 2008, next to 30% for Hollywood's output. In comedy and multicultural drama, the French seem to have found two new formulae to beat the traditional low-plot, high-art movie, a genre typically shot in close-up in elegant apartments and late-night cafés. There are two other French comedies in the box-office top five so far this year. And this year's César, the French version of an Oscar, for best film went to the 2007 offering, “La Graine et le Mulet” (“Couscous”), which was directed by Abdellatif Kechiche, aTunisian-born Frenchman. An inter-generational family drama, it follows the efforts of an Arab immigrant in the southern French port of Sète to open a fish-and-couscous restaurant.

Apart from landmark movies such as Mathieu Kassovitz's “La Haine” (“Hate”), which was made in 1995, France's film-makers, like its novelists, have been curiously slow to draw on the rich dramatic tension of *banlieue* life. Mr Kechiche broke ground in 2003 with his touching *banlieue* movie, “L'Esquive” (“Games of Love and Chance”). But few others have managed to find an authentic voice that conveys both the grainy energy and harsh banality of life in the suburbs.

Some wonder how far the new trend is politically motivated. Cannes juries like to use awards to make statements; Michael Moore's “Fahrenheit 9/11” won the 2004 Palme d'Or as well as a standing ovation in Cannes. This week President Nicolas Sarkozy, battling with education reform, congratulated the team behind “Entre les Murs” for depicting “the efforts, the hopes and the successes of teachers”, given the difficulties in such schools. As the pupils-turned-stars returned from the red carpet to their school in Paris, flush with their Cannes victory, there was much hope that it would inspire their fellow schoolmates. Indeed, the film itself got a small state subsidy under the culture ministry's “Images of Diversity” programme. Set up in the wake of rioting in 2005 in the heavily immigrant *banlieues*, this is designed to promote a fresh image of France on the big screen.

Whether all such films will prosper commercially remains to be seen. “Entre les Murs” goes on release in France only in October. Despite its prize, “La Graine et le Mulet” was not a box-office hit in France. In an industry that churns out nearly 200 films every year, most of which disappear without trace, however, that may not be the point.

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A modern Western

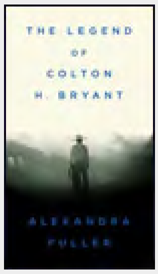
Horses and oil

May 29th 2008
From The Economist print edition

Corbis

Tears in Marlboro country

The Legend of
Colton H. Bryant
By Alexandra Fuller



Penguin; 202 pages; $23.95.
Simon & Schuster; £12.99

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ALEXANDRA FULLER, who made her name with her 2001 family memoir, “Don't Let's Go to the Dogs Tonight”, was born in England and grew up in Africa. Her latest book—set in her new home, the high plains of Wyoming—hangs so faultlessly on its high-altitude, big-sky, oil-drilling bones that it seems not so much to have been written as uncovered by the wind and weather of the American north-west.

Colton Bryant is a cowboy with a heart. At eight, he pedals his bicycle so fast his legs “look like egg-beaters”. He begs his teacher to talk twice as quickly so that class will be over in half the time. Even on Ritalin, Colton does not seem to have “the gear between flat out and stopped”. His classmates call him “retard”, to which he answers over and over: “Mind over matter. I don't mind so it don't matter.”

At 14, Colton's older brother, Preston, takes him out hunting. He pukes at his first kill. “It takes everyone a little differently,” Preston tells him gently. He falls in love with a mustang called Cocoa, who tries as hard as she can to buck him off before she runs away only to be mysteriously rediscovered later on.

Like his father and his grandfather before him, Colton Bryant has oil as well as horses in his blood. So it is only a matter of time before he leaves for the rigs, working for companies that keep their workers on their books as part-time labourers. It makes it easier to fire them the moment they get too old or too slow, or if they slip.

One night, not long before his 26th birthday, Colton slipped and fell from a rig at an Ultra Petroleum well site. There were no rails and he was wearing no harness. No compensation was paid, either. As the locals like to say, “Cowboy up, cupcake, everyone has their freakin' problems.”

Grown men wept at his funeral, and his family put a toy horse and a toy elk in his coffin. Like all Westerns, this story is a tragedy before it even starts because there is no way a man like Colton can win against all the odds out there. Wyoming may be one of those places where the good die young. But in bringing Colton Bryant back to life on the page, Ms Fuller has had her own revenge.

The Legend of Colton H. Bryant.
By Alexandra Fuller.
Penguin; 202 pages; $23.95.
Simon & Schuster; £12.99

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Economist.com BOOKS & ARTS

Later retirement

Making it happen

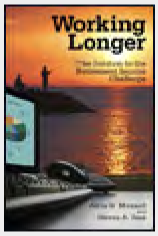
May 29th 2008
From The Economist print edition

LIVE longer, work longer: the cure for population ageing is self-evident, if unpalatable. What is far from obvious is whether such a future will emerge under current arrangements and, if not, how the remedy can be achieved. The merit of "Working Longer", which focuses on America, is that it grasps this thorny issue. The book provides both a concise summary of a wealth of evidence about retirement decisions and a handy guide for middle-aged Americans on how to stay well-off when they hang up their shoes.

The authors, who work at the Centre for Retirement Research at Boston College, set out a dismal prospect for future retirees if they try to rely only on pensions and savings. Social Security, America's public-pensions system, is becoming less generous and employers have drastically scaled back final-salary pension plans and post-retirement health benefits. Although saving through defined-contribution 401(k) plans has grown, it will not provide enough to make up the difference.

Ensuring a prosperous retirement is often represented as a financial task, but the authors believe it should be seen rather as an employment challenge. If Americans were to work longer, they could set a financial goal that is attainable rather than forbiddingly distant. Raising the average retirement age by three years, from 63 to 66, would do the trick.

Working Longer: The Solution to the Retirement Income Challenge
By Alicia H. Munnell and Steven A. Sass



Brookings Institution Press; 207 pages; $29.95 and £17.99

Buy it at
Amazon.com
Amazon.co.uk

On current trends, however, this is unlikely to happen. For most of the 20th century, American men retired earlier and earlier. Although the retreat from work ended in the mid-1980s, the subsequent recovery from the mid-1990s has been sluggish. Young women poured into the labour force over the post-war period. As they have grown older, this has pushed up employment rates for those aged 55-64. But the momentum will not be strong enough to raise women's retirement age to the extent that is necessary.

The obstacle is not one of poor health. Older workers (aged 55-64) started getting healthier in the 1980s, and retirees followed suit in the 1990s. Although 15-20% of older Americans will be unable to carry on working, the rest will be fit enough, especially as far fewer jobs now entail strenuous manual toil.

The blockage lies in the labour market, for two main reasons. First, the temptation to retire once Social Security benefits can be claimed, at the age of 62, seems irresistible for the majority of workers, even though the payments are actuarially reduced. Second, employers are reluctant to retain or hire older people, mainly because they find it hard to lower their wages if their productivity slips. The authors doubt that companies will look on older folk more favourably as younger workers become scarcer, not least since many companies can tap into global labour sources.

If Americans are to retire later, they will need some chivvying. The minimum age when Social Security offers benefits must rise. A change in employers' attitudes would help too. But much will depend on individuals' own efforts. Middle-aged Americans can improve their chances of staying employed by updating skills so that they remain productive. Working longer may be the answer, but hard work is needed to make it happen.

Working Longer: The Solution to the Retirement Income Challenge.
By Alicia H. Munnell and Steven A. Sass.
Brookings Institution Press; 207 pages; $29.95 and £17.99

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James Bond

Centennial

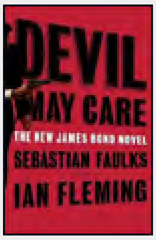
May 29th 2008
From The Economist print edition

JAMES BOND may not have been in it for the money, but Ian Fleming certainly was. In March 1964 Bond's creator was raking it in so successfully he decided to follow the advice of his good friend and fellow golfer, Sir Jock Campbell, and sell a 51% share of the copyright in his books for £100,000. Fleming was not to know that within five months he would be dead. The logic at the time was that it would be cheaper to pay capital-gains tax on a one-off sale than to continue paying Harold Wilson's astronomic income tax.

The Guardian

Faulks, shaken and curled

Devil May Care
By Sebastian Faulks



Doubleday; 304 pages; $24.95.
Penguin; £18.99

Buy it at
Amazon.com
Amazon.co.uk

The purchaser was Booker Brothers, a company chaired by Campbell, which had interests in sugar plantations in Africa and the West Indies. Booker went on also to buy out the copyrights of both Agatha Christie and Georgette Heyer. In a short time its books division became so profitable it decided to plough some of its profits into a literary prize that would give British, Irish and Commonwealth writers something of the kudos and financial reward of the Prix Goncourt in France. Its name was the Booker prize.

Fleming died of heart failure at the age of 56. But his heirs have worked hard to keep his spirit—and his business—alive. In 2000 they bought back the copyright to his work, and are about to appoint a single literary agent in London to oversee the whole Fleming estate. They have their job cut out. The rights to the James Bond films (the real moneymakers) do not belong to them, so they have to make their money where they can, mostly out of books.

Over the years the Fleming clan has authorised a series for children about Bond as a boy ("Before the name became a legend. Before the boy became the man") and another about Miss Moneypenny. Licences have also been sparingly given to other authors to carry on the main Bond line, including one to Kingsley Amis.

This is the year to really cash in, though, which explains why, suddenly, Bond is everywhere: in an excellent exhibition at the Imperial War Museum, on postage stamps and at charity golf days. On May 28th, the centenary of Fleming's birth, a new Bond book was published, by Sebastian Faulks, a British novelist.

Mr Faulks has never written a thriller, but he has a talent for superior pastiche. The first line describes a wet evening in Paris, tipping its cap at Mr Faulks's most famous novels, "Birdsong" and "Charlotte Gray", which are set largely in France. Mr Faulks's Bond is older, sadder, wiser. When the book opens he is teetotal and does deep breathing. That moment passes.

"Devil May Care" is set in 1967, the year after Fleming's last Bond novel. There are cigarettes, quantities of liquor, a brace of pretty twins and a barrel-load of prejudices: "Work had never previously taken him to the Middle East, and for this he was thankful. He regarded the lands between Cyprus and India as the thieving centre of the world." Bond is also constantly changing his clothes. He has tropical suits, tennis whites, Sea-Island cotton shirts and knitted ties, and he travels with what are called "bathing trousers", though that may be because at this stage he is in Iran.

The book races along. Unlike many modern novels, it gets better and better. It reads most of all like the book-of-the-movie. Ironically, none of the non-Fleming James Bond books has ever been filmed. Perhaps this one will be.

Devil May Care.
By Sebastian Faulks.
Doubleday; 304 pages; $24.95.
Penguin; £18.99

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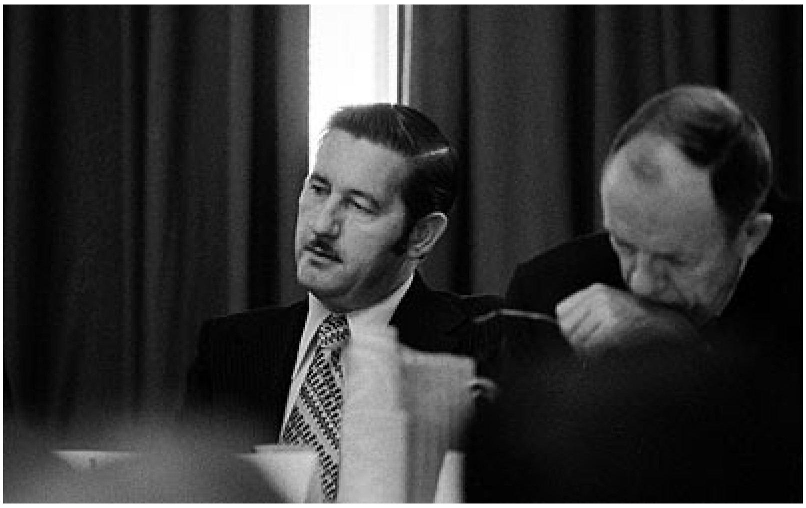
OBITUARY

Robert Vesco

May 29th 2008
From The Economist print edition

Eyevine



Robert Vesco, fraudster, apparently died in November 2007, aged 71

HOW much Robert Vesco stole no one knew for certain. America's Securities and Exchange Commission (SEC) was after him for more than $224m, or more than $1 billion in today's money, which was then the biggest financial fraud in history. But oddly, once the crack teams of lawyers and accountants were on the case, they recovered almost twice as much. And they were still nowhere near the bottom of the schemes that brewed in Mr Vesco's head, behind the pencil moustache, the slicked-back hair and the dark glasses, the very essence of a Hollywood fraudster.

Money being such liquid, transient stuff, it is hardly surprising that financiers should be fugitive. But Mr Vesco capped them all. He was on the run for 35 years, sometimes in a million-dollar yacht eluding the FBI in the blue seas between the Bahamas and Antigua, sometimes in his own Boeing 707, the *Silver Phyllis*, steaming with a variety of nymphs in the on-board sauna or gyrating in the on-board discotheque. He became Tom Adams, a Canadian with four bodyguards and several addresses, and sported a dyed beard. Meetings with Arthur Herzog, his biographer, were held in the dark; once, Mr Vesco kept his back to him. For years only blurred telephoto shots gave proof he was alive. And those were dubious. To some, Mr Vesco's ultimate scam was to suggest that the emaciated man snapped last November in a coffin, with his friends grieving round it, had something to do with him.

A few of the stories about him may have been true. He was said to have poured $60m into the economy of Costa Rica, to which he fled in 1973, propping up single-handedly its ranching, industrial and oil sectors and being kicked out, in 1978, because he wanted to set up a machinegun factory. He was said to have offered Billy Carter, the president's brother, $10m in 1977 to persuade the Carter administration to sell C130 aircraft to Libya (which Mr Vesco could smuggle in on good terms, together with cocaine and Howitzers). Fidel Castro allegedly received a hefty bribe for sheltering him in Cuba after 1982, where he travelled in a convoy of Mercedes from his yachting berth to the golf club.

As long as he had money Mr Vesco was welcome all round the Caribbean, and extradition treaties with America were hastily rewritten to keep him and his dollars in place. But the charges were piling up and the money, after a while, ran out. In 1996 the Cubans sent him to jail for peddling to investors a spurious wonder-drug, Trixolane, as a cure for cancer and AIDS. The conman's patter could run out, too.

Crime, however, was not his whole career. Playing the 1960s markets like a violin was no offence. A clutch of failing machine shops in New Jersey were combined with a Florida public company called Cryogenics to form the dodgy-sounding International Controls Corporation (ICC) and take him public, in 1965, without an SEC filing; by the age of 30, Mr Vesco was a paper millionaire. He perfected the art of the hostile takeover when it was still new, spotting weak companies a mile off and gobbling up shares almost before the victim was aware of it. His buying strategy, sketched out in Magic Marker on flipcharts, was to borrow hugely in order to repay in dollars devalued by inflation, and his sweetest hunting ground became the then unregulated universe of offshore mutual funds.

A well-stuffed briefcase

The quarter-of-a-million dollars he siphoned away at one swoop had originally been invested by thousands of small depositors in Investors Overseas Services (IOS), owned by the arch-scammer Bernie Cornfeld. Mr Vesco, on his hostile takeover of IOS in 1971, immediately began to shift its assets into entities under his control. He meant to set up an independent company somewhere in the Azores, or Morocco, or off Haiti, and do lots of deals with the money; and he wanted to call it RPL, for “Rape, Plunder and Loot”. This may have drawn the SEC's attention.

Under all the oversell, an inferiority complex drove him. His background was poor, Sicilian-American in Detroit, his father a car-worker. He dropped out of school, and fiddled round with bricklaying and gaming parlours before starting to buy companies. On Wall Street his small but ravenous ICC cut no ice with the Lehmans and the Loebs; his rudeness and his loud jackets did not match the mahogany, and he was not invited back.

His chips-on-shoulders and paranoias made him more a potential soulmate of Richard Nixon, and when the SEC charges began to bite in 1972 a cash contribution of $200,000, stuffed in a briefcase, was handed over to the Committee to Re-Elect the President. It didn't work. Nor could Mr Vesco persuade John Mitchell, then attorney-general, to take pity on him. He sometimes interrupted meetings to take calls from him; but whether it was actually Mitchell, no one knew.

Rather than be a fugitive, which was tiring, he wanted to be untouchable. In 1981 or so he tried to buy half of the island of Barbuda, off Antigua, to set up “the Principality of the Sovereign Order of New Aragon”. There, on the vast pink beaches swept by frigate birds and scattered with the wreckage of other people's ships, the Feds could never get a hand on him. And indeed, save for a not-quite-reliable death certificate, they never did.

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Overview

May 29th 2008
From The Economist print edition

In **America** the S&P/Case-Shiller national house-price index fell by 14.1% in the year to the first quarter, the biggest drop in the series's 20-year history. New home sales picked up by 3.3% in April, albeit from a 17-year low in March. The index of consumer confidence compiled by the Conference Board, a business-research group, fell to its lowest level since October 1992.

Businessmen in **Italy** were a little less gloomy in May, according to ISAE, a Rome-based research group. Its index of business confidence rose for the first time in seven months. The mood in **France** worsened. The sentiment index published by INSEE, the national statistics office, fell from 106 to 102, its lowest since December 2005.

Italy's economy flirted with recession on either side of the New Year. GDP rose by 0.4% in the first three months of 2008, after having declined by as much in the previous quarter.

Consumer-price inflation in **South Africa** rose to 11.1% in April, the highest in five years. Inflation is a worry for policymakers in other emerging markets too. **Hungary's** monetary council raised its benchmark interest rate, from 8.25% to 8.5%, to try to bring inflation down to its 3% target. **Malaysia's** central bank kept its benchmark interest rate at 3.5%, but said it would act if the risks of higher inflation grew. **Poland's** central bank also kept its key rate unchanged, at 5.75%, but warned that meeting its inflation objective may require further interest-rate increases.

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Output, prices and jobs

May 29th 2008
From The Economist print edition

Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production	Consumer prices			Unemployment
	latest	qtr*	2008†	2009†	latest	latest	year ago	2008†	rate‡, %
United States	+2.5 Q1	+0.6	+1.1	+1.7	+0.2 Apr	+3.9 Apr	+2.6	+3.5	5.0 Apr
Japan	+1.0 Q1	+3.3	+1.3	+1.5	-0.7 Mar	+1.2 Mar	-0.1	+0.9	3.8 Mar
China	+10.6 Q1	na	+9.6	+9.0	+15.7 Apr	+8.5 Apr	+3.0	+5.9	9.5 2007
Britain	+2.5 Q1	+1.6	+1.7	+1.7	+0.2 Mar	+3.0 Apr§	+2.8	+2.6	5.2 Mar††
Canada	+2.9 Q4	+0.8	+1.4	+2.1	-2.9 Feb	+1.7 Apr	+2.2	+1.8	6.1 Apr
Euro area	+2.2 Q1	+2.8	+1.6	+1.5	+2.0 Mar	+3.3 Apr	+1.9	+3.0	7.1 Mar
Austria	+3.5 Q1	+3.2	+2.3	+2.3	-1.1 Mar	+3.3 Apr	+1.8	+2.3	4.1 Mar
Belgium	+2.1 Q1	+1.6	+1.7	+1.7	+5.7 Feb	+4.2 Apr	+1.8	+2.9	10.3 Apr‡‡
France	+2.2 Q1	+2.6	+1.5	+1.5	+1.0 Mar	+3.0 Apr	+1.3	+2.7	7.5 Q4§§
Germany	+1.8 Q1	+6.1	+1.7	+1.6	+4.6 Mar	+2.4 Apr	+2.1	+2.6	7.9 May
Greece	+3.6 Q1	+4.6	+2.8	+3.0	-5.4 Mar	+4.4 Apr	+2.5	+3.9	8.0 Feb
Italy	+0.2 Q1	+1.6	+0.6	+1.0	-2.5 Mar	+3.3 Apr	+1.5	+2.8	6.0 Q4
Netherlands	+3.1 Q1	+1.0	+2.5	+1.9	-0.6 Mar	+2.0 Apr	+1.8	+2.3	4.0 Apr††
Spain	+2.7 Q1	+1.2	+2.2	+1.8	-13.3 Mar	+4.7 May	+2.3	+3.6	9.3 Mar
Czech Republic	+5.4 Q1	na	+4.7	+5.4	-2.1 Mar	+6.8 Apr	+2.5	+6.3	5.2 Apr
Denmark	+1.9 Q4	+1.2	+1.5	+1.6	-2.5 Mar	+3.2 Apr	+1.7	+2.9	1.8 Apr
Hungary	+1.6 Q1	na	+2.3	+3.4	+4.3 Mar	+6.6 Apr	+8.8	+5.9	8.0 Mar††
Norway	+0.9 Q1	+0.8	+2.9	+2.5	+4.0 Mar	+3.1 Apr	+0.3	+3.4	2.4 Mar***
Poland	+6.1 Q4	na	+5.1	+4.3	+14.9 Apr	+4.0 Apr	+2.3	+4.2	10.5 Apr‡‡
Russia	+8.0 Q1	na	+7.1	+6.2	+9.2 Apr	+13.3 Mar	+7.4	+13.0	6.6 Apr‡‡
Sweden	+2.8 Q4	+3.1	+2.3	+2.1	+0.8 Mar	+3.4 Apr	+1.9	+3.0	6.0 Apr‡‡
Switzerland	+3.6 Q4	+4.2	+2.1	+1.7	+9.1 Q4	+2.3 Apr	+0.5	+2.0	2.6 Apr
Turkey	+3.4 Q4	na	+3.2	+4.1	+2.4 Mar	+9.7 Apr	+10.7	+10.2	11.6 Q1‡‡
Australia	+3.9 Q4	+2.4	+3.0	+2.9	+0.1 Q4	+4.2 Q1	+2.4	+3.5	4.2 Apr
Hong Kong	+6.8 Q1	+7.4	+4.6	+4.5	-0.3 Q4	+5.4 Apr	+1.3	+5.3	3.3 Apr††
India	+8.4 Q4	na	+7.6	+7.1	+3.0 Mar	+7.9 Mar	+6.7	+6.0	7.2 2007
Indonesia	+6.3 Q1	na	+5.7	+5.9	+1.4 Mar	+9.0 Apr	+6.3	+9.0	9.1 Dec
Malaysia	+7.1 Q1	nil	+5.8	+5.8	+3.0 Mar	+3.0 Apr	+1.5	+2.8	3.0 Q4
Pakistan	+7.0 2007**	na	+4.6	+5.1	+3.2 Mar	+17.2 Apr	+6.9	+12.1	6.2 2006
Singapore	+6.7 Q1	+14.6	+4.5	+5.0	-5.7 Apr	+7.5 Apr	+0.6	+4.3	2.0 Q1
South Korea	+5.7 Q1	+2.9	+4.5	+4.3	+10.0 Mar	+4.1 Apr	+2.5	+2.9	3.2 Apr
Taiwan	+6.4 Q4	na	+4.3	+4.3	+9.6 Apr	+3.9 Apr	+0.7	+2.6	3.9 Apr
Thailand	+6.0 Q1	+5.9	+4.8	+4.6	+10.1 Mar	+6.2 Apr	+1.8	+6.2	1.5 Feb
Argentina	+9.1 Q4	+8.0	+6.2	+4.5	+8.6 Apr	+8.9 Apr	+8.9	+10.3	8.4 Q1‡‡
Brazil	+6.2 Q4	+6.6	+4.6	+4.0	+1.2 Mar	+5.0 Apr	+3.0	+5.1	8.5 Apr‡‡
Chile	+4.0 Q4	+3.7	+3.6	+3.4	-1.0 Mar	+8.3 Apr	+2.5	+6.7	7.6 Mar††‡‡
Colombia	+8.1 Q4	+6.8	+5.0	+4.5	-9.4 Mar	+5.7 Apr	+6.3	+5.5	11.1 Mar‡‡
Mexico	+2.6 Q1	+2.1	+2.1	+2.5	-4.9 Mar	+4.6 Apr	+4.0	+4.7	3.6 Apr‡‡
Venezuela	+4.8 Q1	na	+6.1	+4.9	+12.2 Feb	+29.3 Apr	+19.4	+29.6	8.2 Q1‡‡
Egypt	+6.9 Q1	na	+7.0	+6.8	+7.5 2007**	+16.4 Apr	+11.7	+10.9	9.0 Q4‡‡
Israel	+5.2 Q1	+5.4	+3.5	+3.7	+9.3 Mar	+4.7 Apr	-1.3	+4.1	6.3 Q1
Saudi Arabia	+3.5 2007	na	+6.0	+5.6	na	+10.5 Apr	+2.9	+8.5	na
South Africa	+4.0 Q1	+2.1	+3.9	+4.4	-1.1 Mar	+11.1 Apr	+7.0	+8.2	23.0 Sep‡‡
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*									
Estonia	+0.4 Q1	+7.8	+2.8	+3.7	-4.9 Mar	+11.4 Apr	+5.5	+9.3	5.5 Mar
Finland	+3.7 Q4	+3.8	+2.7	+2.7	+2.5 Mar	+3.5 Apr	+2.6	+3.0	5.8 Apr
Iceland	+4.6 Q4	+1.4	+1.4	+2.6	+0.4 2007	+12.3 May	+4.7	+7.5	1.0 Apr‡‡
Ireland	+3.5 Q4	-3.3	+2.4	+2.2	+7.0 Mar	+4.3 Apr	+5.1	+3.2	5.5 Apr
Latvia	+3.6 Q1	na	+2.4	+3.0	-5.5 Mar	+17.5 Apr	+8.9	+13.2	4.9 Mar
Lithuania	+6.9 Q1	-0.8	+5.8	+5.5	na	+11.7 Apr	+4.8	+8.8	4.7 Mar‡‡
Luxembourg	+3.8 Q4	+7.4	+3.9	+3.6	-0.2 Feb	+3.5 Apr	+2.1	+3.4	4.2 Mar‡‡
New Zealand	+2.8 Q4	+3.1	+1.7	+2.3	+4.2 Q4	+3.4 Q1	+2.5	+3.2	3.6 Q1
Peru	+5.6 Mar	na	+7.5	+6.4	+6.4 Mar	+5.5 Apr	-0.1	+4.8	8.5 Apr‡‡
Philippines	nil	nil	+5.4	+5.5	+8.6 Feb	+8.3 Apr	+2.3	+5.8	7.4 Q1‡‡
Portugal	+0.9 Q1	-1.6	+1.5	+1.6	-5.2 Mar	+2.5 Apr	+2.7	+2.4	7.6 Q1‡‡
Slovakia	+8.7 Q1	na	+7.5	+5.7	+1.8 Mar	+4.2 Apr	+2.7	+3.5	7.4 Apr‡‡
Slovenia	+4.7 Q4	na	+4.5	+4.0	+1.0 Mar	+6.5 Apr	+2.6	+5.2	6.9 Mar‡‡

*% change on previous quarter, annual rate. †*The Economist* poll or Economist Intelligence Unit estimate/forecast. ‡National definitions. §RPI inflation rate 4.2% in Apr. **Year ending June. ††Latest three months. ‡‡Not seasonally adjusted. §§New series. ***Centred 3-month average

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The Economist commodity-price index

May 29th 2008
From The Economist print edition

The Economist commodity-price index

2000=100

	May 20th	May 27th*	% change on one month	% change on one year
Dollar index				
All items	255.8	254.8	-1.2	+26.3
Food	254.5	252.2	-0.7	+54.9
Industrials				
All	257.6	258.1	-1.9	+2.3
Nfa†	200.0	206.3	+7.3	+25.5
Metals	289.1	286.6	-5.1	-4.6
Sterling index				
All items	197.1	195.7	-1.4	+26.7
Euro index				
All items	151.3	149.9	-1.9	+8.3
Gold				
$ per oz	916.95	909.70	+3.6	+38.3
West Texas Intermediate				
$ per barrel	128.93	128.46	+11.2	+103.1

*Provisional †Non-food agriculturals.

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Producer prices

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From The Economist print edition

Producer prices are measured as goods leave the factory. They used to be closely watched as an indicator of pipeline inflation. Two trends undermined their usefulness: the steady decline in manufactured goods as a share of spending, and increasing efficiency in retailing, which meant that factory-gate inflation did not always show up in the shops. But their relevance is increasing again. A steadily growing slice of retail-price inflation has been caused by rising oil and commodity prices. Producer prices are more sensitive to raw-material costs than the price of services is and so pick up inflation signals sooner. A year ago, only a handful of rich countries had factory-gate inflation of more than 4%. Now many of them do.

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Trade, exchange rates, budget balances and interest rates

May 29th 2008
From The Economist print edition

Trade, exchange rates, budget balances and interest rates

	Trade balance* latest 12 months, $bn	Current-account balance latest 12 months, $bn	Current-account balance % of GDP 2008†	Currency units, per $ May 28th	Currency units, per $ year ago	Budget balance % of GDP 2008†	Interest rates, % 3-month latest	Interest rates, % 10-year gov't bonds, latest
United States	−823.8 Mar	−738.6 Q4	−4.6	-	-	−2.4	2.07	4.01
Japan	+102.8 Mar	+216.6 Mar	+4.7	105	122	−2.9	0.75	1.74
China	+256.5 Apr	+249.9 2006	+10.5	6.94	7.65	0.5	4.49	4.42
Britain	−179.7 Mar	−115.4 Q4	−4.0	0.50	0.51	−3.2	5.82	4.96
Canada	+46.2 Mar	+12.5 Q4	−0.1	0.99	1.07	0.4	2.68	3.81
Euro area	+14.1 Mar	+5.3 Mar	−0.1	0.64	0.74	−0.8	4.86	4.35
Austria	+1.0 Feb	+12.2 Q4	+3.0	0.64	0.74	−0.4	4.86	4.52
Belgium	+14.3 Feb	+2.7 Dec	+2.1	0.64	0.74	−0.4	4.92	4.64
France	−59.3 Mar	−35.7 Mar	−1.7	0.64	0.74	−2.9	4.86	4.53
Germany	+273.9 Mar	+264.5 Mar	+6.2	0.64	0.74	1.1	4.86	4.35
Greece	−59.4 Feb	−45.2 Mar	−13.7	0.64	0.74	−2.6	4.86	4.80
Italy	−12.9 Mar	−57.0 Mar	−2.5	0.64	0.74	−2.6	4.86	4.86
Netherlands	+57.3 Mar	+50.7 Q4	+6.3	0.64	0.74	0.6	4.86	4.53
Spain	−147.1 Mar	−150.3 Feb	−9.2	0.64	0.74	−0.7	4.86	4.56
Czech Republic	+4.4 Mar	−4.7 Mar	−2.9	16.1	21.1	−2.5	4.16	4.95
Denmark	+4.1 Mar	+4.1 Mar	+0.9	4.77	5.55	3.6	5.40	4.61
Hungary	+0.2 Mar	−6.9 Q4	−5.9	155	187	−4.2	8.69	8.25
Norway	+66.9 Apr	+64.1 Q4	+16.8	5.04	6.06	17.5	6.51	4.75
Poland	−14.7 Mar	−18.6 Mar	−3.8	2.17	2.85	−2.1	6.48	6.18
Russia	+152.9 Mar	+92.4 Q1	+5.4	23.6	25.9	2.5	10.50	6.54
Sweden	+19.3 Mar	+38.1 Q4	+7.2	5.98	6.92	2.4	4.04	4.36
Switzerland	+13.6 Apr	+71.1 Q4	+14.9	1.04	1.23	0.9	2.77	3.12
Turkey	−66.8 Mar	−40.4 Mar	−6.5	1.23	1.33	−2.9	17.67	6.66‡
Australia	−21.9 Mar	−56.4 Q4	−5.9	1.04	1.22	1.5	7.74	6.50
Hong Kong	−24.4 Apr	+28.0 Q4	+9.1	7.81	7.80	2.9	1.89	3.01
India	−77.7 Mar	−12.8 Q4	−2.4	42.7	40.9	−3.2	7.46	8.40
Indonesia	+39.8 Mar	+11.0 Q4	+2.3	9,300	8,840	−2.1	8.64	7.11‡
Malaysia	+31.5 Mar	+28.9 Q4	+12.5	3.24	3.40	−3.1	3.63	4.26‡
Pakistan	−19.1 Apr	−8.4 Q4	−8.8	67.8	60.7	−4.7	13.54	10.11‡
Singapore	+30.5 Apr	+35.8 Q1	+24.4	1.36	1.53	1.0	1.38	3.05
South Korea	+6.0 Apr	+2.5 Mar	+0.3	1,037	931	0.2	5.35	5.53
Taiwan	+13.1 Apr	+32.2 Q1	+5.3	30.5	33.0	−1.8	2.70	2.65
Thailand	+8.8 Mar	+13.3 Mar	+3.2	32.4	34.6	−3.1	3.38	4.60
Argentina	+11.7 Apr	+7.3 Q4	+2.8	3.12	3.08	1.1	14.44	na
Brazil	+31.7 Apr	−14.7 Apr	−0.8	1.67	1.96	−1.8	11.64	6.16‡
Chile	+22.2 Apr	+7.2 Q4	+2.6	480	528	7.0	6.60	4.59‡
Colombia	−0.2 Feb	−5.9 Q4	−3.5	1,767	1,930	−1.7	9.49	5.56‡
Mexico	−9.6 Apr	−4.8 Q1	−1.2	10.3	10.8	nil	7.44	8.15
Venezuela	+23.7 Q4	+20.0 Q4	+7.0	3.15	4.23§	2.1	17.70	6.55‡
Egypt	−20.5 Q4	+0.5 Q4	+0.3	5.36	5.70	−7.2	9.21	4.74‡
Israel	−12.4 Apr	+5.0 Q4	+0.2	3.29	4.05	−1.4	3.73	5.34
Saudi Arabia	+150.8 2007	+95.0 2007	+27.7	3.75	3.75	17.9	2.61	na
South Africa	−10.6 Mar	−20.6 Q4	−7.8	7.68	7.19	0.4	12.20	9.78
MORE COUNTRIES Data for the countries below are not provided in printed editions of *The Economist*								
Estonia	−4.4 Feb	−3.4 Mar	−12.7	10.0	11.7	0.2	6.47	na
Finland	+12.3 Mar	+12.5 Mar	+4.1	0.64	0.74	4.6	4.70	4.49
Iceland	−1.6 Apr	−3.2 Q4	−12.0	73.7	61.9	1.4	15.82	na
Ireland	+37.0 Feb	−12.7 Q4	−4.0	0.64	0.74	−0.9	4.86	4.63
Latvia	−7.3 Mar	−6.3 Mar	−13.2	0.45	0.52	nil	5.14	na
Lithuania	−7.8 Mar	−5.8 Mar	−11.5	2.21	2.57	−0.7	5.18	na
Luxembourg	−6.1 Feb	+3.9 Q4	na	0.64	0.74	1.5	4.86	na
New Zealand	−3.5 Apr	−10.2 Q4	−7.3	1.28	1.37	3.1	7.30	6.48
Peru	+8.3 Mar	+1.5 Q4	+0.4	2.86	3.18	1.6	5.50	na
Philippines	−7.3 Mar	+6.4 Dec	+4.0	43.7	46.3	−0.1	6.56	na
Portugal	−28.4 Feb	−24.5 Mar	−8.3	0.64	0.74	−2.5	4.86	4.72
Slovakia	−0.6 Mar	−4.5 Jan	−3.3	19.7	25.4	−2.1	4.19	4.75
Slovenia	−3.3 Mar	−2.6 Feb	−2.5	0.64	0.74	−0.2	na	na

*Merchandise trade only. †*The Economist* poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.

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Markets

May 29th 2008
From The Economist print edition

Markets

	Index May 28th	% change on one week	% change on Dec 31st 2007 in local currency	% change on Dec 31st 2007 in $ terms
United States (DJIA)	12,594.0	-0.1	-5.1	-5.1
United States (S&P 500)	1,390.8	nil	-5.3	-5.3
United States (NAScomp)	2,486.7	+1.6	-6.2	-6.2
Japan (Nikkei 225)	13,709.4	-1.6	-10.4	-4.5
Japan (Topix)	1,348.7	-1.6	-8.6	-2.5
China (SSEA)	3,629.3	-2.4	-34.3	-30.9
China (SSEB, $ terms)	248.5	-0.8	-35.4	-32.1
Britain (FTSE 100)	6,069.6	-2.1	-6.0	-6.5
Canada (S&P TSX)	14,688.6	-0.7	+6.2	+5.5
Euro area (FTSE Euro 100)	1,186.9	-1.2	-13.7	-7.7
Euro area (DJ STOXX 50)	3,743.2	-1.3	-14.9	-9.1
Austria (ATX)	4,388.8	-0.8	-2.8	+3.9
Belgium (Bel 20)	3,710.9	-1.5	-10.1	-3.9
France (CAC 40)	4,971.1	-1.1	-11.5	-5.4
Germany (DAX)*	7,033.8	-0.1	-12.8	-6.8
Greece (Athex Comp)	4,090.1	-1.5	-21.0	-15.6
Italy (S&P/MIB)	32,758.0	-0.9	-15.0	-9.2
Netherlands (AEX)	481.7	-1.2	-6.6	-0.2
Spain (Madrid SE)	1,451.5	-2.4	-11.6	-5.5
Czech Republic (PX)	1,675.9	+0.4	-7.7	+4.1
Denmark (OMXCB)	422.9	-1.8	-5.8	+0.7
Hungary (BUX)	22,738.2	-0.2	-13.3	-3.6
Norway (OSEAX)	568.2	-3.9	-0.3	+7.3
Poland (WIG)	46,868.5	-0.3	-15.8	-4.7
Russia (RTS, $ terms)	2,396.9	-2.9	+0.8	+4.6
Sweden (Aff.Gen)	313.0	-0.6	-8.1	-0.6
Switzerland (SMI)	7,474.5	-1.3	-11.9	-4.0
Turkey (ISE)	39,384.9	-4.0	-29.1	-32.3
Australia (All Ord.)	5,754.5	-2.7	-10.4	-1.5
Hong Kong (Hang Seng)	24,249.5	-4.8	-12.8	-12.9
India (BSE)	16,525.4	-4.2	-18.5	-24.9
Indonesia (JSX)	2,433.8	-2.4	-11.4	-10.5
Malaysia (KLSE)	1,260.6	-1.6	-12.8	-11.0
Pakistan (KSE)	12,255.0	-12.3	-12.9	-20.9
Singapore (STI)	3,132.8	-2.0	-9.6	-4.6
South Korea (KOSPI)	1,805.6	-2.3	-4.8	-14.1
Taiwan (TWI)	8,665.7	-3.9	+1.9	+8.3
Thailand (SET)	833.0	-5.8	-2.9	+0.9
Argentina (MERV)	2,233.4	+0.6	+3.8	+4.8
Brazil (BVSP)	73,153.0	+1.2	+14.5	+22.3
Chile (IGPA)	14,304.5	+1.6	+1.6	+5.4
Colombia (IGBC)	9,854.8	-1.6	-7.8	+5.2
Mexico (IPC)	31,647.0	+1.7	+7.1	+13.0
Venezuela (IBC)	34,793.5	-2.8	-8.2	-37.4
Egypt (Case 30)	11,016.9	+3.6	+5.2	+8.4
Israel (TA-100)	1,026.6	+0.1	-11.1	+4.0
Saudi Arabia (Tadawul)	9,491.3	-1.9	+19.6	+19.6
South Africa (JSE AS)	32,209.0	-2.1	+11.2	-1.1
Europe (FTSEurofirst 300)	1,326.7	-1.0	-11.9	-5.9
World, dev'd (MSCI)	1,515.1	-1.1	-4.6	-4.6
Emerging markets (MSCI)	1,195.5	-3.1	-4.0	-4.0
World, all (MSCI)	384.8	-1.4	-4.6	-4.6
World bonds (Citigroup)	768.5	-1.3	+5.2	+5.2
EMBI+ (JPMorgan)	440.5	-0.9	+1.6	+1.6
Hedge funds (HFRX)	1,324.8	-0.2	-0.4	-0.4
Volatility, US (VIX)	22.5	21.6	22.5	(levels)
CDSs, Eur (iTRAXX)†	75.3	+15.8	+48.7	+58.9
CDSs, N Am (CDX)†	110.0	+8.5	+25.6	+25.6
Carbon trading (EU ETS) €	26.2	+1.9	+17.6	+25.7

*Total return index. †Credit-default swap spreads, basis points.
Sources: National statistics offices, central banks and stock exchanges; Thomson Datastream; Reuters; WM/Reuters; JPMorgan Chase; Bank Leumi le-Israel; CBOE; CMIE; Danske Bank; EEX; HKMA; Markit; Standard Bank Group; UBS; Westpac.

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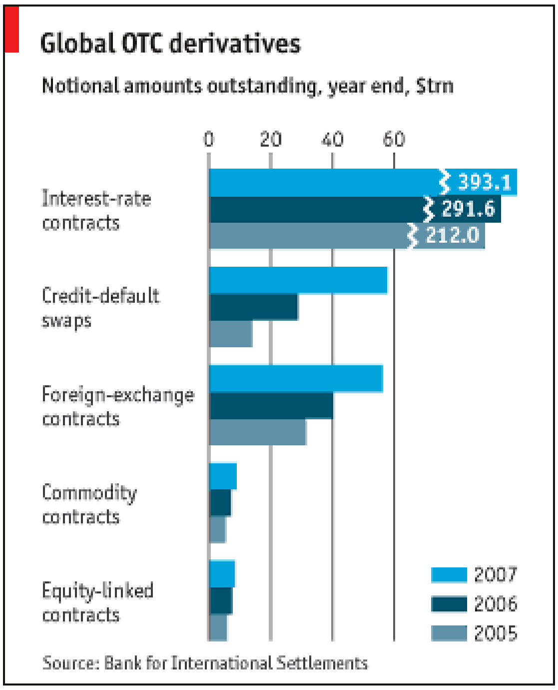
Global OTC derivatives

May 29th 2008
From The Economist print edition



The notional value of over-the-counter (OTC) derivatives rose by almost 44%, to $596 trillion in the year to December, according to new figures from the Bank for International Settlements. A derivative is a financial contract whose value is based on the price of assets, such as stocks, bonds, commodities or currencies. OTC derivatives are tailored bets supplied by specialists, such as investment banks, and distinct from standardised contracts traded at arms-length on an exchange. The notional value is not the size of the bet; rather it is a reference value against which payments are set. So the notional value of interest-rate contracts, the most common OTC derivative, represents the “principal” rather than the “coupon”.

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