

INSIDE: A 14-PAGE SPECIAL REPORT ON CORPORATE SOCIAL RESPONSIBILITY

# The Economist

JANUARY 19TH-25TH 2008

[www.economist.com](http://www.economist.com)

Romney's win in Michigan

Cloned food

Satellite wars

The global inflation scare

Democracy in retreat

## Invasion of the sovereign-wealth funds



PRINT EDITION
<p><b>Invasion of the sovereign-wealth funds</b></p>
<a href="#">Full contents</a>   <a href="#">Subscribe</a>
<a href="#">Enlarge current cover</a>
<a href="#">Past issues/regional covers</a>
NEWS ANALYSIS
POLITICS THIS WEEK
BUSINESS THIS WEEK
OPINION
<a href="#">Leaders</a> <a href="#">Letters to the editor</a> <a href="#">Blogs</a> <a href="#">Columns</a> <a href="#">Kallery</a>
WORLD
<a href="#">United States</a> <a href="#">The Americas</a> <a href="#">Asia</a> <a href="#">Middle East &amp; Africa</a> <a href="#">Europe</a> <a href="#">Britain</a> <a href="#">International</a>
<div>Country Briefings</div> <div>Go</div> <div>Cities Guide</div> <div>Go</div>
SPECIAL REPORTS
BUSINESS
<a href="#">Management</a> <a href="#">Business Education</a>
FINANCE & ECONOMICS
<a href="#">Economics Focus</a> <a href="#">Economics A-Z</a>
SCIENCE & TECHNOLOGY
<a href="#">Technology Quarterly</a>
BOOKS & ARTS
<a href="#">Style Guide</a>
PEOPLE
<a href="#">Obituary</a>
MARKETS & DATA
<a href="#">Weekly Indicators</a> <a href="#">Currencies</a> <a href="#">Rankings</a> <a href="#">Big Mac Index</a> <a href="#">Chart Gallery</a>
DIVERSIONS
<a href="#">Correspondent's Diary</a>
RESEARCH TOOLS
AUDIO AND VIDEO
DELIVERY OPTIONS
<a href="#">E-mail Newsletters</a> <a href="#">Audio edition</a> <a href="#">Mobile Edition</a> <a href="#">RSS Feeds</a> <a href="#">Screensaver</a>
CLASSIFIED ADS
The Economist Group
<a href="#">Economist Intelligence Unit</a> <a href="#">Economist Conferences</a> <a href="#">The World In</a> <a href="#">Intelligent Life</a> <a href="#">CFO</a> <a href="#">Roll Call</a> <a href="#">European Voice</a> <a href="#">EuroFinance</a> <a href="#">Economist Diaries and Business Gifts</a> <a href="#">Reprints and Permissions</a>
Advertisement

Print Edition

January 19th 2008

On the cover

The biggest worry about rich Arab and Asian states buying up banks is the potential backlash: [leader](#)



The world this week

Politics this week

Business this week

KAL's cartoon

Leaders

Capital markets

The invasion of the sovereign-wealth funds

Democracy in retreat

Freedom marches backward

Ethical capitalism

How good should your business be?

The militarisation of space

Dangerous driving in the heavens

Global warming

Get the price right

Letters

On Pakistan, Belgians, Italy, cliff jumping, China, tribes, Mormons, Ivar Kreuger

Briefing

The militarisation of space

Disharmony in the spheres

United States

Michigan's Republican primary

All must have prizes

The Democrats in Michigan

Vote early at your peril

Sex, race and Democrats

Outrage all round

On the campaign trail

Primary colour

The economy

Stampede to stimulus

University fees

Affording Ivy

Depopulation

The Great Plains drain

Lexington

Blood and oil

The Americas

Brazil's economy

This time it will all be different

Panama

Party time

Colombia

Liberation politics

Barbados

Sweet success

Asia

Taiwan's legislative election

Bowing out

Japan

The "caretaker"

South Korea

The "bulldozer"

Australia's new prime minister

Rudd, sweat and tears

Sir Edmund Hillary

Plain man, mighty deeds

India's army

Unfit for service

Previous print editions

Jan 12th 2008

Jan 5th 2008

Dec 22nd 2007

Dec 15th 2007

Dec 8th 2007

More print editions and covers »

Subscribe

Subscribe to the print edition

Or buy a Web subscription for full access online

 RSS feeds

Receive this page by RSS feed

Advertisement

A special report on corporate social responsibility

Just good business

The feelgood factor

The next question

A stitch in time

A change in climate

The good consumer

Going global

Do it right

Sources and acknowledgments

Offer to readers

Business

The food industry

Son of Frankenfood?

Corporate law

The battle of StoneRidge

Regulation in Japan

Crime and punishment

Italy's violin cluster

Con brio

Spanish-language publishing

Lost in translation no more

Media in America

Reading the Metro

Virtualisation

The rise of the hypervisor

Face value

Google's guru of giving

Briefing

Sovereign-wealth funds

Asset-backed insecurity

Finance & Economics

Global inflation

A delicate condition

Bank losses

A Citi situation

Buttonwood

Finding default

Indian IPOs

Power play

Portuguese banks

Millennium bug

American house prices

Baby boom and bust

Economics focus

Selling sex

Science & Technology

Pricing and the brain

Hitting the spot

Acoustic shielding

Sound reflections

A messenger from Mercury

Syphilis

Montezuma's revenge

A bombing in Kabul  
A bubble bursts

Middle East & Africa

George Bush and the Arabs  
Hard to make friends

Iraq  
A hint of political compromise at last

Kenya  
A cracked nation holds its breath

South Africa  
Let's all arrest one another

Zimbabwe  
A serious rival, at last?

Advertisement

Europe

Germany's state elections  
Pay and punishment

French defence policy  
En garde

French broadcasting  
No English, please

Serbia  
Still surly

Energy in Poland  
Walking on hot coals

The race for the EU presidency  
Blair for president?

Charlemagne  
Roll up, roll up, get your energy here

Britain

Northern Rock  
Running out of time

Party-funding scandal  
Here we go again

Biofuels  
Sugar in the tank


Children's television  
School's out

Public-sector pay disputes  
The pedagogues are revolting 

Equality v jobs  
Robbing Peter to pay Pauline 

Sprucing up cities  
The regeneration game 

Bagehot  
The Scottish Obama

 Articles flagged with this icon are printed only in the British edition of *The Economist*

International

Measuring liberty  
When freedom stumbles

The World Bank  
Lin's long swim

Broadband  
Open up those highways

Advertisement

Antarctic science  
Snow place like home

Books & Arts

The secret of happiness  
It's in Iceland

America and the world  
Big think that gets you a headline

British post-war history  
At the centre

Crime writing  
Death watch

The American Museum of Finance  
Curating capitalism

Obituary

John Harvey-Jones

Economic and Financial Indicators

Overview

Output, prices and jobs

The Economist commodity-price index

The Economist commodity-price index

Trade, exchange rates, budget balances and interest rates

Markets

Latin American growth forecasts

Advertisement

Classified ads						Sponsors' feature	About sponsorship »
<b>Jobs</b> CEO Bank Serbia The Chief Executive Officer will be responsible for directing the operations of a commercia....	<b>Business / Consumer</b> #1 rated internet business looking for professional consultants. No previous technical experience required.	<b>Tenders</b> Apply Today - WSI is the world's largest network of professional Internet Marketing Consultants. Full Training and Support.	<b>Property</b> Exclusive NYC condo for sale Exclusive New York City condo Luxury Time Warner Center, midtown Manhattan 2 bed, ....	<b>Jobs</b> Chief of Party - Modernizing Financial Institutions Seeking Chief of Party for USAID project in West Bank/Gaza Stri....	<b>Business / Consumer</b> #1 Career Opportunity. World's top Internet Franchise is currently looking to expand their franchise. Become an Internet Consultant Today. Apply Here.		

## Politics this week

Jan 17th 2008

From The Economist print edition

George Bush toured the **Middle East**, visiting seven countries in his effort to advance peace between Israelis and Palestinians and to rally Gulf Arabs against Iran. The president promised the Saudis and other Gulf countries more arms, while praising their modest progress towards giving their people more of a democratic say. [See article](#)

In one of the bloodiest weeks for many months in the **Gaza Strip**, Israeli forces killed at least 23 Palestinians, two-thirds of them armed fighters, in an effort to stop them firing rockets at nearby Israeli towns.

A right-wing party, Yisrael Beiteinu, quit the **Israeli** government coalition led by Ehud Olmert, condemning his peace talks with the Palestinian president, Mahmoud Abbas, and cutting the government's majority in the 120-seat parliament from 18 to 7.

After a year of deadlock, the **Iraqi** parliament passed a law that would restore various rights, including pensions and jobs, to former members of the long-ruling Baath party (bar its more senior levels), prompting the main Sunni alliance in parliament to return to the Shia-led coalition government. Meanwhile, the IMF predicted a good year for Iraq, with growth up 7% and buoyant oil exports. [See article](#)

Political deadlock continued in **Kenya** after disputed elections. The new parliament, dominated by the opposition, met for the first time, but President Mwai Kibaki continued to resist calls to share power or hold fresh elections. Several more opposition demonstrators were killed by the police. [See article](#)

Prosecutors in **South Africa** said they would charge Jackie Selebi, the chief of police, with corruption. He has been suspended from duty and resigned as head of Interpol, the international police agency. [See article](#)

The Zambezi and other rivers threatened to flood swathes of **Mozambique**, where at least 50,000 people have already left their homes. The UN undertook a massive relief effort.



## Dr Lula pays a house call

After talks in Havana with **Fidel Castro**, Brazil's president, Luiz Inácio Lula da Silva, said that the 81-year-old Cuban leader was in "impeccable" health and ready to resume his political role. Shortly afterwards, Mr Castro released a statement explaining why he was still too ill to campaign in parliamentary elections. He has not been seen in public since undergoing stomach surgery 17 months ago.

Two female hostages were released by **Colombia's** left-wing FARC rebels after being held captive for six years in the jungle. Venezuela's president, Hugo Chávez, helped broker the deal. [See article](#)

## Romney's romp

**Mitt Romney** received a much-needed boost to his presidential ambitions by

winning the Republican primary in Michigan. John McCain came nine percentage points behind in second place, proving again that the opinion polls are not to be trusted in the fluid early stages of the election process. After the vote the party's leading candidates decamped to South Carolina, which holds its Republican primary on January 19th. [See article](#)



The **Democrats** became embroiled in a row over race following Hillary Clinton's suggestion that Lyndon Johnson and Martin Luther King played equal roles in the civil-rights era. After senior black politicians waded into the debate, Mrs Clinton and Barack Obama accused each other of stirring up trouble ahead of the party's primary in South Carolina on January 26th. [See article](#)

A third-party presidential campaign led by **Michael Bloomberg** came a step closer when two supporters began circulating a petition to draft him as a candidate. The mayor of New York said he was flattered, but reiterated that he would not join the fray.

A study from the Guttmacher Institute reported that the number of **abortions** performed in the United States dropped to 1.2m in 2005, the lowest level since 1976. The authors cited several explanations for the fall, including better access to contraception.

## Fortress France

President Nicolas Sarkozy said **France** would open a permanent military base in the United Arab Emirates, its first in a Gulf state and in a country where it has no colonial history. France is conducting a defence review: the decision may signal a shift in policy. [See article](#)

In another blow to **Italy's** shaky coalition government, the justice minister, Clemente Mastella, resigned after his wife was placed under house arrest as part of a corruption investigation.

Relations between **Russia** and **Britain** deteriorated further after Russia said it would stop giving visas to employees of the British Council, a cultural organisation, and forced the council's offices in St Petersburg and Yekaterinburg to close. Britain is at odds with Russia over its refusal to deport a former KGB officer to face charges over the poisoning in London of Alexander Litvinenko in late 2006.

## Taiwanese straits

In **Taiwan's** legislative elections, the opposition Nationalist Party, the Kuomintang, trounced the ruling Democratic Progressive Party. Taiwan's president, Chen Shui-bian, resigned as chairman of the DPP, which faces an uphill struggle in March's presidential election. [See article](#)

A four-man suicide-bombing squad attacked Kabul's only five-star hotel, killing at least eight people. **Afghanistan's** government blamed the Taliban, which threatened further attacks against Western restaurants in Kabul. [See article](#)

On the day a ceasefire agreement between **Sri Lanka's** government and the Liberation Tigers of Tamil Eelam was formally annulled, more than 30 people were killed in a bomb attack on a bus in the south of the island.

The coalition government in **Japan**, led by the Liberal Democratic Party, used its majority in the lower house of parliament to push through the renewal of a bill allowing the navy's ships to take part in refuelling operations for the war in Afghanistan. The opposition Democratic Justice Party did not carry out its threat to bring down the government. [See article](#)

Manmohan Singh, **India's** prime minister, visited **China** for the first time since taking office in 2004. Both countries promised to increase trade and military co-operation.

Reuters

**Sir Edmund Hillary**, conqueror of Mount Everest in 1953, died at the age of 88. [See article](#)





---

Copyright © 2008 The Economist Newspaper and The Economist Group. All rights reserved.

---

## Business this week

Jan 17th 2008

From The Economist print edition

Citigroup and Merrill Lynch tapped into more **foreign investment** to repair their tattered balance sheets. After reporting a fourth-quarter net loss of \$9.8 billion and further subprime-related write-downs of around \$18 billion, **Citigroup** said it would raise an extra \$14.5 billion from the governments of Singapore and Kuwait as well as private financiers; **Merrill Lynch** announced it was receiving an additional \$6.6 billion from Asian and Middle Eastern investment groups. [See article](#)

Quarterly net profit at **JPMorgan Chase** fell by 34% compared with a year ago. The Wall Street bank's subprime-related write-downs amounted to \$1.3 billion.

### To the rescue

**Countrywide Financial's** share price tumbled again. After months in decline it had risen in anticipation of **Bank of America's** announcement on January 11th that it would take over the beleaguered mortgage lender. The optimism soured when analysts questioned the \$4 billion all-share deal. Countrywide became mired in credit woes last year and on several occasions has had to deny market rumours that it is bankrupt.

In its most important decision on **securities litigation** in more than a decade, America's Supreme Court ruled that investors who have been defrauded by a company could not sue third parties, such as banks and suppliers, unless they had relied directly on the parties' advice when making their investment. The court said that such lawsuits allowed "plaintiffs with weak claims to extort settlements from innocent companies." [See article](#)

**Oracle** agreed to pay \$8.5 billion for **BEA Systems**, almost \$2 billion more than when it first approached its rival in October. BEA accepted the offer after what it called a "diligent and thoughtful process". Carl Icahn, an activist shareholder with a 13% stake in BEA, had urged the company to sell.

Guy Hands warned **EMI's** recording artists that they should no longer expect huge album advances. Mr Hands's private-equity firm bought the music company last year. Despite falling market share, EMI has indulged its stars with rewards that many consider to be excessive in relation to the talent on display.

### Departure bored

Boeing confirmed that the maiden test flight and first delivery of its **787 Dreamliner** would be postponed by an additional three months, the second such setback for its new jet because of assembly problems. The test flight is now scheduled for sometime between April and June; the first delivery for early next year.

Meanwhile, **Airbus** said it had delivered 453 aircraft in 2007, 12 more than **Boeing**. However, the Americans took more net orders than the Europeans: 1,413 to 1,341.

After six successive quarters in profit, **American Airlines** made a small loss, of \$69m, which it put down to higher fuel costs.

The **European Commission** began two new antitrust investigations into **Microsoft** in response to complaints from its rivals, this time focusing on the compatibility of its Office package with other companies' software and the bundling of its Internet Explorer web browser with Windows.

The commission's antitrust regulator also opened an inquiry into **European drug companies** by raiding the premises of GlaxoSmithKline, AstraZeneca and others. The inquiry is focused on whether drug companies (no company has been charged with wrongdoing) have colluded to block generic and new

medicines from entering the market.

Investors flocked to subscribe to shares in India's **Reliance Power**. The public offering is expected to raise nearly \$3 billion, which will make it India's biggest when Reliance is floated on the stockmarket. [See article](#)

An agreement was reached in the row about how best to develop the giant **Kashagan oilfield**. Kazakhstan's state energy company will double its stake in the venture, while Italy's **Eni** will share the operation and development of the field with the venture's other shareholders—Royal Dutch Shell, Exxon Mobil and Total— when the oil starts flowing in 2011. The Eni-led project has been beset by delays and rising costs.

Investors continued to rally to precious metals amid uncertainty about the American economy. The price of **gold** breached \$900 a troy ounce for the first time and **platinum** reached another record.

## An expensive year

**Consumer prices** in America rose by 4.1% in December. Energy and food costs (up by 17.4% and 4.9% respectively) were to blame. Without those two volatile categories, “core” inflation was lower, at 2.4%. The Federal Reserve makes its next decision on interest rates at the end of the month.





## KAL's cartoon

Jan 17th 2008

From The Economist print edition

Illustration by Kevin Kallaugh



## Capital markets

## The invasion of the sovereign-wealth funds

Jan 17th 2008

From The Economist print edition

**The biggest worry about rich Arab and Asian states buying up Wall Street is the potential backlash**



BEN BERNANKE once spoke of dropping money from helicopters, if necessary, to save an economy in distress. The chairman of the Federal Reserve probably did not envisage that choppers bearing the insignia of oil-rich Gulf states and cash-rich Asian countries would hover over Wall Street. Yet just such a squadron has flown to the rescue of capitalism's finest.

On January 15th the governments of Singapore, Kuwait and South Korea provided much of a \$21 billion lifeline to Citigroup and Merrill Lynch, two banks that have lost fortunes in America's credit crisis. It was not the first time either had tapped the surplus savings of developing countries, known as sovereign-wealth funds, that have proliferated in recent years thanks to bumper oil prices and surging Asian exports. Since the subprime-mortgage fiasco unfolded last year, such funds have gambled almost \$69 billion on recapitalising the rich world's biggest investment banks (far more than usually goes the other way in an emerging-markets crisis). With as much as \$2.9 trillion to invest (see [article](#)), the funds' horizons go beyond finance to telecoms and technology companies, casino operators, even aerospace. But it is in banking where they have arrived most spectacularly. They have deftly played the role of saviour just when Western banks have been exposed as the Achilles heel of the global financial system.

### Moneymen or mischief-makers

At first sight this is proof that capitalism works. Money is flowing from countries with excess savings to those that need it. Rather than blowing their reserves on gargantuan schemes, Arab and Asian governments are investing it, relatively professionally. But there are still two sets of concerns. The first has to do with the shortcomings of sovereign-wealth funds. The second, bigger, problem is the backlash they will surely provoke from protectionists and nationalists. Already, Nicolas Sarkozy, the French president, has promised to protect innocent French managers from the "extremely aggressive" sovereign funds (even though none has shown much interest in his country).

Although sovereign-wealth funds hold a bare 2% of the assets traded throughout the world, they are growing fast, and are at least as big as the global hedge-fund industry. But, unlike hedge funds, sovereign-wealth funds are not necessarily driven by the pressures of profit and loss. With a few exceptions (like Norway's), most do not even bother to reveal what their goals are—let alone their investments.

For the bosses at the companies they invest in, that may be a godsend: how nice to be bailed out by a

discreet “long-termist” investor who lets you keep your job, rather than be forked out in the Augean clean-up hedge-fund types might demand. A quick glance back at “long-termist” nationalised industries shows what a mess that leads too. And it is not just a matter of efficiency. The motives of the sovereign money-men could be sinister: stifling competition; protecting national champions; engaging, even, in geopolitical troublemaking. Despite their disruptive market power, their managers have little accountability to regulators, shareholders or voters. Such conditions are almost bound to produce rogue traders.

So far there is no evidence of such “mischievous” behaviour, as the German government calls it (curiously, from another country yet to attract the sovereign-wealth crowd). And weighing the risk of such eventualities against the rewards of hard cash, on the table, right now, makes it clearly daft to raise too much of a stink. America is either in recession or near one; Mr Bernanke has all but promised more aggressive rate cuts, but confidence in the banking system is low. There is a wise old proverb about beggars and choosers.

The relatively friendly welcome sovereign funds have found in America may be temporary. Before the credit crunch American politicians objected to Arabs owning ports and Chinese owning oil firms. On January 15th Hillary Clinton said: “We need to have a lot more control over what they [sovereign-wealth funds] do and how they do it.” Once an emergency has passed, foreign money can often be less welcome. One of Singapore’s funds, Temasek, has learned that lesson to its cost in Indonesia.

In politics, appeals to fear usually sell better than those to reason. But the hypocrisy of erecting barriers to foreign investment while demanding open access to developing markets is self-evident. Host countries should not set up special regimes for sovereign wealth. Although every country has concerns about national security and financial stability, most already have safeguards for bank ownership and defence.

Until East and West even out the surpluses and deficits in their economies, sovereign-wealth funds will not go away. Ideally, the high-savings countries of the Middle East and Asia would liberalise their economies, allowing their own citizens to invest for themselves, rather than paying bureaucrats to do it for them. But do not expect miracles. In the meantime, what should be done to keep the rod of protectionism off their—and the world’s—backs?

## **Shed light or take heat**

For a start, more transparency would go a long way towards easing concerns: an annual report that discloses the fund’s motives and main holdings would be a start. Investments through third parties, such as hedge funds, help too, providing an additional layer of protection against the misdeeds of rogues. Ideally, the funds would eventually take fewer stakes in individual companies, which expose them to the inevitable risks of stockpicking and political pressure. Investing across indices provides more diversification anyway.

At a time when Western governments have at last learned to let the private sector run banks (however lousily it is sometimes done), it is far from ideal that state-owned funds from emerging economies should be buying stakes in them, even minority ones. On the other hand, such cross-border bargain-hunting gives developing countries a bigger direct stake in capitalism’s future. The chief danger will not lie with them. The problem is likely to be in the rich world—and a rising nervousness about foreign money.

## Democracy in retreat

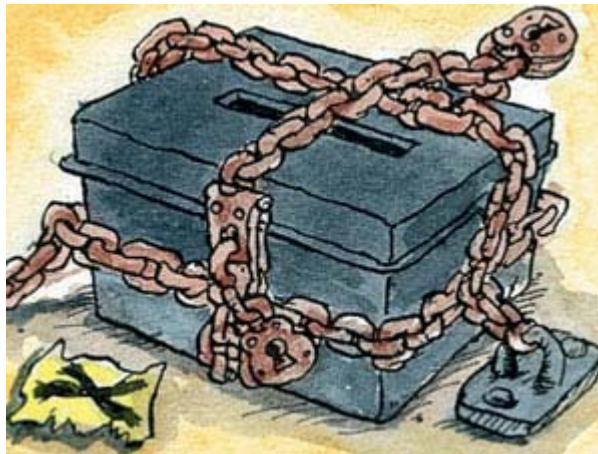
## Freedom marches backward

Jan 17th 2008

From The Economist print edition

## Why the setback is likely to be temporary

Illustration by David Simonds



YOU hardly need Freedom House in order to get the gist. Most people will already have noticed that these have not been the most inspiring of times for democracy and human rights. December brought the murder of Benazir Bhutto in Pakistan and what was almost certainly the stealing of an election in Kenya, one of Africa's relative successes, fast descending into a nightmare of tribal violence. And now comes confirmation from the American think-tank. Freedom House's closely watched annual review confirms that 2007 was the second year in a row during which freedom retreated in most of the world, reversing a democratic tide that had looked almost unstoppable during the 1990s following the collapse of communism and the break-up of the Soviet Union (see [article](#)).

Undeniably, the news is grim. But when democracy is the issue, it can be a mistake to extrapolate too much from the advances and retreats of a single year or two. Here, also prompted by recent events, are two brighter observations.

First, most people in most places still want democracy. This near-universal appetite is evident not only in what people say (even in conservative Muslim countries, where God-given *sharia* can be more popular than any law made by man, people tell opinion pollsters they want to elect their own governments). It is also reflected in what people do. Kenya's voters turned out in droves and queued for hours under a scorching sun. So in recent years, and at huge risk to life and limb, have voters in Afghanistan and Iraq.

All these countries, it is true, are now riven by political violence. But that does not prove that their voters cannot grasp the democratic idea, only that voters' choices can be uncongenial to the few who have power and are prepared neither to yield nor share it. Where the strong are willing to use violence to thwart the popular will, democratic movements can be stopped in their tracks, as in Myanmar, or provoked into a violent reaction of their own, as in Kenya. But the idea itself is harder to squash or suborn. In many newly democratic parts of the world, including most of Latin America, its roots are spreading wider and burrowing deeper.

Which leads to a second reason for optimism. There are many reasons why societies advancing fitfully towards democracy can suffer setbacks. Political transitions are disorderly. If the disorder becomes scary enough, as in Russia or Iraq, people may well come for a time to place less value on freedom and more on basic physical and economic security. But autocracies suffer setbacks too, and usually for one overwhelming reason. As Winston Churchill hinted in his aphorism, rulers who try to govern without democracy eventually discover that none of the alternative systems works as well.

## **After they've tried all the others**

Look no further than the current news. Miss Bhutto was back home campaigning for election because it had become evident to Pervez Musharraf and his American backers that military rule was failing to hold Pakistan together. In Thailand, the generals who pushed out the elected prime minister, Thaksin Shinawatra, in 2006, have found running the country harder than expected; if they are wise, they will heed the verdict of the people, delivered in December's election, that they want the former lot back. In January 2007 Bangladesh's army intervened to halt the alternation of power between two venal, incompetent but nonetheless elected political dynasties. But after a miserable year holding the ring, the generals would be glad of a way to give back the power they grabbed. Freedom House may well be right that democracy is on the back foot right now. In the longer run, its appeal is undiminished.

## Ethical capitalism

## How good should your business be?

Jan 17th 2008

From The Economist print edition

**Corporate social responsibility has great momentum. All the more reason to be aware of its limits**

Illustration by Ian Whadcock



HOW wonderful to think that you can make money and save the planet at the same time. "Doing well by doing good" has become a popular business mantra: the phrase conjures up a Panglossian best-of-all-possible-worlds, the idea that firms can be successful by acting in the broader interests of society as a whole even while they satisfy the narrow interests of shareholders. The noble sentiment will no doubt echo around the Swiss Alps next week as chief executives hobnob with political leaders at the World Economic Forum in Davos.

For these are high times for what is clunkingly called corporate social responsibility (CSR). No longer is it enough for annual reports to have a philanthropic paragraph about the charity committee; now companies put out long tracts full of claims about their fair trading and carbon neutralising. One huge push for CSR has come from climate change: "sustainability" is its most dynamic branch. Another has been the internet, which helps activists scrutinise corporate behaviour around the globe. But the biggest force is the presumption that a modern business needs to be, or at least appear to be, "good" to hang on to customers and recruit clever young people.

Thus for most managers the only real question about CSR is how to do it. Our [special report](#) this week looks at their uneven progress in that regard. But it is also worth repeating a more fundamental question this paper has asked before: is the CSR craze a good thing for business and for society as a whole?

Begin with business, where the picture is mixed. Much good corporate citizenship is a smug form of public relations. Public relations is part of business. A bad name has seldom been more expensive, especially when there is a war for talent and customers can look at your supply chain in Vietnam on YouTube. Public companies, remember, are creations of the state. In return for the privilege of limited liability, society has always demanded vaguely good behaviour from them. The cost of this implicit social franchise, whether shareholders like it or not, has risen. Companies as varied as Nike in clothing, GlaxoSmithKline in pharmaceuticals and Wal-Mart in retailing have had to change their ways quickly to avoid consumer or regulatory backlashes.

And it is not just a question of fending off disaster. CSR has got more focused: there are fewer opera houses, more productive partnerships with NGOs. Greenery, in particular, has paid off for some companies' shareholders. Toyota stole a march on other carmakers by appearing greener. European power companies which helped set up the continent's carbon-trading system did extremely well out of it.



Some people complain that this sort of “good corporate citizenship” is merely another form of self-interest. Correct—and good. They should be happy that this category has grown. The difficulties with CSR come when companies get it out of proportion. For instance, there is a lot of guff about responsibility being at the core of a firm's strategy. But even the business gurus who promote the idea admit that examples are scarce. And being a champion at responsibility does not guarantee great financial results, as recent setbacks at Starbucks and Marks & Spencer have shown.

An inconvenient truth for advocates of CSR is that the connection between good corporate behaviour and good financial performance is fuzzy at best. The latest academic research suggests that a positive link exists, but that it is a weak one. Of course, it's not clear which way the causality runs—whether profitable companies feel rich enough to splash out on CSR, or CSR brings profits. Either way, there is no evidence to suggest that CSR is destroying shareholder value, as Milton Friedman and others feared. But nor is it obviously the most productive way for managers to spend their energies. Caution is especially called for at a time when the CSR bandwagon is on a roll.

## **Caveat voter**

If companies need to be vigilant about the limits of CSR, the same applies even more to society as a whole. A dangerous myth is gaining ground: that unadorned capitalism fails to serve the public interest. Profits are not good, goes the logic of much CSR; hence the attraction of turning companies into instruments of social policy. In fact, the opposite is true. The main contribution of companies to society comes precisely from those profits (and the products, services, salaries and ideas that competitive capitalism creates). If the business of business stops being business, we all lose.

Most of the disasters have come from politicians seeking to offload public problems onto business: American health care is one sad example. But companies are increasingly keen on public policy. Take for instance, the vogue for “multi-stakeholder initiatives”—firms getting together with competitors, activists and others to set rules for a particular area of business (diamonds, project finance, extractive industries and so on). In some impoverished places such “soft law” helps to fill a void. But be wary: businesses do not always adhere to voluntary rules; they naturally want ones that help them make money. Above all, it is governments, not firms, that should arbitrate between interest groups for the public interest.

So the apparent triumph of CSR should prompt humility, not hubris. There is money to be made in doing good. But firms are not there to solve the world's political problems. It is the job of governments to govern; don't let them wiggle out of it.

## The militarisation of space

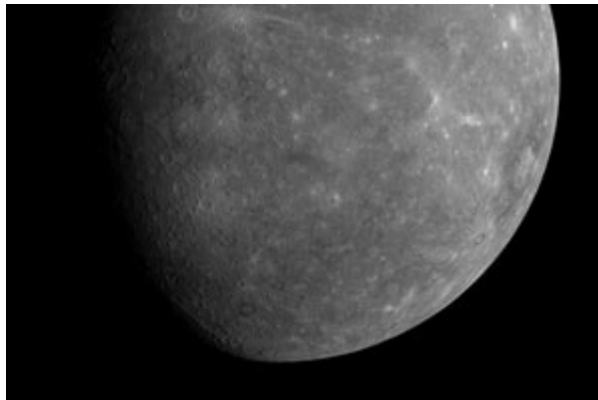
### Dangerous driving in the heavens

Jan 17th 2008

From The Economist print edition

#### The world needs a better code of conduct for spacefarers

Reuters



ON THE roads, at sea and in the air, mankind has invented sensible rules to avoid accidents. In space, something like a free-for-all prevails. On a good day, spacefaring nations observe certain understandings, such as how to launch objects safely into orbit. On a bad day, it is celestial road rage.

A year ago, the Americans fumed when China tested a missile by shooting up one of its own weather satellites. One thing that made the test look anti-social was that it created the worst-ever cloud of man-made debris in the heavens. Ever since, other satellites have had to be moved periodically to avoid the shrapnel. And bumping into things is not just a matter of collecting scratches. At orbital speeds, colliding with an object the size of a pebble can ruin the day of a multi-billion dollar spacecraft.

There was, however, a second reason for America's anger over the Chinese test. America is space's pre-eminent military power. Or, more exactly, given that America has held back from putting weapons in space, it has used space to preserve and extend the pre-eminent military power it enjoys on earth. By using a missile to blow apart one of their own satellites, the Chinese showed that they could if they chose blow apart the spy and navigation satellites on which America's armed forces (and grateful drivers everywhere using GPS systems) depend. Indeed, the Chinese test may have been intended to send precisely this warning.

Given the dangers of a clash in space, and the degree to which the military and civilian uses of space have blurred together (see [article](#)), why have the big powers so far failed to negotiate either arms-control agreements or simple rules of the road, as they have on earth? In the case of arms control, the explanation is that America is suspicious. Russia and China have offered to negotiate a treaty banning space weapons. The Americans are not sure whether that is feasible.

How, for example, do you define what is a weapon, since any flying object can be made into one simply by bashing it into someone else's satellite? Besides, the Americans fear that as top space power, with ambitious plans for anti-missile systems still in the pipeline, they would end up losing from any new treaty, while Russia and China would have to give up less. On January 23rd a conference on disarmament is due to reopen in Geneva, but on this point it is stuck. America says it is ready to talk in general about space security, but only if others agree to negotiate a treaty to stop production of fissile material for nuclear weapons. Thanks to the opposition of China and Pakistan, that may not happen any time soon.

America's reluctance to sign any arms-control agreement that might jeopardise its national security is understandable. But its refusal even to begin to talk about a weapons ban in space has been unduly rigid. Once negotiations started, some of its doubts about the possibility of a useful and verifiable treaty might

be dispelled. Besides, it is not at all clear that America itself would lose from the existence of such an agreement. Since the Americans have invested most in space, it is they who could suffer more if war or accident were to fill space with clouds of debris and kill or blind their satellites.

## **At least write a spaceway code**

In the meantime, the big spacefaring countries ought to consider negotiating some less formal rules of the road. These would seek to stop dangerous driving, maintain safe distances and, most importantly, avoid harm to each other's satellites. If they co-operated on surveillance of space, such countries could also do a much better job of monitoring space debris. America would still have the fanciest spacecraft, and could reserve its judgment on arms control. But in heaven as it is on earth, the more eyes on the road, the safer for all.

## Global warming

## Get the price right

Jan 17th 2008

From The Economist print edition

## What America can learn from Europe's attempts to cut carbon emissions

Illustration by Daniel Pudles



THE Scandinavians say they're already green; the eastern Europeans say they're too poor; the Belgians say they're too small; the French say they're too nuclear; and so on. As Europe negotiates the final details of its new plan to tackle climate change, which will be published on January 23rd, arguments are raging over how the burden should be distributed. Behind the row, though, something encouraging is going on. Europe has learnt from its experience of trying to constrain emissions, and is getting better at it. America should pay attention, and avoid Europe's early mistakes.

## Turning the screw

Europe's main tool for cutting carbon is its Emissions-Trading Scheme (ETS). Firms in the dirtiest industries in all the member states are issued with permits to emit carbon dioxide; if they want to pump out more, they have to buy more permits. The higher the price, the greater the incentive to cut emissions.

From the start, permits were given away free (as business wanted) instead of being auctioned (as economists wanted). As a result, in non-traded sectors (especially energy, the biggest polluter) firms have been passing on the cost of carbon to customers and making windfall profits. What's more, swathes of industry were left out of the scheme altogether. And many countries over-estimated their emissions, so too many permits were issued. As a result, the carbon price crashed and, ten years after the European Union signed the Kyoto protocol and five years after it ratified it, most European countries do not look like meeting their commitments.

On January 23rd the European Commission will in effect admit these mistakes. A sharply tighter ETS regime is likely to come into force. A lot of permits will be auctioned. Arguments over the proportion continue, but it could be more than half. The carbon price is likely to rise sharply as a result.

The commission has made some compromises in order to get everybody to buy in to this reform. Energy security is getting attention because of the East's fear of Russia. Bones are being thrown to Denmark's wind industry, Germany's solar industry and everybody's farm lobby through tough targets for renewables and biofuels. The result is a bit of a dog's dinner (see [article](#)). But the core of the plan—a reformed ETS, producing a higher carbon price—is likely to survive.

Some businesses are, understandably, concerned about the consequences for their competitiveness.

Energy-intensive companies maintain that a carbon price high enough to make a difference will push costs up and companies out. Emissions will not be cut: they will go abroad.

That is a serious consideration, particularly when other developed countries (especially America) are slow to adopt carbon constraints. Yet a study of British industry published this week by Britain's Carbon Trust undermines the idea that a carbon price of €20 (\$30) a tonne—high enough to make a range of clean-energy technologies worthwhile—would be a huge burden. It suggests that industries making up less than 1% of Britain's GDP (and 50% of its manufacturing emissions) would be “significantly” affected. Aluminium, cement and some steel production are the most vulnerable. The Carbon Trust reckons that the ETS can bring about deeper cutbacks in its next phase, after 2012, without damaging competitiveness.

Still, while Europe has a carbon price and the rest of the world does not, there is a cost. If the rest of the world follows where Europe leads, that temporary price will be worth paying. If it doesn't, it won't; and Europe will eventually give up trying to cut its emissions.

Fortunately, the planet has not yet reached that impasse. America seems likely, once it has a new president, to adopt emissions constraints. It has much to learn from Europe. Best of all, set a carbon tax, which is less susceptible to capture by business lobbies than is a cap-and-trade system. If you must adopt the latter, auction permits, otherwise emissions will continue to rise and polluters will profit instead of paying.

## On Pakistan, Belgians, Italy, cliff jumping, China, tribes, Mormons, Ivar Kreuger

Jan 17th 2008

From The Economist print edition

The Economist, 25 St James's Street, London SW1A 1HG

FAX: 020 7839 2968 E-MAIL: [letters@economist.com](mailto:letters@economist.com)

### Comparative politics

SIR – The title of your leader on Pakistan ("[The world's most dangerous place](#)", January 5th) confirms the old adage in journalism: when it bleeds it leads. Yes, Pakistan is going through trying times, but it is far from being the world's most dangerous country. Having just returned from Pakistan, which I traversed without let or hindrance with my Indian passport and Hindu name, I can say emphatically that its people are warm and friendly and passionate about democracy and the forthcoming elections.

Parts of my own country (and Nepal and Sri Lanka) are racked by Maoist guerrilla warfare and violent separatist-movements. I do not recall you designating India as the world's most dangerous place when Rajiv Gandhi was assassinated during electioneering, or Indira Gandhi for that matter. The latter's killing was followed by a brutal and murderous pogrom against Sikhs and Delhi burned for days. The truth always contains shades of grey.

Shreekant Gupta  
Visiting senior research fellow  
Institute of South Asian Studies  
Singapore

SIR – Your leader contained some good common sense. You mentioned two solutions that would enable democracy to take root here: a fair election and a credible inquiry into the murder of Benazir Bhutto. However, this regime will pursue neither as it has already destroyed most of our democratic institutions. The advice you gave was generous, but please note that America has given zero aid to Pakistan to strengthen its democracy.

Zubair Torwali  
Swat, Pakistan

### Statistical error

SIR – As a Belgian citizen I was astonished to read your claim that Adolphe Quetelet was a "French statistician" ("[Census sensitivity](#)", December 22nd). Quetelet was a Belgian mathematician and is considered to be among our country's brightest and most renowned personalities.

Ward Vloeberghs  
Louvain, Belgium

### Italy's finances

SIR – Your article on Italy's fiscal policy ("[Tax bonanza](#)", January 5th) missed two important facts. First, a large part of the new revenue raised has been used to bring about an extra reduction in the deficit, an absolute priority for Italy given its huge public debt. Second, progress in curbing current spending has been significant in the past two years thanks to the action of the present government. Current spending has been stabilised as a percentage of GDP (net of interest payments) and is now decreasing. This is partly because of improved economic growth, but is also explained by this government's control on spending. Indeed, compared with the same period in 2006, current expenditure decreased in absolute value during the first ten months of 2007.



Tommaso Padoa-Schioppa  
Minister of economy and finance  
Rome

## Extreme sports

SIR – I am guessing that those Norwegians who jump off cliffs for fun would not take such dire risks if they had to pay for hospital treatment ("[Human lemmings](#)", December 22nd). Thank goodness Norway offers free universal health care. If these daredevils had to pay for the cost of nine months in rehab after fracturing a leg they would be less cavalier with their well-being. It's all a matter of economics.

Bruce Sheiman  
New York

SIR – Your suggestion that we "toss a rock over the edge" the next time we are strolling on a cliff is the exact opposite of the usual advice given in mountainous areas. I shall now avoid walking below a cliff if there is another reader of *The Economist* around.

Nevis Hulme  
Gairloch, Ross

## The power of calligraphy

SIR – You outlined four management methods that Mao employed to rule China ("[Mao and the art of management](#)", December 22nd). When I studied Chinese in the late 1970s we always avoided the controversial issue of why simplified written characters had been introduced in China by Mao. The official reason was that it improved literacy among a diverse and widely uneducated population. However, it also obliterated any chance that the ancient texts so integral to Chinese culture, or anything else written before Mao's rise to power, could be read easily by a citizen.

So add one more key ingredient to those you listed for managers who want to gain and keep power: rewrite history by rendering the past inaccessible. As one of my classmates joked in 1979, "The optimists study Russian."

Stephanie Selice  
Wilmington, Delaware

SIR – Though clearly a stab at humour, your article on Mao's management style was a tad too unsettling for this Chinese, whose family endured Mao's brutality. What's next—tips on team-building from Hitler?

Yujiao Ma  
Toronto

## Tribal culture

SIR – The Sentinelese are not the only tribe of hunter-gatherers who still resist contact with the outside world ("[Noble or savage?](#)", December 22nd). There are over 100 uncontacted tribes worldwide, many of them hunter-gatherers. Nor are the Sentinelese warlike. They defend their tiny island with good reason—intruders have shot and killed Sentinelese, and neighbouring tribes have been wiped out after contact with outsiders.

Far from being "in a state of almost constant tribal warfare", most contemporary hunter-gatherers are struggling to defend their land from the governments, companies or settlers who want them off it.

Stephen Corry  
Director  
Survival International  
London

## Revealed truths

SIR – No religion can really stand up to historical scrutiny. Your cursory treatment of Mormon theology (“From polygamy to propriety”, December 22nd) was marked by incredulity, but failed to note that many mainstream Christian beliefs also require leaps of faith. Mormons believe that God directed Joseph Smith to “thin metal plates”, whereas Christians claim that God dictated commandments to an elderly Israelite on a mountaintop. Which incident requires the greater leap of faith?

Hosea Martin  
Chicago

## **Business ethics**

SIR – It is a great pity that Ivar Kreuger, “the world's greatest swindler”, lived before his time (“The match king”, December 22nd). “The patron saint of sinners” conned businessmen in the early 20th century. If he were alive today governments would have rushed in to use taxpayers' money to bail him out. He would have received a golden parachute worth millions of dollars. With the royalties from his autobiography, plus carefully chosen lecture assignments, he would have lived out his retirement in luxury. Instead Kreuger committed suicide. How times, and values, have changed.

J. Rengarajan  
Chennai, India

## The militarisation of space

### Disharmony in the spheres

Jan 17th 2008 | COMBINED AIR OPERATIONS CENTRE  
From The Economist print edition

**Modern American warfare relies on satellites. They make America powerful but also vulnerable, particularly in light of China's new celestial assertiveness**

Illustration by Andy Baker



A HUSHED, dimmed hall in the nerve centre that controls America's air operations from Somalia to Afghanistan is dominated by giant video screens tracking coalition aircraft. Blue dots show the location of ground forces, with "troops in contact" highlighted for priority air support. Smaller screens show live black-and-white footage, relayed by satellite from unmanned drones which, in their turn, are remotely controlled by pilots in America.

The Combined Air Operations Centre's exact location in "southwest Asia" cannot be disclosed. But from here commanders supervise tens of thousands of sorties a year. Through aircraft surveillance pods they get a god's eye view of operations that range from old-fashioned strafing to the targeted killing of insurgent leaders with bombs guided by global positioning system (GPS) satellites, and emergency air drops to isolated soldiers using parachutes that steer themselves automatically to the chosen spot.

These days America fights not in a fog of war but, as one senior air force officer puts it, in a "huge cloud of electrons". Large amounts of information, particularly surveillance videos, can be beamed to soldiers on the ground or leaders in America. The officer says this kind of "network-centric" warfare is "as revolutionary as when the air force went from open cockpits to jet aeroplanes."

If Napoleon's armies marched on their stomachs, American ones march on bandwidth. Smaller Western allies struggle to keep up. Much of this electronic data is transmitted by satellites, most of them unprotected commercial systems. The revolution in military technology is, at heart, a revolution in the use of space. America's supremacy in the air is made possible by its mastery of space.

During the cold war space was largely thought of as part of the rarefied but terrifying domain of nuclear warfare. Satellites were used principally to monitor nuclear-missile facilities, provide early warning should they be fired and maintain secure communications between commanders and nuclear-strike forces. Now, by contrast, the use of space assets is ubiquitous; even the lowliest platoon makes use of satellites, if only to know its position.

Space wizardry has made possible unprecedented accuracy. As recently as the Vietnam war, destroying a bridge or building could take dozens if not hundreds of bombing runs. These days a plane with "smart" bombs can blast several targets in a single sortie, day or night, in good weather or bad. Needless to say, precise intelligence and sound judgment are as important to military success as fancy kit.

But might this growing reliance on space and cyberspace become a dangerous dependence, a fatal weakness? Air force officers talk of space being America's Achilles heel. Satellites move in predictable orbits and anybody who can reach space can in theory destroy a satellite, even if only by releasing a cloud of "dumb" pellets in its path—using a shotgun rather than a hunter's rifle to kill the orbiting "bird".

The Taliban or al-Qaeda can do little about America's space power except hide themselves from its intelligence-gathering satellites. But the Pentagon worries about what would happen if America came up against a major power, a "near-peer" rival (as it calls China and Russia), able to intercept space assets with missiles and "space mines", or to disable them with lasers and electronic jammers. "There are a lot of vulnerabilities," admits an American general, "There are backups, but our space architecture is very fragile."

The precise nature of these weaknesses is a well-guarded secret. But wargames simulating a future conflict over Taiwan often end up with the "Red Force" (China) either defeating the "Blue Force" (America) or inflicting grievous losses on it by launching an early attack in space, perhaps by setting off one or more nuclear explosions above the atmosphere. "I have played Red and had a wonderful time," says the general, "It is pretty easy to disrupt Blue. We should not expect an enemy to play by established norms in space. They will play dirty pool."

One shot China has been practising became clear a year ago, on January 11th 2007. In a nuclear-proof air force command centre, built on giant shock-absorbing springs within Cheyenne Mountain, outside Colorado Springs, officers tracked a missile fired from a mobile launcher deep inside China. It followed what one American official said was a "strange" trajectory, designed neither to land a warhead nor to put a payload into orbit. Instead it intercepted one of China's ageing weather satellites. The impact about 850km (530 miles) above Earth created a huge field of space debris, contributing about 28% of the junk now floating around in space (see chart).

## Litter louts do their worst

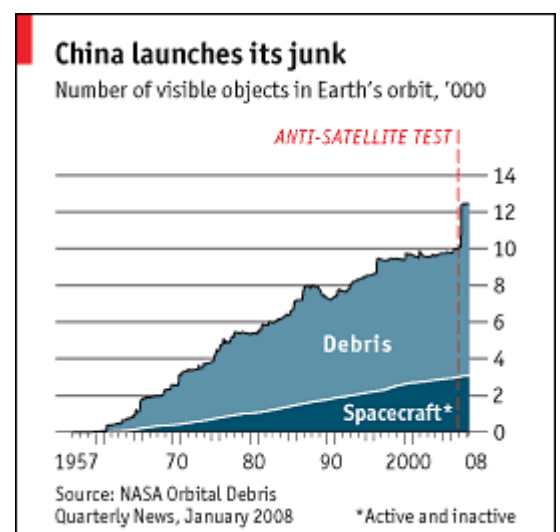
Creating all this rubbish seems a bit irresponsible for a country seeking to be a great space-faring nation. It is true that both America and Russia carried out scores of similar anti-satellite (ASAT) tests during the cold war. Then they stopped, not least because the celestial shrapnel was endangering their hugely expensive satellites. They also accepted that spy satellites provided a degree of mutual reassurance in nuclear arms control. The last piece of American ASAT debris fell back to Earth in 2006, say Pentagon officials. China's shrapnel, created in a higher orbit, could be around for a century to come.

The missile shot put America on notice that it can be challenged in space. The Chinese routinely turn powerful lasers skywards, demonstrating their potential to dazzle or permanently blind spy satellites. "They let us see their lasers. It is as if they are trying to intimidate us," says Gary Payton, a senior Pentagon official dealing with space programmes. The only conclusion, he argues, is that "space is no longer a sanctuary; it is a contested domain."

In a report to Congress in November, a commission examining America's relations with China gave warning that "the pace and success of China's military modernisation continue to exceed US government estimates." China's principal aim, the report said, is to develop the wherewithal to delay or deter American military intervention in any war over Taiwan.

The ASAT test intensifies the concern of those who already find plenty to worry about in Chinese military literature. A study for the American Enterprise Institute, a think-tank, cites a Chinese theorist who argues that China should adopt a policy of overt deterrence in space. Other Chinese argue that their country's territorial sovereignty extends to space. This kind of thing reinforces the hawkishness of American hardliners.

Ashley Tellis, a senior associate at the Carnegie Endowment, another think-tank, believes China ultimately seeks to build a "Sinocentric order in Asia and perhaps globally." Any attempt to negotiate arms-control agreements in space would be futile, he argues, and America "has no choice but to run the offence-defence space race, and win."

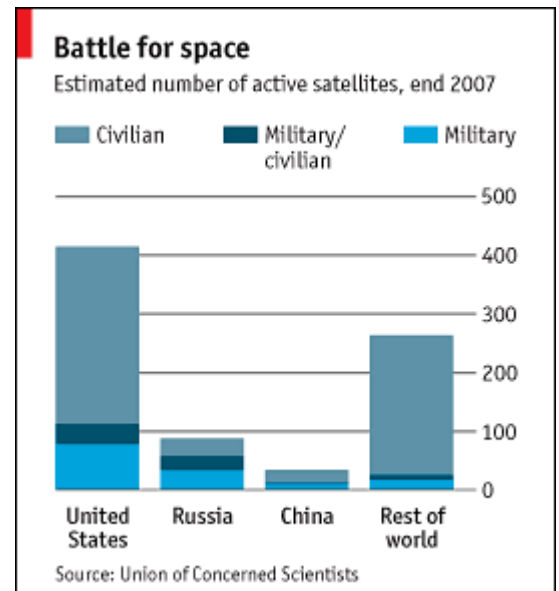


Other experts, such as Michael Krepon, co-founder of the Henry L. Stimson Centre, a security think-tank, play down the Chinese peril. Mr Krepon says that though similarly alarming conclusions could have been drawn from American or Soviet military literature in the cold war, a space war never took place. What is more, the greater China's economic reliance on satellites, the keener it will be to protect them.

Even those who doubt that America would really go to war against China for the sake of Taiwan worry about the dangers posed by the growing number of countries that have access to outer space. Ten countries (or groups of countries) and two commercial consortia can launch satellites into orbit. A further 18 have ballistic missiles powerful enough to cross space briefly. By the end of 2006, 47 countries and other groups had placed satellites in orbit, either on their own or with help from others. In its crudest form, any object can become a space weapon if directed into the path of a satellite.

In testimony to Congress last year, General James Cartwright, a former head of America's Strategic Command, said that "intentional interference" with all types of satellites, "while not routine, now occurs with some regularity". GPS signals are relatively weak and easy to jam. For several months in 2006 electronic jammers in Libya interfered with the Thuraya satellite telephone system, apparently because the Libyan government wanted to make life difficult for smugglers in the Sahara desert.

Satellites are not just military tools; they have also become a vital part of globalised civilian life. It is hard to disentangle military from civilian uses of space. Military GPS satellites support a myriad of civilian uses, including road directions for taxi drivers, navigation for commercial airliners, tracking goods in transit and time signals for cash dispensers. But the armed services' hunger for electronic data means that four-fifths of America's military data is transmitted through commercial satellites. A single Global Hawk unmanned surveillance aircraft flying over Afghanistan can eat up several times more satellite bandwidth than was used for the whole of the 1991 war against Iraq.



## Star wars delayed

Space provides the high ground from which to watch, listen and direct military forces. But the idea that countries would fight it out in space has so far been confined to science fiction. International law treats outer space as a global common, akin to the high seas. Countries are free to use space for "peaceful purposes" but may not stake territorial claims to celestial bodies or place nuclear weapons in space. "Peaceful" has been interpreted to mean "non-aggressive" rather than non-military. Space is highly militarised but for the moment nobody has placed weapons there, not openly at least.

During the cold war, under Ronald Reagan's presidency, America worked on plans for space-based weapons designed to shoot down ballistic missiles. But this "star wars" programme faded with the collapse of Soviet communism. Before being appointed defence secretary in 2001, Donald Rumsfeld chaired a special commission to review America's space policy. It issued a stark warning that America could suffer a crippling surprise attack on its space systems—a "space Pearl Harbour"—and argued that America "must develop the means both to deter and to defend against hostile acts in and from space."

America then broke out of the Anti-Ballistic Missile Treaty, freeing itself to pursue a slimmed-down version of missile defence. The latest official statement on America's space policy, issued in 2006, affirms the country's freedom of action in space, the right of self-defence and the right to "deny, if necessary, its adversaries the use of space." At the UN General Assembly, America has stood alone in voting against a resolution supporting negotiations on a treaty to prevent a space arms race, an idea pushed by China and Russia.

Yet the Bush administration has stopped short of taking the fateful step of "weaponisation" in space. Perhaps it is too preoccupied with Iraq, and certainly the downfall of Mr Rumsfeld removed a powerful champion of space weapons. A year after China's ASAT shot, the defence budget passed by the Democrat-controlled Congress did not provide any money for a missile defence "space test-bed".

One of the big disincentives to placing weapons in space has been the technical difficulty and cost of such an enterprise. A recent study by the Centre for Strategic and Budgetary Assessments (CSBA), a defence think-tank, concluded that ground-based systems were almost always more cost effective and reliable than space-based weapons, whether used to attack missiles, enemy satellites or targets on land.

America is still hedging its bets. With some tweaking, say experts, the ground-based interceptors for shooting down ballistic missiles could be used against satellites. A host of technologies under research, such as high-powered lasers to destroy missiles rising through the air, could be applied to anti-satellite warfare.

## **A game of celestial dodgems**

The core fear is that any conflict in space would cause the most injury to America since America has the most to lose. Damaged planes crash to the ground and destroyed ships sink to the bottom of the sea. But the weightlessness of space means that debris keeps spinning around the Earth for years, if not centuries. Each destruction of a satellite creates, in effect, thousands of missiles zipping round randomly; each subsequent impact provides yet more high-speed debris. At some point, given enough litter, there would be a chain reaction of impacts that would render parts of low-Earth orbit—the location of about half the active satellites—unusable.

As matters stand, ground controllers periodically have to shift the position of satellites to avoid other objects. This month, NASA was tracking about 3,100 active and inactive satellites, and some 9,300 bits of junk larger than 5cm, about 2,600 of them from the Chinese ASAT test. Given their speed, even particles as small as 1cm (of which there may be hundreds of thousands) are enough to cripple a satellite.

For America, then, avoiding a space war may be a matter of self-preservation. The air force has adopted a doctrine of “counterspace operations” that envisages either destroying enemy satellites in a future war or temporarily disabling them. But for the most part, America's space security relies on passive measures: sidestepping an attacker by moving out of the way of possible strikes; protecting the vital organs of satellites by “hardening” them against laser or electromagnetic attack; replacing any damaged satellites; or finding alternative means to do the job, for example with blips or unmanned aircraft.

More esoteric space research has ideas such as sending small satellites to act as “guardian angels”, detecting possible attacks against the big birds. It also includes plans for breaking up satellites into smaller components that communicate wirelessly, or deploying “space tugs” that would repair and refuel existing satellites.

Few of these options are cost-free. More manoeuvrable satellites are heavier, as they have to carry more fuel; protective equipment makes satellites cumbersome and more expensive; placing a satellite farther away from Earth, where it is more difficult to attack, means it will broadcast a weaker signal or require more costly sensors and antennae. The promise of cheap, reuseable launch vehicles has yet to materialise. All this makes it hard for America to achieve its goal of “operationally responsive space”: the ability to place satellites in orbit quickly and inexpensively.

The essential prerequisite for better space security is to improve “situational awareness”: that is, to know what is in space, who it belongs to and whether it is acting in a threatening manner. America already has the world's most developed space monitoring system with a network of radars and telescopes. But its surveillance is patchy. Objects in orbit are catalogued periodically rather than tracked continuously. Space surveillance is not really like air-traffic control: it is more akin to trying to track ships at sea with the naked eye, watching them leave port and predicting when they will next come in sight of land. There are gaps in coverage, particularly over the southern hemisphere, and much of the antiquated surveillance system cannot fuse the data to create an overall picture.

Space surveillance would seem to be ideally suited to international co-operation. Yet the Americans, Chinese, Russians and Europeans all seem intent on doing their own monitoring. They are frightened of giving away their space secrets to rivals. Accurate and timely information on space objects is vital for defending a satellite, but also necessary for attacking one.

## **Coming back down to Earth**



Many strategists argue that the most vulnerable parts of the American space system are closer to home. Ground stations and control centres, particularly those of commercial operations, are exposed to conventional bombing, whether by armies or terrorists. Communication links to and from satellites are open to interference. In cyber-warfare, critical parts of the space system could be attacked from distant computers. Even without external meddling, notes Tom Ehrhard, a senior fellow at the CSBA, American forces struggle to find enough bandwidth and to prevent the myriad of electronic systems from jamming each other.

Some remedial action is being taken. Backup ground stations are being set up in case the main GPS control centre outside Colorado Springs is disabled. New satellites will have a more powerful GPS signal that is harder to block. America is experimenting with satellite-to-satellite communication by laser, which can carry more data and is less prone to interference than radio waves.

And the armed forces are starting to train for warfare with few or no data links. Simulated attacks by both space and cyberspace "aggressors" are being incorporated into events such as the regular "Red Flag" air-combat exercises over the Nevada desert. But, said an officer at one recent wargame, there are other ways of doing things. "If you really want to take us down, why go to space? You could just try to take out the control tower or bring down the electricity supply to the base."

## Michigan's Republican primary

## All must have prizes

Jan 17th 2008 | DETROIT  
From The Economist print edition

**After Mitt Romney's victory, no one has the slightest idea who will win the Republican presidential nomination**

"I'VE got Michigan in my DNA. I've got it in my heart and I've got cars in my bloodstream." That was Mitt Romney before he won the Republican primary in Michigan this week, thumping John McCain by 39% to 30% and leaving Mike Huckabee flat in the snow with 16%. Presumably he now likes the place even more.

His rivals instantly discounted his victory. Mr Romney grew up in Michigan. His father, George Romney, was a popular governor in the 1960s. The day before the primary, Mr Romney showed a friendly crowd at a country club some souvenirs of his dad's unsuccessful bid for the White House. There was a campaign comb (cue for a quip about the family hair), some campaign pins and a slogan: "Set our country straight: Romney in 68". The crowd loved it. But voters in South Carolina will be harder to sway.

That said, Mr Romney ran a smarter campaign in Michigan than in Iowa and New Hampshire, where he aimed lots of negative ads at Mr Huckabee and Mr McCain but lost. In Michigan, his message was more upbeat. He talked a lot about the economy, and sold himself as the candidate best qualified to fix it. Mr McCain, who won Michigan in 2000, helped him by sounding gloomier. He said, probably correctly, that some of the jobs Michigan has lost will never come back.

Exit polls showed that voters cared more about the economy than anything else. Small wonder: Michigan has stalled. Its car firms are ailing; its people are leaving. Unemployment, at 7.4%, is the highest in America. Voters judged Mr Romney most capable of easing their pain. A successful venture capitalist before he was governor of Massachusetts, he palpably knows more about money than his rivals.

The candidates all pandered to Michigan's biggest special interest. At the Detroit motor show they all followed the same routine: the nod (as a car-company executive described the latest model), the 'ah' (of admiration) and the fiddle (with various gadgets in the car). Naturally, they shunned foreign vehicles like a handshake with Osama bin Laden.

Mr McCain pandered the least. On the stump, he banged on about climate change. (His home state of Arizona is so dry, he said, the trees chase the dogs.) Mr Huckabee pandered the most empathetically, staring into insecure workers' eyes and announcing that "there's a world of hurt out there in America." Mr Romney pandered with the most facts at his fingertips, helped by the fact that his dad was a car-firm boss before he was a politician.

In his first 100 days in office, Mr Romney said he would bring together car firms, unions and government and make a plan to revive the industry. He would reduce taxes, trim regulations, make health insurance (a huge chunk of the cost of an American car) cheaper and curb frivolous lawsuits. He would also slow the tightening of fuel-economy standards. "Take off those burdens and let's show them how fast a Mustang will actually go," he said.

Mr Romney has come first or second in all the votes so far. His people tout him as the most acceptable candidate to the broadest range of Republicans. Fiscal conservatives like him. Evangelicals may not love him as they do Mr Huckabee, a Baptist preacher, but they concur with his current positions on abortion and gay marriage. He lacks Mr McCain's national-security credentials, but says he will keep the armed forces strong. Add brains and good looks, and you have a plausible nominee, though his Mormonism and his policy shifts are problems for many.

Mr Romney's detractors offer several rebuttals. John McCain's fans note that in head-to-head polls against Hillary Clinton and Barack Obama, their man is the only Republican who wins. But a lot could change before November, and the qualities that attract independent voters to Mr McCain, such as his liberal views on immigration, repel many Republicans.

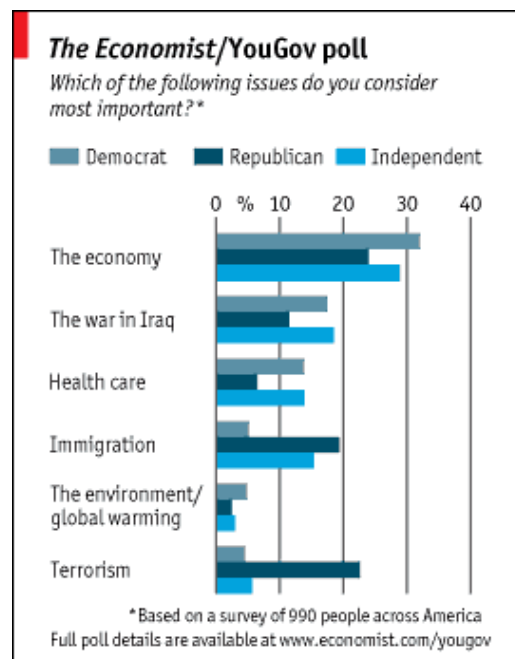
Mr Huckabee's fans reckon that Mr Romney will lose because his money can't buy him charisma. And it is indeed hard to imagine him strumming a guitar, cracking jokes about the Rolling Stones or getting in a snowball fight outside a polling booth, as Mr Huckabee did in Michigan.

Mr Romney did well in nearly every Republican group in Michigan—he even beat Mr Huckabee among evangelicals. But he has yet to prove himself on unfamiliar terrain. And he cannot win nationally unless he attracts more support from less prosperous people. Shortly before he addressed that friendly country club, someone announced that three cars were parked inappropriately outside: a silver Mercedes, a red Jaguar and a gold one.

Three lessons can be drawn from Michigan. One is that the race for the Republican nomination is even more open than before. Three frenzied contests have thrown up three winners. (Mr Romney also won Wyoming, a race his rivals skipped.) South Carolina on January 19th will be a bare-knuckle scrap. Rudy Giuliani, a former mayor of New York, will join the mêlée on January 29th in Florida. No one has the slightest idea who will win.

The second lesson is that if America tips into recession, the sirens of populism will warble louder. A conventional economic conservative won this week, but only by echoing some populist refrains. Both Mr Romney and Mr McCain are free-traders, but both suggest on the stump that some types of trade are unfair. And nearly all candidates in both parties hint that switching to alternative fuels will cut off funds for Islamic terrorism, by reducing the price of oil. This is bunk. Only an imperceptible portion of petrodollars bankroll terrorism, which is anyway quite cheap. Al-Qaeda coped just fine when oil was \$10 a barrel.

The third lesson is that although political junkies have been obsessed with the campaign for more than a year, many Americans have barely begun to think about it. Turnout in Michigan was low. Standing behind floor-to-ceiling bulletproof glass, the manager of a liquor store in downtown Detroit said he did not realise there was an election going on. "You're from a newspaper?" he asked. "You want to sell it in my store?"



## The Democrats in Michigan

### Vote early at your peril

Jan 17th 2008 | ANN ARBOR  
From The Economist print edition

#### The risky business of defying the Democratic National Committee

FOR years Michigan's Democrats have said that the primary system gives Iowa and New Hampshire unfair attention. So last autumn the state's Democrats and equally miffed Republicans moved their contests right up into January. Michigan became a political hot spot, with candidates swooning at Detroit's latest cars and promising to revive the state's economy. At least, that's what the Republicans did. No Democrat turned up, except for Dennis Kucinich.

The Democratic National Committee (DNC) angrily stripped Michigan and Florida, the other big state to defy the party and move its contest forward, of their delegates to the party convention in August, when the candidate will be nominated. (The Republican Party's gentler punishment was to cut the number of delegates in half.) Mark Brewer, Michigan's Democratic chairman, says the DNC will let his delegates attend the convention, but that remains to be seen.

The result of all this, complained a writer for the *Detroit Free Press*, was a primary comparable to "NASCAR on bicycles, Halloween with no costumes and Miss America without swimsuits" (the last event might not be as dull as he meant). Hillary Clinton won 55% of the vote; hardly a victory, since her only rivals on the ballot were Chris Dodd (who withdrew from the race weeks ago), Mike Gravel (who?) and Mr Kucinich (the candidate who just won't go away).

A remarkable 40% voted "uncommitted" in support of Barack Obama and John Edwards, who took their names off Michigan's ballot in deference to the official schedule. Their supporters hope the "uncommitted" vote will earn them delegates who could support their candidate at the convention—assuming any delegates from Michigan are allowed.

Many local Democrats are angry with both the state and the national party. "People are so disappointed and discouraged," explained Christina Montague, leader of Michiganders for Obama. One of Mr Edwards's supporters has sued the state party, unsuccessfully, for disenfranchisement.

Michigan's Democratic leaders are supporting their decision to go early. Carl Levin, Michigan's senior senator, hopes to inspire other states to demand that the DNC change its "cockamamie" system. (He has a bill that would do just that.) Mr Brewer insists that the early primary is "short-term pain for long-term reform". Pain, yes. The reform is less certain.

Still, the DNC has not yet won this skirmish. If the attempt to strong-arm the states alienates the Democratic base in Michigan or Florida, the party may be the real loser in November.

## Sex, race and Democrats

## Outrage all round

Jan 17th 2008 | WASHINGTON, DC  
From The Economist print edition



Fraternal greetings

## The Democrats are convulsed by emotive arguments

IN A high-minded moment in the Democratic debate in Las Vegas on January 15th Hillary Clinton declared that "what's most important is that Senator Obama and I agree completely that, you know, neither race nor gender should be a part of this campaign." Meanwhile, back in the real world, their respective camps were arguing about nothing else.

Many blacks have taken objection to a couple of remarks that the Clintons made during the New Hampshire primary. Mrs Clinton averred that "Dr King's dream began to be realised when President Lyndon Johnson passed the Civil Rights Act of 1964". Bill Clinton—the two are joined hip and thigh during this campaign—accused Mr Obama of purveying a "fairy tale".

The Clintons have reacted furiously to the charge of racial insensitivity—and their team has busily accused the Obama camp of twisting their words for partisan advantage. They have a point. Mr Clinton was referring to Mr Obama's opposition to the Iraq war. Mrs Clinton was emphasising the importance of experience in bringing about solid legislative change (though one wonders what sort of experienced Democratic politician speaks anything but reverently of Dr King). The Obama camp's hypersensitivity to presumed racial slights undercuts their champion's claim to be running as a post-racial politician.

Still, Mr Obama's lieutenants were not the only people to take offence. Donna Brazile, Al Gore's former campaign manager and a neutral in this race, thought that they crossed the line, as did James Clyburn, an extremely influential South Carolina congressman. And black radio stations have been talking about nothing else.

Mr Clinton's excuses were drowned in the noise created by Robert Johnson, a black mogul who founded Black Entertainment Television. Introducing Mrs Clinton in South Carolina, Mr Johnson claimed that the Clintons "have been deeply and emotionally involved with black issues since Barack Obama was doing something in the neighbourhood—and I won't say what he was doing but he said it in his book." Mr Johnson's preposterous claim that he was talking about Mr Obama's community activism rather than his cocaine use has persuaded nobody.

The debate is not likely to die down—despite the candidates' protestations about taking gender and race off the table. The South Carolina primary looms on January 26th—the first primary in the South and the first that has not been played out before an overwhelmingly white electorate. Blacks make up half of the Democratic electorate in the state, and are leaning heavily towards Mr Obama. A Rasmussen poll found

the two candidates neck and neck a month ago. This week Rasmussen found Mr Obama leading by 38 points to 33. Mr Obama leads by 53 to 30 among blacks but loses by 21 to 40 among whites.

The row also reflects deep cleavages along race and gender lines among Democratic voters nationally. Rasmussen shows Mr Obama beating Mrs Clinton by 66% to 16% among blacks but trailing her 27% to 41% among whites. Gallup shows Mrs Clinton leading Mr Obama by 49 points to 19 points among females who are older than 50 and by 42 points to 28 points among women aged 18 to 49.

Mrs Clinton is banking on her edge among women. Her tearful moment in a New Hampshire diner, which is widely credited with reviving her floundering campaign, went down particularly well with older women. She repeatedly emphasises her hard work on behalf of her gender. In a remarkable exercise in doublethink she claimed on one of the Sunday talk shows that "you have a woman running to break the highest and hardest glass ceiling. I don't think either of us wants to inject race or gender in this campaign. We're running as individuals".

The other reason why the debate will continue is that the Clintons' main aim at the moment is to drive up Mr Obama's "negatives". They desperately need to reverse polls that show that, despite his failure in New Hampshire, Mr Obama is picking up support in a large swathe of demographic groups.

This will involve attacking his political record and picking apart his personal biography (it is striking that two Clinton supporters have already brought up Mr Obama's admitted cocaine use). None of this is likely to go down well with Americans who regard Mr Obama as one of the most talented politicians of his generation, and who hope that he will become America's first black president.



## On the campaign trail

### Primary colour

Jan 17th 2008

From The Economist print edition

#### The Mayor doth protest too much

"Miss, no matter how many times you ask the question, I'm not a candidate. That's the answer. I can't go into nitpicking. This is ridiculous."

*Michael Bloomberg, Mayor of New York, gets snappy with reporters. [CNN.com](#), January 14th*



#### Civil union

"Hillary, marry me, baby."

*Senator Hillary Clinton has some very enthusiastic supporters in Los Angeles. [CNN.com](#), January 11th*

#### Street cred

"I had an old, beat-up car, had a little, tiny beat-up apartment. I was wearing raggedy, beat-up clothes. I got holes in the shoes, had holes in my car. You all've been there. You know what I'm talking about."

*Barack Obama talks up his working class credentials, discussing his years as a community organiser in Chicago, January 11th*

#### Only human

"Sweat a bit."

*Jack Welch advises Mitt Romney on how to make himself less perfect. [MSNBC](#), January 14th*

#### Take a break

"He took one day off, then got right back to work being the governor of New Mexico. He's a glutton for punishment."

*Tom Reynolds, campaign spokesman for Bill Richardson who dropped out of the presidential race on January 10th. [Washington Post](#), January 14th*

#### Play hard

"Get rough, Fred, get rough."

*A South Carolinian voter who would like to see Fred Thompson more engaged. [Washington Times](#), January 14th*

#### Lucky charms

"Some of our superstitions are a day old, some are many years old."

*John McCain, hoping to win in Michigan, carried a lucky penny and was wearing the same sweater he wore when he won in New Hampshire. [ABCNews.com](#), January 15th*

#### Scary monsters

"He's not the happiest boy today. I think he must be a Romney voter. Look at him. He's so sad."

*Mike Huckabee tries to comfort a crying toddler in Michigan. [Associated Press](#), January 15th*



## The economy

## Stampede to stimulus

Jan 17th 2008 | WASHINGTON, DC  
From The Economist print edition

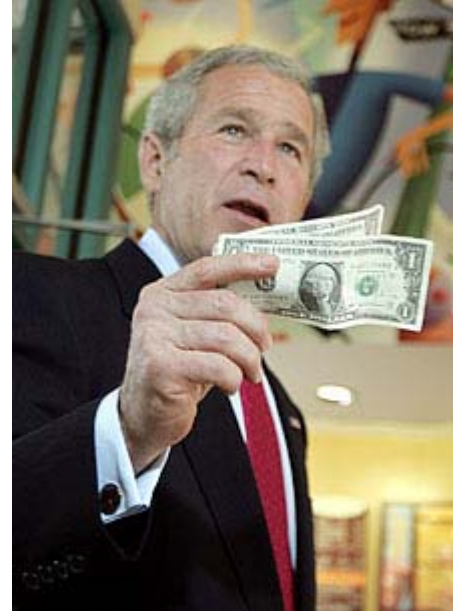
**Politicians want to give the economy a boost. They're likely to make a hash of it**

AP

JUST occasionally, Washington's creaky political machine can whirl into rapid action. Something of the sort is happening in the debate about fiscal stimulus. A month ago, a few academics were calling on Congress to spur the weakening economy with tax cuts or higher spending. Now, after a run of statistics suggest the economy has stalled, politicians of all stripes have jumped on the bandwagon.

The White House wants to announce a stimulus package in George Bush's state-of-the-union address of January 28th. Nancy Pelosi, the speaker of the House of Representatives, wants the details hashed out before then. With neither party keen to face voters in the midst of a recession, legislation now seems quite possible. Less obvious is whether it will make any sense.

Most economists agree on the characteristics of sensible fiscal stimulus: the measures should conform to three "T"s: timely, well-targeted and temporary. Take too long, and the recession could be over before stimulus is agreed. Target the money on people most likely to spend it and you get the most demand-boosting bang for the buck. Don't let the measures permanently worsen the government's budget position. Consensus is even emerging on the appropriate size of any boost: somewhere around \$100 billion, a bit less than 1% of GDP. That could provide the economy with a significant short-term jolt. Calculations by Douglas Elmendorf of the Brookings Institution suggest that a temporary tax rebate worth \$100 billion could boost the annualised rate of GDP growth by between 0.8 and 3 percentage points in the quarter in which it was enacted.



**Mr Bush has a plan**

Unfortunately, even the wonks do not agree on what measures best fit these criteria. At a Brookings Institution forum on January 10th, Martin Feldstein, a Harvard professor and leading Republican economist, argued for an income tax rebate and opposed extending unemployment insurance. Mark Zandi, head of [Moody's Economy.com](#), favoured more help for the jobless and a payroll tax holiday. Think-tanks have piled in too. The Economic Policy Institute wants job-generating infrastructure improvements. The Centre on Budget and Policy Priorities wants more help for struggling state governments.

So far, the only politicians to weigh in with detailed plans are people who cannot enact them this year: presidential candidates. Some are reasonably sensible. Barack Obama, for instance, wants everyone to get a \$250 tax cut, which would double if economic indicators continue to worsen. Others look more like a fiscal Christmas tree. Hillary Clinton wants a \$70 billion package: \$30 billion in housing assistance, \$25 billion in home-energy subsidies, \$10 billion on expanding payments to the unemployed and \$5 billion for environmental projects. The Republican presidential candidates want to make Mr Bush's tax cuts permanent—an odd priority just now since they don't expire until 2010.

Early indications suggest that both the White House and congressional leaders are eschewing such a fiscal free-for-all. The speculation is that Mr Bush will push for tax breaks for businesses and a tax rebate for individuals, but will not insist on extending his tax cuts. Top Democrats in Congress are also keen on a tax rebate, but they want to make sure it helps poorer consumers, perhaps by making it refundable for those who do not pay income tax. They also want more government spending, perhaps by extending unemployment insurance or by giving more money to the states.

Barney Frank, an influential Democrat on economic issues, says that stimulus must pass before the end of February. But the coming negotiations could become a nightmare. In the Senate, 60 votes out of 100

are needed to guarantee passage. Republicans may demand an extension to the Bush tax cuts. Individual senators are likely to add their pet projects and priorities. Gridlock could easily delay any compromise package past the point at which it would do the economy any good. The three "T"s may have become Washington's new mantra. But the odds of politicians delivering are still slim.

## University fees

### Affording Ivy

Jan 17th 2008 | WASHINGTON, DC  
From The Economist print edition

#### Some helpful subsidies from Harvard and Yale

WEAK dollar or no, \$46,000—the price for a single year of undergraduate instruction amid the red brick of Harvard Yard—is expensive. But nowadays cost is no barrier to entry at many of America's best universities. Formidable financial-assistance policies have eliminated fees or slashed them deeply for needy students. And last month Harvard announced a new plan designed to relieve the sticker-shock for undergraduates from middle and even upper-income families too.

Since then, other rich American universities have unveiled similar initiatives. Yale, Harvard's bitterest rival, revealed its plans on January 14th. Students whose families make less than \$60,000 a year will pay nothing at all. Families earning up to \$200,000 a year will have to pay an average of 10% of their incomes. The university will expand its financial-assistance budget by 43%, to over \$80m.

Harvard will have a similar arrangement for families making up to \$180,000. That makes the price of going to Harvard or Yale comparable to attending a state-run university for middle- and upper-income students. The universities will also not require any student to take out loans to pay for their tuition, a policy introduced by Princeton in 2001 and by the University of Pennsylvania just after Harvard's announcement. No applicant who gains admission, officials say, should feel pressured to go elsewhere because he or she can't afford the fees.

None of that is quite as altruistic as it sounds. Harvard and Yale are, after all, now likely to lure more students away from previously cheaper options, particularly state-run universities, enhancing their already impressive admissions figures and reputations.

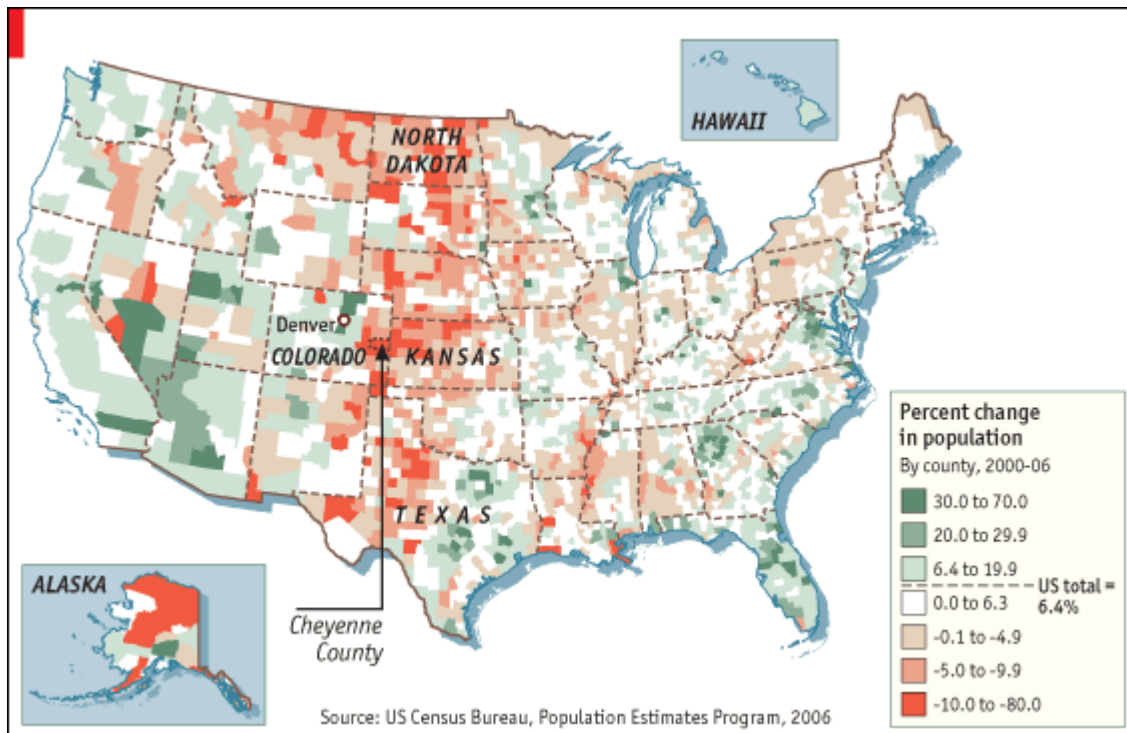
The schemes also provide a model for structuring university fees in which high prices for rich students help offset modest prices for poorer ones and families are less reliant on federal grants and government-backed loans.

Less wealthy private colleges whose fees are high will not be able to copy Harvard or Yale easily. But America's state-run universities, which have traditionally kept their fees low and stable, might well try a differentiated pricing scheme as they raise cash to compete academically with their private counterparts. Indeed, the University of California system has already started to implement a sliding-fee scale.

## Depopulation

## The Great Plains drain

Jan 17th 2008 | CHEYENNE WELLS  
From The Economist print edition



## How the interior is learning to live with a shrinking population

IN EASTERN Colorado, the human tide ebbs. Cheyenne county, which had 3,700 inhabitants in 1930, now has just 1,900. And the drift away from the area seems to be speeding up. In the old county jail, which is now a museum, a photograph from 1910 shows a three-storey schoolhouse towering over the town of Cheyenne Wells. The new school is one storey high—yet it already seems too big.

America as a whole is growing briskly. Between 2000 and 2006 its population swelled by 6.4%, according to the Census Bureau. Yet the expansion has passed many areas by. Two-fifths of all counties are shrinking (see map). In general, people are moving to places that are warm, mountainous or suburban. They are leaving many rural areas, with the most relentless decline in a broad band stretching from western Texas to North Dakota. In parts, the Great Plains are more sparsely populated now than they were in the late 19th century, when the government declared them to be deserted.

A big reason is improvements in farming technology. Tractors in eastern Colorado do not resemble the vehicles that trundle around farms on the east coast and in Europe. They are many-wheeled monsters, sometimes driven by global positioning systems. Toby Johnson says his 40,000-acre (16,200-hectare) ranch in Cheyenne county employed between eight and ten workers in the 1950s. It now has two, including him. When old farmers retire, their plots tend to be swallowed up by larger, more efficient operators.

The population of the Great Plains teeters on this shrinking agricultural base. While much of Colorado grew, Cheyenne county shrank every year between 2000 and 2006, when it lost more than 300 people. Children are disappearing even more quickly. Ten years ago 495 pupils enrolled in the county's public schools; this year 320 did. In Kit Carson, the second-biggest settlement, the school enrolled just four teenagers in the tenth grade. Shops and houses nearby are already boarded up. If the school were to close, there would be little reason for the town to exist at all.

Rayetta Palmer, a councilwoman in Cheyenne Wells, can nonetheless cite a list of local strengths. The

few children get lots of attention: Kit Carson's schools have a pupil-to-teacher ratio of seven to one, compared with 18 to one in Denver, the state capital. As a result, they do well in tests. Crime is rare. The community is strikingly cohesive: at the petrol stations that double as cafés, locals do not take empty tables but sit together, as in a school dining room.

The trouble is that such qualities are not the sort of thing that might persuade businesses to move to the area. Some are more likely to deter them. The strong community spirit sometimes morphs into a fierce resistance to change, particularly when it is advocated by newcomers. Cindy Perry, who has tried to revitalise Kit Carson by renovating buildings and starting a shop, woke one morning to find a newly-painted building covered with graffiti.

## Fighting back

Optimists point to two likely developments that may slow the decline. Assuming a power line is built, wind farms will probably appear in the area in the next few years, as they have in western Texas. That will generate construction jobs and tax revenues. A more ambitious proposal involves building a "super-highway" between Mexico and Canada, which would pass through eastern Colorado. Backers say it would almost double traffic through Cheyenne county, leading to an increase in jobs and perhaps even in people. Yet the road is many years from being built.

Cheyenne county is not especially poor. Indeed, at the moment it is enjoying an agricultural boom. Heavy snow last winter, combined with a drought in Australia, means local wheat farmers have a large crop to sell at record prices, which touched \$10 a bushel for the first time last month. In parts of north-east Colorado, corn farmers are profiting from a strong demand for ethanol. Yet the future of irrigated agriculture (the most profitable kind) is gloomy. In central Colorado, thirsty cities have been buying water rights from farmers. Elsewhere, farmers have been prevented from pumping groundwater by lawyers in Kansas, downriver. If the wells close, the corn boom will end.

There is a somewhat drastic alternative. In the 1980s two academics from Rutgers University suggested turning the plains into a "buffalo commons", where the animals that grazed the area before white immigration would be encouraged to return. The idea was so unpopular that its authors occasionally had to be protected by police. But it is nonetheless coming to pass.

Buffalo meat is leaner than beef, and thus well suited to contemporary health worries. Partly as a result, the buffalo are coming back: some 62,000 were slaughtered between January and November last year, a 17% rise over a year earlier. Of the plains states, only North Dakota has openly mulled turning over large tracts of land to the furry megafauna. But other areas, including eastern Colorado, have preserved grasslands and are touting their natural resources and history—a vivid one of brutal treks and Indian massacres.

Jo Downey of the Plains Development Corporation reckons nothing can stop the drift away from places like Cheyenne county, and others agree. The challenge for the future is not to stem the tide, but to keep life as pleasant as possible for those who remain. This is not an easy task. Compared with the consequences of rapid growth, such as traffic jams and illegal immigration, to which so much political energy is devoted, the problems of depopulation can appear intractable.



## Lexington

**Blood and oil**

Jan 17th 2008

From The Economist print edition

**Americans have always been conflicted about black gold**

Illustration by Kevin Kallaugher



FLAGELLATING the oil business is one of America's proudest traditions. Ida Tarbell, the greatest of the muckraking journalists, accused Standard Oil of building its empire on "fraud, deceit, special privilege, gross illegality, bribery, coercion, corruption, intimidation, espionage or outright terror". Upton Sinclair demonised the oil barons in his 1927 novel "Oil!". Today bookshop shelves are crammed with tomes denouncing the Bush oil dynasty, or predicting that America's dependence on oil will bring environmental Armageddon.

Paul Thomas Anderson's "There Will Be Blood" is a striking contribution to this tradition. The film, which is loosely based on Sinclair's book, is a study of frontier capitalism at its rawest. It is set in the badlands of the West—all scrub and rocks—where the people are too poor to buy bread and the only solace lies in the wonder-working power of Pentecostalism. The discovery of oil suddenly pours wealth into the community, but also brings all the usual sins of greed and envy. The local preacher is consumed by the dream of building a huge church.

The film is also a study of obsession. Daniel Day-Lewis's performance as Daniel Plainview, a wildcatter-turned-tycoon, is not only mesmerising (*Slate's* Dana Stevens describes it as "beyond praise"). It is also utterly merciless. Most of Hollywood's business anti-heroes are redeemed by their attachment to their families: the heroin baron at the heart of "American Gangster" at least buys a mansion for his mother. But the only two relationships Plainview manages—with his adopted son and a man who claims to be his half-brother—both collapse. Plainview is eventually left with nothing but his oil fortune and the resentments he has accumulated while making it.

Why have some Americans always harboured such hostility to the oil industry? Their loathing long predates worries about man's carbon footprint. It flies in the face of America's love affair with cars and the extravagant use of fuel. Many oilmen, too, have been quintessential entrepreneurs, self-reliant types who have wrestled wealth out of an unforgiving frontier. The great oil tycoons have recycled their wealth through philanthropy on a huge scale. Yet they are often hated.

One reason is the sheer wealth and power of the oil families. America is one of the few rich countries with a large oil industry (the other two—Canada and Norway—are not given to America's ostentatious displays of wealth and power). The first oil boom after 1870 produced such titans as John D. Rockefeller (America's first billionaire) and Stephen Harkness. A second oil boom after the second world war produced a new generation of Texan tycoons such as the Hunts and the Basses.

Kevin Phillips has compiled fascinating lists of America's 30 richest families throughout the 20th century. The list for 1901-14 contains six families who made their money wholly or partly out of oil. The lists for 1968 and 1982 contain eight and 11 families respectively. These oilmen have repeatedly redefined American power. Rockefeller's Standard Oil had the legislatures eating out of its hand. The sunbelt oilmen helped to promote the careers of Ronald Reagan and the Bushes.

Another reason for hating the oil industry is that it has offered "progressives" not one convenient target but two. The first is "monopoly". In 1900 Standard Oil controlled more than 90% of the country's oil supply. Though that monopoly was eventually broken, a wave of mega-mergers in the 1990s has turned the remaining oil companies into some of the biggest businesses in the world. Two years ago Congress held a series of feisty hearings on the industry's alleged price-gouging, hearings that were hardly made more civil by the news that Lee Raymond, the head of Exxon Mobil, had been given a retirement package of \$400m.

The second target is frontier capitalism. The very thing that excites conservatives about the frontier—the fact that it allows spirited entrepreneurs to test themselves against nature in the pursuit of huge fortunes—disturbs liberals. Mr Anderson echoes long-standing liberal complaints. Primitive oil wells burst into flames all over his film. Men fall into tarry pits. The obsessed and misanthropic Plainview makes more money than he can spend while others are ruined.

## **A growing slick of worries**

These days the oil critics have an embarrassment of riches to work with. Environmentalism is a perfect vehicle. The lust for oil is doing something more dangerous than creating the makeshift towns of Plainview's day: it is threatening to turn the world into an overheated mausoleum. And the Bush dynasty is the perfect foil. Dick Cheney subcontracted America's energy policy to his pals in the energy business and then fought like a demon to keep the proceedings secret. Two Bush presidents in a row have gone to war with the same oil-rich Arab country. George Bush junior has smirked at the problem of global warming—and the man he duelled with in 2000 has turned himself into the world's leading champion of environmentalism.

Worries about oil are also spreading from its molten liberal core across the rest of the political spectrum. For many conservatives, "oil" now sums up images of sinister Arabs rather than rugged Texans (the United States now imports more than half its oil compared with less than a third in 1970). They fret that America's appetite for oil is enriching potentially hostile regimes in the Middle East. Most of the Republican candidates talk about energy independence.

None of these problems is going to go away. Since oil is a global product, the notion of energy independence will remain a chimera. Americans, too, will remain reluctant to pay more for petrol or alter their energy-dependent way of life. Plenty more books and films excoriating oil can be expected in the years to come. Few, though, will be as good as "There Will Be Blood".

## Brazil's economy

**This time it will all be different**

Jan 17th 2008 | SÃO PAULO  
From The Economist print edition

**Why Brazil is better placed than it used to be to cope with a world slowdown**

Agencia Estado



BRAZILIANS know about economic and financial crises. The squalls afflicting America and threatening Europe look like a gentle breeze when compared with the frequent and violent blow-ups that litter Brazil's economic history. Much of the problem has been Brazil's vulnerability to shocks imported from around the rest of the globe. So what might happen if the economies in the rich world stumble again this year?

Recent precedents do not look good. Since the introduction of a new currency, the real, in 1994, which serves as the year zero for economic policy, growth has picked up to a reasonable rate three times. Each time, points out Eduardo Giannetti da Fonseca, an economist, people have speculated that Brazil was at last on the road to a bright new future. And each time something has come along to puncture this optimism: in 1998 it was the Asian financial crisis, in 2001 Argentina's bond default and in 2005 a rapid rise in inflation.

Now bullishness is abundant once again. The economy grew at an estimated annualised rate of 6% in the final quarter of last year (which is probably too fast). The Bovespa, Brazil's stockmarket, jumped by 60% in value during 2007. And yet even though recent history counsels caution, there are reasons to believe that the economy should cope better with whatever the world throws at it.

"Brazil has never been so well placed to face a downturn," says Mailson da Nobrega, finance minister from 1988 to 1990, a period that coincided with an inflation crisis. He now works for Tendencias, a consultancy. Arminio Fraga, who was in charge of the central bank during the Argentine collapse and the bond market's swoon at the prospect of Luiz Inácio Lula da Silva's election as president, cautiously agrees. "A lot has been driven by favourable winds," says Mr Fraga, who now runs Gavea, an investment fund. "If they stop then we are not in a position to blow up, but it won't be irrelevant."

What changed? First, domestic demand is strong. Brazil's headline real interest rate is just below 7% which, as Alexandre Bassoli of HSBC bank points out, would tip most countries into recession, but is low by Brazilian standards. The result has been a flowering of credit, which helped domestic demand grow by an annualised rate of almost 7% in the third quarter. It would take a sharp rise in rates to kill this off, and that looks unlikely.

Second, Brazil is fairly well integrated into world markets. It is not overly dependent on America, which accounts for less than a fifth of exports. The remaining four-fifths are reasonably well spread between Europe, Asia and the rest of Latin America. Admittedly, most of what Brazil produces for foreign consumption is in the form of primary goods (from orange juice to footballs), which means that export growth correlates strongly with commodity prices. But exports are not made up of any single commodity

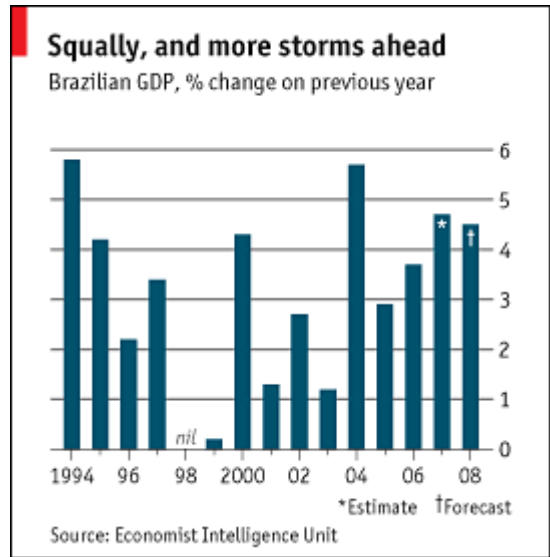
(unlike oil-rich Venezuela's, for example). "Even if China buys less Brazilian iron ore, the hope is that Chinese people will keep eating Brazilian protein," says Jose Mendonca de Barros of MB Associados, a consultancy.

Third, Brazil is less vulnerable to financial shocks than it once was. A large part of this is due to a combination of a central bank that acts independently and transparently, publishing minutes of meetings promptly on its website; and a floating exchange rate, adopted in 1999. Before then, whenever the current account deteriorated, the central bank was forced to hike rates, killing growth.

Brazil has retired its dollar-denominated debt, which has been a source of trouble in earlier financial crises. In the past, when the currency depreciated this debt ballooned, causing further problems. Now that government debt is denominated in reais, a similar move in the exchange rate reduces government liabilities. This was tested in August last year, when the real lost 11% of its value in a couple of weeks, and the government debt effectively shrank. Foreign direct investment is strong, and Brazil now holds more dollars than it owes, a happy development that has led to misguided suggestions of setting up a sovereign wealth fund.

Even so, Brazil is clearly far from immune to what happens in the rest of the world. The economy also seems to be moving into a less benign phase. After years of big surpluses, the current account looks set to run a small deficit this year. Inflation, which had been falling, picked up toward the end of last year to give an annual inflation rate in December of 4.5%. That is right on the central bank's target, and forecasters expect inflation to increase only slightly this year. But markets have been wrong on this before.

Moreover, the economy still suffers from problems that make growth above 5% look like a stretch. Government debt is still too high, Brazil invests too little, and the government takes too much for itself, spending it on things that do little to raise the economy's potential. "The easy part of growth is over," says Mr da Fonseca. But if Brazil is able to sustain steady growth without being blown off-course by events elsewhere, the country will look very different in ten years' time.



**Panama****Party time**

Jan 17th 2008 | PANAMA CITY  
From The Economist print edition

**President Torrijos's grip is beginning to falter**

PANAMA'S president, Martín Torrijos, is said to have been elected in May 2004 for two reasons: his promise to tackle vested interests and his genes. His father, General Omar Torrijos, a former dictator, is revered as the man who won back the Panama Canal from the Americans. Hitherto, this had given Mr Torrijos the clout to persuade the ruling centre-left Democratic Revolutionary Party (PRD), founded by his father, to accept much-needed economic reforms. But his grip may now be faltering.

As president, Mr Torrijos has overhauled the deficit-ridden social-security system, and seen off opposition from anti-globalisers to a \$5.25 billion project to widen the canal. He has also negotiated a free-trade treaty with the United States. But this has not yet been ratified by Washington—for a reason that reveals the continuing strength of the PRD's nationalist left-wing.

The United States is refusing to ratify the deal so long as Pedro Miguel González, a PRD member, remains president of Panama's National Assembly. He is wanted by America for the murder of an American army sergeant in 1992, three years after the American invasion of Panama, when the country's dictator, Manuel Antonio Noriega, was toppled. He had been backed by the PRD.

Mr Torrijos has made private appeals to his party to get Mr González to step aside before the latter's term ends in September. But he seems unwilling to risk a public confrontation with the PRD's nationalistic wing or the country at large. By delaying the possibility of ratification until shortly before the American presidential election, he risks killing the deal. Many business leaders are appalled.

The president has other troubles, too. Inflation has edged up, prompting a rash of wage demands and public-sector strikes. Under the constitution, he cannot stand for a second term. He may not have much say about who will succeed him as president either. Elections are due in 2009. Balbina Herrera, housing minister and standard-bearer of the PRD's left wing, is currently in the lead. The opposition is fractured and compromised by its business ties. Although the economy is booming, Mr Torrijos may find that vested interests end up proving stronger than the appeal of genes.



## Colombia

## Liberation politics

Jan 17th 2008 | BOGOTÁ

From The Economist print edition

## FARC rebels free two women hostages

HELLISH tales of men chained to trees, debilitating diseases, and surgery carried out with a kitchen knife have emerged from Colombia's jungles with the release of two women held captive by leftist FARC rebels for the past six years. It is believed to be the first time hostages have been freed without any quid pro quo.

After a botched release attempt in December, Clara Rojas and Consuelo González de Perdomo were handed over to a Venezuelan-led commission on January 10th and flown to Caracas, the Venezuelan capital, to greet awaiting relatives and a beaming Hugo Chávez, Venezuela's president, who had brokered the deal.

Colombians were gripped with horror mixed with fascination as the two former Colombian politicians recounted the ordeals they and their fellow captives had had to withstand. The 44-year-old Ms Rojas, who gave birth to a baby boy fathered by one of her captors in 2004, underwent a caesarean on a wooden table. The child, named Emmanuel, was taken from her eight months later. The FARC had promised to hand over the boy together with his mother and Ms González in December. But the mission was scrapped when it was discovered that the child had been living all along in foster care in Bogotá. Mother and son have now been reunited.

The release of the two hostages was aimed at scoring a propaganda victory for Mr Chávez, who is regarded by the rebels as a kindred spirit. At the same time, evidence of the harsh conditions in the FARC's jungle prisons is designed to turn up the pressure on President Álvaro Uribe to secure the release of the 44 remaining high-profile hostages—including Ingrid Betancourt, a former presidential candidate with dual French-Colombian citizenship, and three American defence contractors—in exchange for hundreds of guerrillas jailed by Mr Uribe's government.

However, Mr Chávez has already upped the ante, appealing to Colombia, other Latin American countries and Europe to stop labelling the FARC as a terrorist organisation and to classify it instead as a legitimate insurgent group. Most government leaders promptly rejected the idea out of hand. Daniel Ortega, Nicaragua's president and one-time rebel leader, is the only one to have supported it.

The FARC have long sought political recognition in an attempt to downplay their criminal element, says Michael Shifter of a Washington-based think-tank, Inter-American Dialogue. They finance themselves largely through drug-trafficking and kidnapping for ransom. Just three days after the release of the two women, six tourists, including one foreigner, were kidnapped near the Pacific town of Nuquí.

Mr Uribe now appears to be trying to call the FARC's bluff. If political status is what they want, he says, they will have to sit down and engage in a fully fledged peace process to end a conflict that has dragged on for four decades. If and when progress is made on that front, then Colombia's government "would be the first to stop calling them terrorists," he said.

Proof of their continuing "terrorist" status could be found in the letters and photographs of eight of the remaining hostages, sent with the released women, Mr Uribe suggested. In a letter to his family, Luis Mendieta, a Colombian police officer, who has been held for nearly ten years, said his legs had become partially paralysed. "It's neither the physical pain nor the chains around my neck that torment me," he wrote. "It's the mental anguish."

AFP



**Out of the jungle: grandmother González**

Although Mr Uribe may not like it, any deal with the FARC will almost certainly have to involve Mr Chávez despite the souring of relations between the two men. Last August Mr Uribe invited Mr Chávez to help broker a deal with the rebels, only to revoke his decision three months later. But when in December the FARC offered to free the two women into the hands of the Venezuelan leader, Mr Uribe grudgingly accepted. Mr Chávez now accuses Mr Uribe of being uninterested in peace, prompting Colombia's foreign minister to demand that the Venezuelan leader "cease his political aggression" toward Colombia.

Nicolas Sarkozy, the French president, who has made the release of Mrs Betancourt a priority, certainly feels it best to continue to curry favour with both men. In separate letters to them, he congratulated Mr Uribe for taking "courageous decisions" over the hostages, while praising Mr Chávez for his "imaginative and tenacious diplomatic action" in securing the release of the women.

Despite continued tensions between the two presidents, Colombia is likely to be seeing rather more of Mr Chávez's imaginative diplomacy.



## Barbados

## Sweet success

Jan 17th 2008 | PORT OF SPAIN  
From The Economist print edition

**A change of power in one of the Caribbean's best-run and most stable democracies**

IT WAS an all-night party in Barbados after the island's general election on January 15th. "Plenty change," a Bridgetown bar-owner grinned, and he wasn't just referring to the mounds of cash he was counting. After 13 lonely years in opposition, three election defeats and a series of long-running party-leadership squabbles, David Thompson led his Democratic Labour Party (DLP) triumphantly back to power, with 20 of the 30 parliamentary seats. In the previous election, in 2003, it won just seven seats.

By American standards, the campaign was blissfully short. The election was called on December 20th, leaving just two lively weeks after the Christmas and new-year break to get the voters in. There is no great ideological gulf between Mr Thompson's party and the outgoing Barbados Labour Party (BLP). But from time to time Barbadians like to shake up the political scene. Although Owen Arthur, the BLP leader, was regarded as a good manager, people felt that he had become a little arrogant after his 13 years in power, and some of his party rather too comfortably settled.

Voters also fretted over rising food prices, cost overruns on a road project and property prices jacked up by villa-buying foreigners. Then there was a row over claims by the BLP that Taiwan had funded Mr Thompson's campaign in exchange for a promise of diplomatic recognition. This was hotly denied by the DLP, anxious to avoid a rift with China.

Barbados is one of the Caribbean's oldest and most stable democracies, consistently getting top-drawer rankings for its political and civil liberties. From 1639 an elected House of Assembly—not the British-appointed colonial governor—controlled the island's cash. The first mixed-race member, Samuel Jackman Prescod, won a seat in 1843. Universal suffrage eventually followed in 1951, and independence 15 years later. On a visit to the island in 1859 Anthony Trollope, a British novelist, found it irritatingly well run.

Barbados also tops all other Latin American and Caribbean countries in the UN Development Programme's human-development index. Transparency International, a corruption watchdog, ranks it second cleanest in the region, just behind Chile. In September unemployment hit an all-time low of 7%, down from a peak of 27% in 1993 when the DLP was last in power.

"Change" (of leadership) was the DLP's campaign watchword. The new government, which inherits an uncomfortably big public debt, equal to 88% of GDP, will have other changes to deal with, too. Important business decisions are increasingly likely to be taken in neighbouring Trinidad rather than Barbados. Many big local firms are already majority-owned by Trinidad shareholders. Now two Trinidad companies are fighting for control of Barbados Shipping & Trading, the island's biggest conglomerate.

Sugar, the economic mainstay until the 1960s, will lose its guaranteed European market by 2015, and is already suffering EU price cuts. Costs are among the world's highest, but cane keeps the landscape in good order. Shutting down sugar would dent the country's confidence, too. Mr Arthur had proposed a new \$156m sugar factory, using cane for electricity and biofuel, and exporting pricey premium-brand Plantation Reserve sugar. The DLP called the plan a "mishmash", but has yet to come up with a better one.

Meanwhile, the island's medium-sized independent hotels, the backbone of its tourist industry, are facing rising costs and increasing competition from cruise ships; some have closed. High oil prices will push up air fares this year. Further ahead, global (over)warming may cut the pulling power of Barbados's tropical beaches, now attracting over half a million tourists a year.

On the upside, there may be oil. In 2004 Barbados faced down Trinidad in a dispute over their maritime boundaries, and two years later won a big slice of seabed, which America's Geological Service believes may contain some generous deposits, though the waters are deep and the geology complex. A bid round

for exploration rights, which has already sparked interest from several big oil companies, closes in April. Over to you, Mr Thompson.

## Taiwan's legislative election

## Bowing out

Jan 17th 2008 | TAIPEI

From The Economist print edition

## Electoral humiliation marks the end of the Chen Shui-bian era



AP

[Get article background](#)

CHEN SHUI-BIAN, Taiwan's president, called it the worst defeat in the history of his Democratic Progressive Party (DPP). After eight years of Mr Chen's lacklustre rule, it was routed in the legislative election on January 12th. The opposition Nationalist party, the Kuomintang (KMT), which wants much closer ties with China, is girding itself to return to power.

Having won more than 70% of the parliamentary seats, the KMT hopes its candidate, Ma Ying-jeou, will stroll to victory in the presidential poll on March 22nd. Under Mr Ma, the KMT—which ruled all of China until it fled the Communists to take refuge in Taiwan in 1949—predicts rapid improvements in relations with China: regular direct flights between Taiwan and the mainland (non-existent since 1949); many more Chinese tourists; and fewer investment barriers between the two sides.

But Mr Ma cannot rest easy. As they announced their victory in the legislative polls, he and his colleagues did not look jubilant. The DPP's share of the seats had fallen from nearly 40% to under a quarter. The Taiwan Solidarity Union, whose support had helped it control about 45% of the seats in 2004, was wiped out. Yet the DPP's share of the vote, 38%, was much the same; and turnout, at under 60%, was low. The DPP believes many of its voters stayed at home. They could still, despite what the polls say, tip the balance in favour of the DPP's presidential candidate, Frank Hsieh.

Mr Hsieh must be feeling a little happier now that he has taken over the chairmanship of the DPP from Mr Chen, who stepped down to atone for the defeat. (He will relinquish the presidency in May, on reaching the two-term limit.) Mr Chen had tried in vain to rally support for the DPP by playing up Taiwan's separateness from China. Mr Hsieh is more loth to provoke the Chinese and shares the KMT's desire for closer economic ties. He will want to distance himself from Mr Chen, some of whose family members and aides have been dogged by allegations of corruption.

The economy will be a big issue in the presidential poll. Taiwan's GDP has been growing at 4-5% annually for the past three years. Unemployment has stayed at around 4% and inflation last year averaged below 2%. But despite these respectable figures, many in Taiwan believe the economy would do better still if opened further to China. The DPP's fears of a "hollowing out" of Taiwanese manufacturing as the island's industries move to the mainland have failed to materialise.

The DPP administration has tried some opening up. In the face of China's bar on direct contact with Taiwan's government, it has allowed negotiations between quasi-private bodies from the two sides,

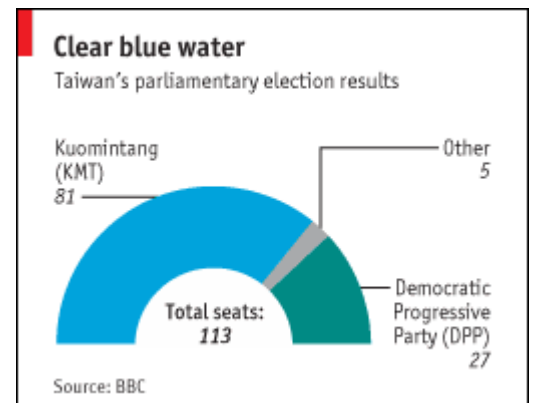
aimed at allowing 1,000 mainland tourists a day to visit the island without having to pass through a third country, as Taiwan now requires. At present only a couple of hundred Chinese tourists come each day. Agreement has been held up by bickering over whether such tourism should be described as between countries. China apparently believes that it would be easier to deal with Mr Ma, who wants 3,000 a day.

Taiwan's hoteliers and shopkeepers, mindful of how big-spending Chinese tourists have helped Hong Kong's economy, are anxious for a breakthrough. In the central city of Taichung, the mayor, Jason Hu of the KMT, says three five-star hotels have been built in the past two years to prepare for the Chinese influx. With no sign yet of its arrival, the hotels are suffering. Despite the KMT's own stand-offishness towards China until the 1990s, Mr Hu unabashedly blames the DPP.

The KMT's supporters say that if their party held both the presidency and the legislature, it would end the deadlock of Mr Chen's rule, during which the KMT and its allies have controlled enough seats to block DPP legislation. The KMT's plans are ambitious. It says it will boost GDP growth to at least 6% a year, with the help of more than \$80 billion in government spending over the next eight years on a variety of big projects ranging from sewage-treatment plants to public-transport projects. Vincent Siew, a former prime minister and Mr Ma's running-mate, says the party may even revive plans—vigorously opposed by the DPP—to expand the country's nuclear-power capacity.

The KMT's ideas for dealing with China are no less ambitious. Mr Siew says a cap on investment in China by any Taiwanese company—of 40% of its net worth—would be lifted. Direct Chinese investment in Taiwan would be allowed for the first time. Su Chi, a KMT legislator, says an agreement with China on direct scheduled flights and cross-strait shipping would be reached within a year.

Mr Ma has said that as president he would not enter talks with China about reunification. But if China removed the hundreds of missiles it has pointed at Taiwan, he would discuss a peace agreement. Last October China's president, Hu Jintao, also called for a peace accord, but on “the condition of the one-China principle”. That is, Taiwan would have to accept it is in effect part of the People's Republic. Even the KMT balks at that.



## Japan

## The “caretaker”

Jan 17th 2008 | TOKYO  
From The Economist print edition

## Fukuda braces for his biggest battle, over the annual budget

Japan's politics

THE Diet, Japan's parliament, this week saw the end of one session, an extraordinary one in every sense, and the start of another that will be ordinary only in name. With the lower house held by his Liberal Democratic Party (LDP) and its allies, and the upper house in the hands of the opposition, Yasuo Fukuda, the prime minister, has an excruciating task in securing the passage of the annual budget.

The extraordinary session was a consequence of the Democratic Party of Japan's victory in the upper-house elections last July. The DPJ's blunt leader, Ichiro Ozawa, vowed to oppose any extension of the navy's mission in the Indian Ocean, where it refuels allies' ships as part of NATO's war in Afghanistan. The government sees the mission as proof of Japan's global commitment; Mr Ozawa says it breaches the country's pacifist constitution.

Mr Ozawa warned Mr Fukuda, who took over as a “caretaker” prime minister in September, that the unprecedented use of the LDP's supermajority in the lower house to override upper-house opposition to the refuelling mission would provoke a formal censure from the upper house. And that would surely bring a general election.

Yet on January 11th, when the LDP used its supermajority to reinstate the mission, no censure followed. As for toppling the government, late last year Mr Ozawa held secret talks with Mr Fukuda on forming a “grand coalition”, an action disowned by his party. If there is any logic to Mr Ozawa's climbdown, it is that the public is indifferent to the refuelling debate. Wages are stagnant and the future of social welfare uncertain: pocketbook matters count. A member of the shadow cabinet says the DPJ is holding its fire for the budget fight. With the economy and stockmarket stumbling, that offers the best chance of bringing down the government.

A drama is certain. The annual budget needs simply to pass the lower house. But all sorts of supplementary bills need upper-house approval. If they do not get it, the ruling coalition could—at some political cost—use its supermajority again. However, procedural rules mean there is not enough time for that before the new fiscal year begins on April 1st. So government programmes might come to a halt, while tax uncertainties would harm investment.

A big battle will be over the renewal of a petrol-tax surcharge, whose proceeds are earmarked for roads and such. If the opposition wills it, petrol will fall by ¥24 (\$0.22) a litre on April 1st, and Mr Fukuda may be loth to anger consumers by forcing a price rise a few weeks later. But who cares about consumers? Most prefectural governments, including DPJ ones, want the surcharge, to lavish as pork on local building firms. Besides, stalling the budget for political ends could backfire on the opposition. And Mr Fukuda may not use his supermajority powers. Budget matters are not black-or-white, and Mr Fukuda is grey by nature. Compromises are possible.

It is a conundrum for the opposition. Unusually, the opinion polls suggest the DPJ is more popular than the ruling coalition and, for all its internal divisions, it has little to lose from a general election. Yet the election is Mr Fukuda's to call, and he says he will not even think of one until he has hosted the G8 summit, in July.

Most politicians now expect an election not in April but late in the summer. That assumes that Mr Fukuda will weather not just the budget fight, but also an almighty mess of lost records at the pensions agency and a defence-procurement scandal that looks about to claim a former defence minister, Fumio Kyuma.

By the summer, though, Mr Fukuda, the “caretaker”, may want to hang on longer. He is not bound to call

an election until September 2009. Stability, of sorts, then. The price? Continued political chaos and none of the bold measures badly needed to set the economy on a firmer footing. In the meantime, as Tadamori Oshima, the LDP's Diet-affairs chairman, moans, "The world believes Japan's politicians are unable to decide on anything, not even to put one foot in front of the other."

**South Korea****The “bulldozer”**

Jan 17th 2008 | SEOUL  
From The Economist print edition

**A president-elect starts to roll**

ASKED about the power of the president in South Korea, an aide to Lee Myung-bak, who was elected to the post last month, said he could do anything except change a man into a woman or a woman into a man. Not yet, anyway. Mr Lee, who will assume office on February 25th, will concentrate yet more power in the presidential palace, Seoul's Blue House.

At a news conference this week, Mr Lee promised a slimmed-down government. The number of ministries will be cut from 18 to 13 by eliminating or merging functions. Important economic and foreign-policy decisions will come from his office. He has also promised to privatise state-owned banks and other businesses. Cuts in corporate and personal taxation are also in the offing. “The Korean economy is too large and too complex to be managed by the government,” he says. But he seems to intend giving it his best shot.

In December Mr Lee urged the chairmen of the country's biggest conglomerates to invest more in their homeland. He has asked South Korea's mobile-phone operators to cut their charges. And he remains committed to building a canal system through the country. Critics deride the scheme as economic lunacy and a boon for construction companies such as the one Mr Lee used to run, Hyundai Construction. Others have drawn overblown comparisons between his leadership style and that of Park Chung-hee, a former military dictator with a penchant for economic micro-management.

That may be unfair. Mr Lee was elected because the country responded to his pledge of faster economic growth. As befits a former businessman, he is pragmatic rather than ideological. He maintains uneasy relations with his conservative Grand National Party. The GNP is there to win him seats in April's parliamentary election so he can pass laws.

Conservatives howled in protest when Kim Man-bok, boss of South Korea's spy agency, told North Korea that Mr Lee's election victory would not change the South's policy of engaging it. He was forced to make a public apology and resign. The same day, as if to emphasise his hardline credentials, Mr Lee visited the American army base in central Seoul.



## Australia's new prime minister

### Rudd, sweat and tears

Jan 17th 2008 | SYDNEY

From The Economist print edition

#### Labor is working. Non-stop

[Get article background](#)

WHEN he led Australia's Labor Party to a resounding election victory last November, Kevin Rudd warned members of his new cabinet they could expect just two days off at Christmas. Even for a workaholic such as Mr Rudd, this proved optimistic. Australia traditionally sinks into a summer slumber in January. The new prime minister wisely reconsidered and took a two-week holiday himself. Back at work on January 14th, he at once sent signals that he plans to be as stingy with taxpayers' money as he expects his ministers to be with their free time.

The next day he and Wayne Swan, the treasurer (finance minister), visited the Sydney headquarters of Australia's independent central bank. Mr Swan explained that the meeting was all about showing government "restraint" in a bid to tame inflation. Labor took power with a mandate to change the political climate. But the economy looms as its biggest worry.

After more than 16 consecutive years of growth, some measures of inflation are running at about 3% a year. The central bank has raised interest rates six times since 2004; economists predict another rise in February. On top of these, Australia's big retail banks have raised their rates in response to the global credit crunch.

A survey this week showed a sharp fall in consumer confidence. Mr Rudd's ministers will finger the former conservative government of John Howard. Over 11 years in power, especially the past three, Mr Howard was prone to splashing money around to buy votes. All this will make it hard for Mr Rudd to meet his own election promise to pour money into health and education, and to phase in tax cuts worth A\$31 billion (\$28 billion). Mr Swan has already pledged to cut A\$10 billion from spending in his first budget in May.

On foreign policy, Mr Rudd has shown he means business in taking a less blustery and less pro-American approach in Australia's region. After his election, the first foreign leader Mr Rudd invited to his Brisbane home was Helen Clark, the prime minister of New Zealand. Then he went to the UN climate-change conference in Bali and reversed the Howard government's refusal to ratify the Kyoto protocol.

On January 15th the government also reversed Mr Howard's decision to sell uranium to India. Australia holds about 40% of the world's known uranium, and the deal was less about commerce than about backing an American agreement on civil nuclear co-operation with India. It went against the grain of Australia's refusal up to then to sell uranium to India and other countries that had not signed the Nuclear Non-Proliferation Treaty.

For all this, Mr Rudd remains possibly the most enigmatic prime minister Australians have elected. The real balance of conservative, reformer and radical in him remains to be discovered once Parliament resumes in February. He has ordained already that Parliament will sit for five days a week instead of four. Reluctantly granted a holiday in January, his ministers can expect little sleep for the rest of the year.

**Sir Edmund Hillary****Plain man, mighty deeds**

Jan 17th 2008

From The Economist print edition

**Down to earth, even at 29,000 feet**

FEW men who find themselves cast as heroes early in life continue to command universal esteem till the end. Sir Edmund Hillary was one. To be the first to reach the top of the world's highest mountain ensured international celebrity and a place in history, but the modesty of a slightly gauche New Zealand beekeeper never departed him. Nor was mountaineering, or indeed apiculture, his only accomplishment.

Reuters

**Sherpa and friend**

Two views are often expressed about his life. One is that conquering Everest was everything. No one would play down the role of Tenzing Norgay, the Sherpa who reached the peak with him, possibly even before him; their partnership was like that of Ginger Rogers and Fred Astaire. But it was Sir Edmund who first wriggled his way up a crack in the 12-metre (40-foot) rockface that had to be overcome after the south summit if the real one was to be achieved, and below which only oblivion awaited.

News of the British-led expedition's triumph on May 29th 1953 reached the world through a report in the London *Times* four days later. The *Times*, a sponsor of the expedition, had used an elaborate code to outwit any rivals monitoring the radio waves. Its scoop was indeed a coup: June 2nd was the day of Queen Elizabeth's coronation.

Sir Edmund was a man of action. After Everest came more expeditions in Nepal, a race to the South Pole and further adventures in the Antarctic, the Himalayas and India. But for some onlookers neither these nor even the Everest expedition was especially remarkable: fitness and physical courage are all very well, they argued, but the world's highest peak was simply waiting to be scaled, and a steady traffic nowadays makes its way to the top unnoticed, except for the litter it leaves.

Both the dismissive and the awe-struck, however, agree that Sir Edmund's other life was wholly admirable, and he himself said he was prouder of it than of anything else. This was his tireless work for the Sherpas, of whom he had become so fond. Through his efforts, and those of Tenzing, hospitals, clinics, bridges, airstrips and nearly 30 schools have been built in the Solo Khumbu region of Nepal just south of Everest. If New Zealand claimed Sir Edmund's loyalty, Nepal, and especially its Sherpas, could surely claim his heart.



## India's army

## Unfit for service

Jan 17th 2008 | DELHI  
From The Economist print edition

**A shortage of officer material is another sign of India's talent deficit**

A FULL-PAGE advertisement ran in many English-language newspapers in India on January 15th for the "Harbingers of Peace and Stability"—the country's 1.1m soldiers. The occasion, Army Day, is an annual celebration of the world's second-biggest regular force. Yet the army now has a particular need of publicity: in a country of over 1 billion people, it needs more officers. Harbingers of the right stuff are proving hard to find.

Reuters

**...but not enough chiefs**

The army is short of 11,000 officers, almost a quarter of the total muster. Worse threatens. The shortage is most acute in the lower ranks, and the Indian Military Academy in Dehradun, a school for officer cadets, can currently fill only 86 of its 250 places. The army is also losing some of the officers that it now has: over 3,000 have applied for early retirement in the past three years. This week the army chief, General Deepak Kapoor, suggested that the government might one day have to introduce conscription.

The general blamed the shortage of officer material, from which the navy and air force are suffering to lesser degrees, on India's zinging economy. Graduate hirelings of the country's trendiest computer-services companies can sometimes earn twice a junior officer's monthly salary of 20,000 rupees (\$500). Moreover, the army has for decades been tangled up in nasty insurgencies in Kashmir and north-eastern India. And it has been hurt by a series of scandals, some involving corrupt top brass, others suicidal soldiers.

To improve matters, the army is banking on a generous pay rise this year; it wants junior officers' salaries to be doubled. This would at least improve its bid for India's small pool of well-educated graduates. But, given soaring wage inflation in private firms, which are also struggling to hire the talent they need, it would not fix the problem.

That will require a bigger talent pool. After all, there is no shortage of young Indians who want an army career—or indeed, given persistent high unemployment, any sort of career. The problem is that only a privileged minority of school- and college-leavers can pass the army's entrance exams for officer training. In order to match India's rise to global importance, the army needs many things: more money, better technology and a coherent foreign policy on which to build its doctrine. Above all, however, like all India, it needs more decent schools.



## A bombing in Kabul

### A bubble bursts

Jan 17th 2008 | KABUL

From The Economist print edition

#### The war is brought home to Kabul's well-protected foreigners

THE website for the Serena Hotel in Kabul used to describe it as “an oasis of luxury in a war-ravaged city”. Afghanistan's only five-star hotel is also a virtual fortress, surrounded by blast barriers, metal detectors, multiple reinforced gates and heavily armed guards. They proved inadequate defences against a four-man Taliban suicide squad that blasted its way into the lobby and then the hotel's spa on January 14th, killing eight staff and guests. Among those left cowering in the basement as American commandos hunted the bombers was Norway's foreign minister, Jonas Gahr Stoere, who had been holding a meeting in a place seen as secure.

The 140 suicide attacks in Afghanistan in 2007 were almost all aimed at Western or Afghan security forces. This was the first by the Taliban to make Kabul's expatriates a direct target. So far they have remained oddly cocooned from the violence in the south of the country, which took some 6,500 lives last year. Foreigners can still walk around Kabul with only modest caution. There are restaurants, bars and even brothels catering to the several thousand expatriates: mainly aid-workers, diplomats and security contractors.

The use of a suicide squad recalled the tactics of Pakistani jihadist organisations. The Afghan security forces were quick to accuse a Pakistan-based Taliban commander, Sirajuddin Haqqani, of plotting the attack. After the Serena bombing, a Taliban spokesman threatened similar violence against Western restaurants. All of this has sent a chill through Kabul's foreign residents. But this is still not Baghdad. Few of Kabul's inhabitants support the Taliban or want to see Western troops or aid agencies leave. There are 20,000 Western and Afghan troops defending the city.

Before the attack there had been explicit security warnings. In the hours afterwards Afghan forces reportedly arrested many of the suicide-bombers' support team. The strength of the Taliban in the provinces close to Kabul does appear to be growing. But, backed by Western intelligence agencies, Kabul's security services seem to be growing more effective.

However, the fear remains that if bombers started killing large numbers of expatriates they might force the withdrawal of some Western aid agencies and perhaps even the UN. That would be bad news for the international reconstruction effort, and worse still for the Afghan people.

## George Bush and the Arabs

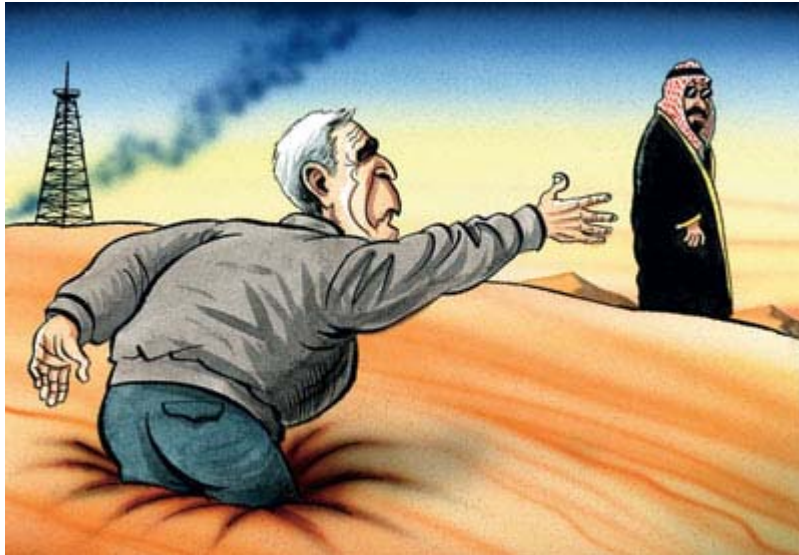
## Hard to make friends

Jan 17th 2008

From The Economist print edition

**Few Arabs are in the mood to give Mr Bush the benefit of their doubt**

Illustration by Peter Schrank



DURING half a century of American engagement with the Arab world, American presidents have tended to get nicer to the Arabs towards the end of their term, when they have less to lose at home by doing so. With his Middle East tour, George Bush has stuck to that rule. The difference is that, with America's failure to sort out Iraq or make peace between Israelis and Palestinians or to persuade Muslims that the war on terror is not unfairly directed at themselves, no other president has had to control quite so much damage.

A speech in Abu Dhabi, capital of the United Arab Emirates, was touted as the keynote of his seven-country tour. In it, he touched on familiar themes, such as the wickedness of Iran's rulers and his belief that only democracy can free people from oppression and insecurity. "You cannot stand up a modern and confident nation when you do not allow people to voice their legitimate criticisms," he said.

While officials from the host country quietly distanced themselves from America's Iran policy, Arab commentators questioned whether the head of an administration responsible for the miseries of Abu Ghraib and Guantánamo could preach human rights or whether Mr Bush's lavish praise for some Gulf monarchs' gestures towards democracy, such as holding highly restricted elections, meant that he cared more about securing cheap oil than promoting real political reform.

The state of American-Arab relations seemed more sharply depicted in Saudi Arabia, when Mr Bush joined in a traditional dance with Prince Salman bin Abdul Aziz, the powerful governor of Riyadh, the Saudi capital, and a possible future king. Meant to display tribal solidarity as he danced, a sword-clutching Mr Bush looked awkward as he shuffled clumsily, arm in arm with his robed companion.

It was, in fact, America that was supplying the real weapons, with an announcement, coinciding with the presidential tour, that it would sell Saudi Arabia 900 guided-bomb kits worth \$123m as part of a longer-term pledge to transfer some \$20 billion in arms to its Arab Gulf allies. Yet the sale's hoped-for favourable impact dissipated when an Israeli military source asserted that Israel, which is getting 10,000 American precision-guided bombs free, would get a smarter version. This comment was meant to reassure America's pro-Israeli Congress about the Saudi sale, but certainly managed to annoy the Saudis. "The region needs smart initiatives, not smart bombs," growled an editorial in Kuwait's daily *al-Rai al-Am*.



Despite the wave of sourness in the Middle East towards Mr Bush's visit, signs were noted that his administration, albeit late in its tenure, was paying more attention to Arab concerns. Assuaging fears that taking too hard a line with Iran could lead to a conflict that would hurt the whole region, Mr Bush tempered his tough language with the hope that if the "talented Iranian people" moderated their rulers' behaviour, Iran and America could become best of friends. Mr Bush also praised a new Iraqi law (see [article](#)) to let some former members of Saddam Hussein's Baath party regain their jobs; some Arab commentators noted that it was Mr Bush's administration that had demanded their dismissal in the first place. The president's repeated determination to bring about a "viable, contiguous" Palestinian state also went some way to alter the impression that his administration has been loth to press Israel to make concessions.

Though urging Arab oil producers to boost output to reduce the high price of oil, Mr Bush was careful to say that he knew many were already producing at full capacity. Such courtesy may reflect, among other things, America's appreciation that rich Gulf producers have declined so far to uncouple their currencies from the dollar, despite its falling value and advice from many local economists. Arab investors, including the sovereign funds of Kuwait and Abu Dhabi, sound willing to inject billions into wobbly American financial houses such as Citibank and Merrill Lynch.

Uglier realities did intrude, however. In Beirut, an American embassy vehicle narrowly evaded a bomb-blast that killed three bystanders, further shaking the hold of Lebanon's pro-American government, which has been locked in a stalemate with its opponents led by Hizbullah, the Iranian-backed Shia militia. And an Israeli raid against rocket-firers in Gaza killed 18 Palestinians, the highest day's death toll for months. The dead included a son of a former foreign minister of Hamas, the Islamist group that seized the strip last summer. He blamed Mr Bush for giving Israel a "green light" for the killings.

## Iraq

## A hint of political compromise at last

Jan 17th 2008

From The Economist print edition

**The passage of a long-awaited law offers a ray of hope for reconciliation**



**Can Maliki be more than just a Shia poster boy?**

FOR nearly two years, Iraqis and outsiders trying to revive their country have been waiting in vain for politicians in Baghdad to agree to a clutch of laws that might coax Iraq's feuding sects towards a common vision. The Americans' military "surge" was explicitly intended to give the politicians a breathing-space so that, as security improved, they could force through some necessary measures. The surge has worked better than expected but the politicians, despite cajoling from their American mentors, have seemed unable to compromise. Now, however, the belated passage of a law to give former members of the once-ruling Baath party a better deal may at last unblock the political logjam.

Earlier this month, parliament voted by a show of hands to approve an "accountability and justice" act that removes many restrictions imposed on the middle (but not top) level of Baath members, whose cadres were disproportionately Sunni. Some 30,000 one-time Baathists may now apply for pensions or even reinstatement in their old jobs, a measure meant to persuade insurgents that there is a place for the Sunni elite in Iraq's new political order.

It is not yet clear whether the new law will do the trick. Radical Shias, who complained that its earlier drafts would have let Baathists infiltrate back into government and perhaps even stage a coup from within, were oddly supportive of the final version; it may not be quite as forgiving as it would first appear. Several thousand senior Baathists are still excluded. According to some readings of the law, others are barred from working in the powerful ministries of interior and defence. Some former Baathists complain that, whatever the law says, they have no desire anyway to go back to work in ministries now dominated by Islamist Shia parties. Others have suggested that the law is a ploy to lure them into the open and have them killed.

In fact, the law's precise provisions may count less than the signal sent by its passage. Pensions for retired Baathists will, of course, be appreciated. But deBaathification affected a fairly small number of people; in some ways it was more a symbol than a tool of Shia domination.

If the Sunni insurgency is to be tamed, it is now more vital for the Shia-led government to accommodate a new generation of Sunnis who have been strikingly successful in leading a movement known as the "Sunni Awakening" against those of the insurgents who are linked to the extremists of al-Qaeda, especially in the Euphrates river valley to the west and north-west of Baghdad. (The worst bloodshed is now in the Tigris river valley north and north-east of Baghdad.)

The Awakening leaders want their own vigilante groups, known in American parlance as "concerned local citizens", to be inducted into the official security forces. This would give Sunni towns and districts the feeling of policing themselves rather than of being occupied by hostile Shia forces. So far, Iraq's prime

minister, Nuri al-Maliki, has been loth to bring the Sunni vigilantes fully into the national security forces for fear they may later turn their arms against the new Shia establishment.

## Now for a little trust

In any event, the hope is that, with the deBaathification dealt with, Shia and Sunni leaders may move ahead on other matters and allay some of the mistrust that has driven both sides into rigid positions for fear of losing sectarian support. Most encouraging, the Iraqi Accord Front, the main Sunni alliance in parliament, whose representatives walked out of Mr Maliki's coalition government in a huff last summer, says it will walk back in, restoring at least a semblance of national unity.

If the government could now pass the oil bill that has been debated for two years, Iraqi politics really might get moving. Unfortunately, there is still no sign of an early breakthrough. The day after the deBaathification law was passed, members of parliament from the powerful and virulently anti-Baathist Shia movement led by a fervid clergyman, Muqtada al-Sadr, signed a pact with representatives of a secular and mainly Shia party led by Iyad Allawi, a former Baathist once favoured by the Americans, and with a small Sunni-led party called the National Dialogue Front, led by Saleh al-Mutlaq, who champions former Baathists' rights. The pact's signatories say that the federal government in Baghdad should retain full control of the oil industry, whereas the Kurds in their autonomous region still insist that they should control, among other things, the management and exploration of oil in their area.

In theory, this odd-looking new alliance in parliament could count on up to 100 votes in the 275-member chamber. Since Mr Maliki's alliance with the Kurds has frayed, thanks to the row over oil and the failure to hold a promised referendum on the disputed province of Kirkuk, 100 votes could be enough to bring him down. But it is not clear how strongly the Sadrists are wedded to the new alliance. Moreover, however unpopular Mr Maliki may be, few Iraqis want to restart the whole tortuous process of building a coalition government. Besides, the Sadrist movement is itself a loose alliance of local warlords and pliant populist politicians. Mr Sadr currently spends more time trying to keep his own house in order than fighting for more power at the national level.

A possible shift of power in the provinces may have a bigger effect. The third big element in the national reconciliation package, after the laws to do with the Baath party and oil, is provincial elections. Most Sadrist and Sunni politicians refused to stand when they were last held, in January 2005, which meant that the provincial councils in Sunni areas were unrepresentative and often toothless. If militant groups could be persuaded to take part this time, the new councils might go some way to empowering the hitherto disaffected Sunnis—and perhaps persuade them to engage in peaceful politics. Then there might be more than a glimmer of hope of the country's returning to the path of peace.

## Kenya

**A cracked nation holds its breath**

Jan 17th 2008 | MOMBASA  
From The Economist print edition

**The economy is shaking as government and opposition remain deadlocked**

[Get article background](#)

NEARLY three weeks after a bitterly disputed election, President Mwai Kibaki (left), who almost certainly lost it, is defiantly refusing to compromise, let alone bow out, in the hope that time is on his side and that the fury of the thwarted opposition, led by Raila Odinga and his Orange Democratic Movement, will gradually subside. International mediators and Western diplomats have made no headway. The violence, which has caused some 600 deaths, has lessened a bit but has certainly not ended.

Mr Odinga's Oranges won at least one notable victory this week after Parliament reopened. Despite a determined and expensive effort by the president's men to win over representatives from smaller parties, the Oranges got their choice as speaker, the third office in the land, when Kenneth Marende, a lawyer, squeaked in by 105 votes to 101. "I need all the prayers I can get," he said afterwards.

Indeed he does. At times the proceedings were absurd. "Let us not make this political," implored the presiding clerk, while the two front benches exchanged taunts of "thief" and "murderer". Mr Kibaki was ignored by the opposition when he limped in; the Oranges rose in applause at Mr Odinga's entry. Mr Marende's election as speaker may have saved lives. Nationwide Orange protests were disruptive but less lethal than they might have been.

So far, Western governments have yet to recognise Mr Kibaki fully. The biggest aid-givers, including the United States, Britain and the European Union, are threatening to divert their largesse from government coffers unless he seeks a "meaningful settlement" with the opposition. It is unclear whether that means the West wants Mr Kibaki to step down.

The Americans were at first readier to endorse his re-election, because he has been their sturdy ally in their war on terror, whereas Mr Odinga, who won most of Kenya's Muslim votes, is warier of an American alliance. Now, however, the Americans seem to have come round to the European and British view that Mr Kibaki should, at the very least, offer Mr Odinga and his party a big role in government or perhaps even agree to run the election again, though that seems highly unlikely.

Other African governments seem loth to interfere. John Kufuor, the Ghanaian president who also chairs the African Union, tried to mediate but entirely failed to shift Mr Kibaki, whose inner circle is plainly dismissive of international arbitration. "We won the election and do not see any point in anyone coming to mediate power-sharing," says John Michuki, a former security minister now in charge of roads. Another would-be mediator, the UN's former secretary-general, Kofi Annan, this week conveniently came down with flu and delayed his trip to Kenya.

But Mr Kibaki is not yet home and dry. His loss of the speakership shows how hard it will be for him to govern through Parliament. He may try to ignore it and run the country from State House. With loyalists running the finance, justice and energy ministries, plus the security services, he may be able to do so. But it may make him even more unpopular outside his Kikuyu heartland and increase the lawlessness.



Reuters



Meanwhile, the economy is fast beginning to suffer. Business in down-town Nairobi, the capital, and in provincial towns across the country, has slumped. Tea-brokers in Mombasa, Kenya's second city, whose port serves most of east Africa, say that another month of instability could ruin the city's regular auction of one the country's main exports.

Asian Kenyans are especially jittery. Many in the western city of Kisumu, Mr Odinga's provincial capital, have fled to Uganda. Some in Mombasa say they want to leave Kenya for good. An exodus of Asians would badly hurt Kenya's economy. So would the loss of shipping business to Dar es Salaam in neighbouring Tanzania, where a number of container ships have already been diverted.

Pictures of angry men with machetes have scared off holidaymakers from the coast. Some hotels have closed for the season, others are nearly empty. Dhows and camel rides have no takers. South of Mombasa, many businesses belonging to Mr Kibaki's fellow Kikuyus have been burnt.

If Mr Kibaki wants to rescue Kenya's faltering economy, let alone mend its politics, he must seek a compromise with his angry opponents. It is not yet clear whether time is on his side—or on Mr Odinga's.

## South Africa

## Let's all arrest one another

Jan 17th 2008 | JOHANNESBURG  
From The Economist print edition

## How not to run a police force

[Get article background](#)

IT SEEMS, for the moment, as if South Africa's governing class is being engulfed by charges of corruption. Three weeks ago it was the turn of Jacob Zuma, the newly elected leader of the ruling African National Congress (ANC). He was charged with fraud, tax evasion and money laundering and is due in court in August. This week it was the turn of Jackie Selebi, the head of the police. The National Prosecuting Authority says it will charge him with corruption and "defeating the ends of justice". He has been suspended from his job and he also resigned as head of Interpol, the international police body. On January 8th the police also arrested Gerrie Nel, a senior member of a special investigations unit known as the Scorpions, also on charges of corruption. He is the man who had led the investigation into Mr Selebi. All the charges against Mr Nel, however, were dropped a week later.



EPA

**Selebi and the pointing of fingers**

All these cases point to an unduly incestuous relationship between the politicians and the country's supposedly independent security apparatus. They also illustrate the way in which the acrimonious battle for power between Mr Zuma and Thabo Mbeki, the country's president whom he defeated in December's ANC leadership election, is poisoning both the civil service and the political system.

Mr Selebi is Mr Mbeki's man, and the president has discredited himself by defending his friend too doggedly. Months ago Mr Selebi admitted to being a friend of Glen Agliotti, a drug trafficker who was implicated in the murder in 2005 of a shady mining magnate. When faced with angry public calls to replace Mr Selebi, Mr Mbeki merely asked South Africans to trust him. The prosecuting authority's new allegations are particularly damaging. It says that as well as handing out bags of cash to Mr Selebi, Mr Agliotti also paid for some of the police chief's shopping. In return, Mr Selebi protected Mr Agliotti's friends and shared confidential documents with him. The police chief denies all the charges.

The prosecuting authority, already accused of abusing its power to settle scores against Mr Zuma, has itself been caught in the crossfire, as have the Scorpions, who report to it. In September Vusi Pikoli, the national prosecutor, was suspended as he was poised to arrest Mr Selebi. Mr Mbeki said this was due to a breakdown in Mr Pikoli's relations with his boss, the justice minister. But the timing of Mr Pikoli's fall fed suspicions that he was in fact being punished for going after Mr Selebi.

Mr Nel's arrest was seen by some as retaliation by Mr Selebi's force against the Scorpions, since they had helped bring the charges against Mr Selebi. That the charges against Mr Nel were dropped so fast suggests that they were pretty spurious in the first place. The episode will only deepen the bitter rivalry between the Scorpions and the regular police.

This murky sort of business would scandalise any country. But in one plagued by some of the highest levels of violent crime in the world, it is tragic that South Africa's law-enforcement officials should expend so much energy fighting each other rather than the criminals. The police judged that they needed no fewer than 20 armed officers to arrest Mr Nel at his home. On the hopeful side, the charges against Mr Selebi show that no one yet is above the law. But if they turn out to be true, it will further reduce confidence in a police force that is often perceived, at best, as merely incompetent.





## Zimbabwe

**A serious rival, at last?**

Jan 17th 2008

From The Economist print edition

**Robert Mugabe may be facing his most dangerous opponent yet**

THE new year has brought little joy to most Zimbabweans, as they struggle to survive worsening food shortages, hyperinflation and joblessness. But at least there is a flicker of movement on the political front. The ruling ZANU-PF is said to be on the brink of splitting, ahead of parliamentary and presidential elections due in March. Simba Makoni, a former finance minister, has been named as a prospective splinter's possible leader. Could he pose a serious challenge to President Robert Mugabe's hitherto firm grip on power?

Mr Makoni, who has been in and out of cabinet since 1980, is still part of the ruling party's top leadership. Widely respected as a technocrat and one of ZANU-PF's few stalwarts untainted by corruption, he is a danger to Mr Mugabe because he could appeal both to disgruntled people in the ruling party as well as to the opposition. He does not have much grassroots support, but, in the words of Sydney Masamvu of the International Crisis Group, a Brussels-based lobby, he heads "a coalition of the wounded, the marginalised and the bitter" within ZANU-PF. Some within this coalition have links to Solomon Mujuru, a powerful party figure and former army chief whose wife is a vice-president. But it is unclear whether Mr Mujuru, who has hedged his bets in the past, is directly involved in Mr Makoni's brave—or rash—bid.

Mr Mugabe would struggle to see off a big revolt within his ZANU-PF, especially if it were in cahoots with the opposition Movement for Democratic Change (MDC). But such an alliance would be hard to forge. Mr Mugabe has destroyed or co-opted his rivals for decades. The success of this latest rebellion would depend on whether the economic catastrophe and Mr Mugabe's excesses make enough ZANU-PF people stand up to the president and then stick together. If so, it may convince the MDC, which is itself split into two factions and is weak on its own, to close ranks and jump on a bandwagon led by Mr Makoni.

In the meantime, talks between ZANU-PF and the two-headed MDC resumed this week. Following the beating-up of MDC leaders last March, South Africa's president, Thabo Mbeki, has been trying to mediate between the two sides. As a goodwill gesture, the MDC agreed to a constitutional amendment proposed by the ruling party that upped the number of seats in parliament, though the new constituencies are likely to favour ZANU-PF, which keeps a firm grip on rural areas. In December, repressive security and media laws were eased a bit. In a breakthrough, both sides agreed in principle to a new constitution.

But the talks have not improved things on the ground. Amnesty International, a human-rights group, says the government still beats and tortures its opponents. Local watchdogs have decried irregularities in voter registration ahead of the election and in demarking constituencies.

The MDC also wants the new constitution, which includes a requirement for an independent electoral commission, enacted before the election. This would mean preparing for it all over again, which Mr Mugabe unsurprisingly refuses to do. So the opposition wants the election postponed, and Morgan Tsvangirai, one of the MDC's rival leaders, has threatened to boycott it if these conditions are not met.

Mr Mugabe, in power since 1980, is bent on winning another term. The South Africans hope that, fairly soon after that, he will step down and hand over to an anointed successor from within ZANU-PF, perhaps Emerson Mnangagwa, a former security chief who has been the Mujurus' rival in the ruling party. The new ruler might—so the plan goes—reach out to one faction of the MDC and form a national unity government. The West might then pile in with cash and advice to give Zimbabwe a fresh start.

But Mr Makoni's bid, if he makes it, would turn all such calculations upside down. It is unclear how Mr Mugabe would handle or squash him—or whether Mr Makoni would take a big chunk of ZANU-PF with him or form a wider coalition from outside the ruling party. The MDC faction led by Arthur Mutambara is said to be keen to join up with him.

Mr Mugabe, for his part, is said to be terrified that a new regime would send him to face charges of crimes against humanity at the international court in The Hague. In any event, Mr Makoni has given Zimbabweans at least a fleeting moment of hope that real change is in the offing at last.

## Germany's state elections

## Pay and punishment

Jan 17th 2008 | WIESBADEN  
From The Economist print edition

Reuters

**To judge from its state election campaigns, Germany's governing parties are flirting with recklessness**

THE blows were struck in Bavaria but the impact was felt as far away as Hesse. On December 20th a young Greek and his Turkish companion answered a pensioner who told them to stop smoking on the Munich underground by beating him up. "We have too many young foreign criminals," responded Roland Koch (above, with Angela Merkel). Mr Koch is fighting to be re-elected for a third term as Hesse's premier. Foreign miscreants, he declared, should be deported; young ones should be taught a lesson with "warning-shot arrests", "education camps" and stiffer sentences.

Mr Koch pronounced himself "the acknowledged voice of a silent majority of Germans". The row over that claim has swamped local issues in the election and poisoned already tense relations between the two parties in Germany's "grand coalition" government.

State elections often test the popularity both of German governments and of the themes deployed later in national contests. The previous chancellor, Gerhard Schröder, called an early federal election after his Social Democratic Party (SPD) lost power in North-Rhine Westphalia in May 2005. This time, three forthcoming state elections—in Hesse and Lower Saxony on January 27th and in Hamburg on February 24th—are trials not so much of the ruling grand coalition as of the reluctant partners that constitute it, the SPD and the Christian Democratic Union (CDU).

Lower Saxony's premier, Christian Wulff of the CDU, should easily defeat his SPD rival. Hamburg, a city-state, matters little, though it could produce Germany's first state-level coalition between the CDU and the Greens. But in Hesse, a medium-sized state that thrives as a hub of transport and finance, the race is close and the stakes high. The SPD hopes to pull out of its political tailspin, the CDU to confirm its position as front-runner in the federal election, due by September 2009.

Mr Koch's scolding of foreign hooligans brought the talk to boiling-point. It is "an insult to every corner of Germany", thundered the SPD's Frank-Walter Steinmeier, who is both vice-chancellor and foreign minister. Joschka Fischer, a former Green leader and foreign minister, plans to break his vow of political silence to boost his party and slam Mr Koch's.

To Mr Koch's surprise, the SPD has been making some headway. His challenger, Andrea Ypsilanti, has been championing the party's demand for minimum wages in selected low-paid industries and, eventually, throughout the economy. The party hopes to distance itself from the reforms enacted by Mr Schröder, which alienated supporters and helped fuel the rise of the Left Party, heir to East Germany's

communists. For the first time in two years, says Klaus-Peter Schöppner, a pollster, the SPD is setting the political agenda.

The CDU dares not resist too stoutly. Although state governments have little say in wage policy, the gap in Hesse between the SPD and the CDU has narrowed to four percentage points, from nearly 20 when Mr Koch won an absolute majority in 2003. Ms Ypsilanti, a former stewardess from a working-class family, has pulled almost even with Mr Koch as voters' first choice for the state's top job.

So he has changed the subject to teenage thuggery, a theme taken up by the CDU's national leaders. "There can be no taboo issues in election campaigns," says the chancellor, Angela Merkel. Whether this tack will pay off is unclear. More than 60% of Hesse's voters back tougher treatment of young criminals, but 56% want minimum wages, according to Forschungsgruppe Wahlen, a pollster.



But Mr Koch is still fighting charges that he has cut the number of police and is embarrassed by new figures showing that assaults by teenagers have jumped by 66% since 1999, more than almost anywhere else in Germany. He may have gone too far when he suggested parts of the penal code for youth could be applied to children under 14, which was widely read as an argument for throwing them in jail.

Both parties' vote-grubbing initiatives seem more populist than sensible. Nearly 1,000 experts have signed a statement declaring that the "penal law cannot be a substitute for helping children and teenagers or for policies that promote integration" of minorities. Opinion on minimum wages is more divided, but most economists think they are an inefficient way to fight poverty and that, set too high, they will destroy jobs.

Mr Koch has dabbled in divisive politics before (a campaign against dual citizenship helped him to win office the first time), but he has governed as a technocrat, not an ideologue. Crime has fallen, thanks partly to his enthusiasm for video surveillance of public places; he has repaired the school system. He recently won planning approval for a fourth runway for Frankfurt's airport, Europe's third-busiest, which may help prolong the state's economic upswing. On knotty tax issues, the CDU has often turned to him to strike compromises with the SPD finance minister, Peer Steinbrück. Mr Koch may still hope one day to replace Ms Merkel as chancellor and CDU leader.

But his lustre has dimmed. Hesse was slow to cut back study in *Gymnasiums*, schools that prepare students for university, from nine years to eight. When it acted, it was clumsy, angering the majority of voters who say education is their top concern. Mr Koch excels as an orator but flops on television. The amiable Ms Ypsilanti, meanwhile, has begun to master policy and smarten up her speeches.

Likely to lose his absolute majority, Mr Koch hopes to govern with Germany's liberals, the Free Democrats. But the election could produce more awkward results. If the Left Party crosses the 5% threshold for entering the state assembly, that could produce a left-wing majority with the SPD and the Greens. But the SPD says it will not depend on the Left either in coalition or even just for support. That could lead either to a three-party combination (the Greens and Free Democrats plus one of the big parties) or, more likely, to yet another unloved grand coalition. Even if the CDU were to lead it, Mr Koch

might give up.

Germany's leaders say they are eager to put the ugliness of the elections behind them: 2008 is the coalition's "key year", says Ms Merkel. But the row over punishment and pay is ominous. The two big parties have come to resemble each other. To persuade voters there is a difference, both have shown, in state elections, that they are prepared to flirt with reckless ideas.

## French defence policy

## En garde

Jan 17th 2008 | PARIS  
From The Economist print edition

## The significance of France's military base in the Gulf

Alphafrance

**Down the Champs-Élysées, and out into the world**[Get article background](#)

FRANCE'S announcement this week that it is to open a military base in the United Arab Emirates could mark a strategic shift in its defence policy. It will be France's first permanent base in the Gulf, in a country where it has no colonial ties. By drawing its 400 troops from an existing base in Djibouti, it hints at a withdrawal from France's traditional African backyard. Moreover, coming in the middle of France's first full defence review for 14 years, it suggests a radical rethinking of the country's defence and security policy.

The future of French overseas military bases is one element under review. France now has around 5,000 soldiers in three permanent bases in Africa: Senegal, Gabon and Djibouti. It also has 2,600 soldiers on a peacekeeping mission in Côte d'Ivoire, and 1,100 on the ground in Chad soon to be joined by another 2,000 as part of a French-led European Union force. Ties of history keep French soldiers in Africa. But President Nicolas Sarkozy has told the defence review team to "construct the security and defence of tomorrow according to needs, not habits".

Mr Sarkozy has pre-empted his own review's conclusions, not due till March, by announcing the Emirates base, just across the Gulf from Iran. It shows that the French are ready to move outside their traditional sphere and to match their military presence to strategic interests rather than colonial links. Although the base will be small, it also suggests that Mr Sarkozy, who has taken a tougher line on Iran than his predecessor, may be ready to take a bigger part in stabilising the region.

There could be more surprises to come. Jean-Claude Mallet, head of the defence review, says it aims to define a "new doctrine" of security and defence. Mr Sarkozy has told him nothing should be taboo. A white paper is due in the spring and legislation is planned by the summer.

One idea is that France should set up a National Defence and Security Council, loosely modelled on the American version, to co-ordinate domestic and foreign security. Another suggestion will be a commitment to maintain defence spending at about 2% of GDP, roughly the same as in Britain. Despite defence-spending increases, French military types complain about the lack of transport aircraft and the shoddy state of the helicopter fleet.

Perhaps the trickiest issue is France's role in NATO. It is a member, and participates in many NATO operations: one-third of the 10,000 French soldiers on missions abroad are under a NATO banner; a

French general commands the NATO force in Kosovo. But since de Gaulle pulled France out of the alliance's integrated military command in 1966, it has had no say in NATO defence planning. Mr Sarkozy, who likes to make a splash and please the Americans in equal measure, has hinted strongly that France could soon rejoin fully.

Not, however, without one key condition: more progress on European defence. Mr Sarkozy, in short, wants the British to back European defence properly, and the Americans to stop distrusting this on the ground that it may be a rival to NATO.

The trouble is that Gordon Brown, Britain's prime minister, is in no hurry to pursue anything that has the slightest whiff of deeper European integration, especially with the EU's reform treaty still before the British parliament for ratification. Relations between Mr Sarkozy and Mr Brown are businesslike rather than warm. They may not be helped by the ostentatious love-in between Mr Sarkozy and Tony Blair, who spoke (in French) to rapturous applause at an event organised by the president's centre-right party last weekend. The French have found it hard to drum up support for the EU force in Chad: neither the British, who are stretched in Iraq and Afghanistan, nor the Germans are sending any troops.

French officials are frustrated by the lack of British response to their hints about NATO. But it is hard to see room for compromise. Something less than a full-blown EU defence headquarters would not satisfy the French; anything too grand or NATO-duplicating would not get past the British. As one French official puts it, however, "Sarkozy will not accept no response. If he doesn't get agreement, he'll go somewhere else." There is even talk of dealing directly with America, doubtless pleased with France's planned Emirates base. But it is hard to see that working in America's fraught election year.



## French broadcasting

## No English, please

Jan 17th 2008 | PARIS  
From The Economist print edition

## The “pro-American” president takes on France's English-speaking television

“GOBSMACKED!” That is how one journalist at France 24, a television news channel, described the newsroom's reaction to President Nicolas Sarkozy's announcement that the channel should in future broadcast only in French. That such a colloquialism—in English—reverberates so readily around a French television studio shows how bilingual the channel has become in a land known for linguistic chauvinism.

France 24, jointly owned by the public broadcaster and TF1, a private station, was set up just over a year ago as a result of French exasperation at American dominance of the airwaves. The French were vexed, particularly during the invasion of Iraq, by the cheerleading of American networks, and wanted a CNN *à la française*. From the start, it was obvious that to offer a “French perspective” to others, it would have to broadcast in languages other than French, just as al-Jazeera knew it could not broadcast only in Arabic. France 24 began with channels in French and English; an Arabic station followed.

France 24 can be slow to react to breaking news. It has a small budget—€80m (\$119m) a year—and a relatively sparse network of reporters, though it can draw on those of its sister news organisations. It has struggled to find distribution channels, notably in America. But it has turned out not to be a mere mouthpiece of French government. And it has supplied a useful alternative both in style (more long debates) and content (more, say, on Lebanese politics) to other global news channels.

So why does Mr Sarkozy want to close down its non-French channels? One reason is budgetary: he says he is “not disposed to finance a channel that does not speak French”. The other is diplomatic. “In order to present a French vision,” he says, “I would really prefer it to be presented in the French language.” The French have long considered their language to be more than a tool of communication: it is an embodiment of culture, identity and independence. To speak to the world in another language seems like a gesture of submission.

For now, France 24's English channel continues to broadcast; managers have told reporters they will lobby hard to keep the station alive. Bernard Kouchner, the foreign minister, says he does not share his boss's view that it is pointless to broadcast in English. For his part, Mr Sarkozy has made a point of embracing America, advertising his love of Hollywood films, even taking his summer holiday in New Hampshire. It would be an irony indeed if the president who promised to liquidate French anti-Americanism ended up abolishing France's best example of reaching out to the English-speaking world.

## Serbia

## Still surly

Jan 17th 2008

From The Economist print edition

## Serbia's presidential election this weekend is critical to the region's future

AFP

[Get article background](#)

WHEN an election was held in Croatia last November, it was hailed as the first in 20 years in which voters could be sure that the winner would not stop Croatia from moving towards the European Union. Judging by the rancorous debates of recent weeks, the people of Serbia, who vote for a president on January 20th, can only envy their neighbours.

There are two serious candidates: Boris Tadic, the pro-European incumbent, and Tomislav Nikolic, acting leader of the extreme-nationalist Radicals. Although more formal power lies with the prime minister, Vojislav Kostunica, than with the president, the result matters hugely. And it comes at a delicate moment. Within weeks Kosovo plans to declare independence, and will be recognised by many countries. How Serbia responds will define its future.

On paper Kosovo is still part of Serbia. But since the war of 1999 it has been under the jurisdiction of the United Nations. Some 90% of its 2m people are ethnic Albanians who have long demanded independence. When that comes, it will be the end of the Serbian control, real or nominal, that began when Serbia retook the province from the Ottoman Turks in 1912.

**Tadic, a tad nervous**

The UN is handing control of Kosovo over to the EU, which has agreed in principle to establish a large mission to deal with police and justice in the province. At the same time Serbia is ready to sign a stabilisation and association agreement (SAA) with the EU, normally a first step towards membership. That would bring substantial funds plus a set of reforms the country needs to make before joining, thereby catching up with Croatia, which is already negotiating its EU membership. It may be helpful that Slovenia, another bit of former Yugoslavia, currently holds the six-monthly rotating EU presidency.

Mr Tadic's party is pro-Western, but still opposes Kosovo's independence. It shares power in government with Mr Kostunica's conservative nationalists. Mr Kostunica has said that any EU mission to Kosovo would be illegal without Serbia's consent, and also that Serbia should not sign its SAA if the mission goes ahead or if most EU countries recognise Kosovo's independence (which they will).

Mr Tadic responds that, whatever happens in Kosovo, Serbia has no choice but to sign the SAA. Mladjan Dinkic, Serbia's finance minister, adds that it would be a "catastrophe" if Serbia were the only country in the region left out of the EU. Serbia, he says, will attract \$6 billion of foreign direct investment this year, but it is clear that potential investors will lose faith if the country abandons its course for the EU. Mr Nikolic, on the other hand, agrees with Mr Kostunica that if most EU countries go ahead with plans to recognise Kosovo, Serbia should give up trying to join the club.

Opinion polls suggest a close result on January 20th, which means a second round between the top two candidates will have to be held on February 3rd. Mr Kostunica's party is not offering a candidate, neither is it backing Mr Tadic; many of the prime minister's supporters may rather vote for Mr Nikolic in the second round. And though Mr Tadic may still squeak through, he cannot count on much enthusiasm from many of his erstwhile supporters who think he has been a weak president, bossed around by Mr Kostunica.

It was originally hoped that Serbia could sign the SAA on January 28th, between the two rounds. That

hope is fading, because some countries are reluctant to let Serbia have the deal until it hands over Ratko Mladic, a Bosnian-Serb general indicted for genocide, to The Hague war-crimes tribunal. Even if the agreement is signed, the quarrel over Serbia's future in Europe will continue—for if the EU sends its mission to Kosovo, Mr Kostunica's party could then block parliamentary ratification of the SAA. Serbia's long slog towards normality never seems to end.

## Energy in Poland

## Walking on hot coals

Jan 17th 2008 | WARSAW  
From The Economist print edition

## Poland does not see why the European Union should stop it burning coal

THE Polish economy is growing fast, despite the global slowdown. That means it is consuming more energy. But the government has no real energy policy—so the country will end up using more coal, with all that implies for carbon emissions.

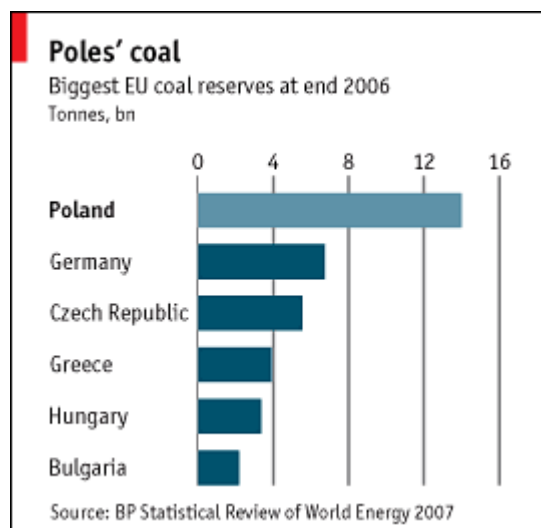
As it happens, the biggest worry about energy in Poland is not carbon but the Nord Stream pipeline, which is due to pump Russian gas directly to Germany under the Baltic Sea, bypassing Poland. Polish objections are not, as in Sweden, about the environmental risks; rather, the Poles fear Russia may exploit its direct access to Germany to divide Europe. All Polish politicians oppose the project. Lech Kaczynski, Poland's president, hoped last year to forge an alliance with four ex-Soviet states to help Poland diversify its energy sources away from Russia. But the president of petro-pumping Kazakhstan, Nursultan Nazarbayev, pulled out, cancelling his trip to a Polish-sponsored energy summit.

Nuclear-power policy is no more successful. An agreement between Poland and the three Baltic countries to build a nuclear-power plant on the site of a former Soviet reactor in Lithuania has not yet been signed. The Poles are unhappy that the Lithuanians are offering them less than the 1,200 megawatts of electricity they need for the project to make economic sense. Another idea is to build a nuclear-power plant in Poland itself, its first. But this is unpopular with Poles, who recall the Chernobyl disaster in Ukraine.

So attention returns to coal. Waldemar Pawlak, the economy minister, has declared his love for the black stuff and, partly in response to record oil prices, has even called for greater emphasis on it. Poland depends on coal for some 95% of its electricity. But the European Union's ambitious plans to cut carbon-dioxide emissions by 20% by 2020 and to boost renewable energy are raising questions over coal. The Poles have already taken the European Commission to court over their emissions allowance, which they say is unreasonably low. This clash will continue, as all EU members seek higher emissions allowances and lower targets for renewables (see [article](#)).

Poland will inevitably continue to rely heavily on coal, says Jerzy Buzek, an engineer who served as prime minister in 1997-2001 and is now a member of the European Parliament. The country has the biggest coal reserves in the European Union (see chart). The government supports the development of technology to make it cleaner and more efficient to burn coal, but that is not yet available. Mr Buzek pins his hopes on techniques to liquefy or gasify coal, but they are not yet developed. The capture and storage of carbon emissions underground is another possibility, but has yet to be used on any scale. And it could send the cost of coal soaring.

Next week, the commission will propose its emissions targets. Like others in eastern Europe, the Poles think the problem has been caused by richer countries. But as the biggest EU member in the region, they need an energy policy, too.



## The race for the EU presidency

### Blair for president?

Jan 17th 2008 | BRUSSELS  
From The Economist print edition

#### With French support

[Get article background](#)

IT TAKES a lot for an Englishman to speak French in public. Yet Tony Blair, who has made a habit of it, did it again on January 12th, delivering a speech in praise of reform and European unity to members of France's centre-right ruling party—all in respectable French. Commentators argued that only one prize could explain why the former British prime minister (and nominally centre-left politician) put himself through the ordeal. At the meeting, President Nicolas Sarkozy came close to giving explicit backing to Mr Blair to become the European Union's first full-time president.

Under the new Lisbon treaty, the EU's 27 members will be represented by a single figure, serving for two-and-a-half years. That replaces the system which sees countries take it in turns to chair EU meetings for six months. Hailing his guest as one of Europe's "great men", Mr Sarkozy called on Europe to "aim high", and not settle for a compromise figure. That certainly sounded like an endorsement, though Mr Sarkozy has also praised Jean-Claude Juncker, the chain-smoking Luxembourg prime minister, and dark master of the EU's arts.

Mr Sarkozy hopes the new chief will be chosen late this year, when France holds the club's rotating presidency. But that can happen only if the treaty is ratified by all 27 members during 2008: a long shot. Just as likely, the president will be chosen in a horse-trading marathon in 2009, which will also pick a head of the European Commission (roughly, the EU's bureaucracy) and a new foreign-policy chief.

Would Mr Blair get the job? Iraq counts against him. So does Britain's semi-detached EU status: it remains outside the single currency and has multiple opt-outs. Would Mr Blair want the job? Maybe not. A tussle looms over who will be the face of the EU abroad, the president or foreign-policy chief. If that fight goes the wrong way, the new president could languish in Brussels chairing dull summits. More fun to tour the world speechifying, in any language.

Charlemagne

## Roll up, roll up, get your energy here

Jan 17th 2008

From The Economist print edition

**Let them burn snake oil**

Illustration by Peter Schrank



IN EUROPE, policy packages are like patent remedies: if they promise to cure one or two ills, they might be worth a try; if a dozen, suspect quackery. On January 23rd the European Commission is to unveil a comprehensive energy policy that promises to curb climate change, increase energy security, shield economies from volatile fuel prices and foster new industries in which Europe will lead the world. The mandate for this monster comes from national leaders, who set themselves a string of ambitious but sketchy energy goals at a summit last March, the European Union's first after growing to 27 members. Beforehand, some people wondered how such a diverse group would agree about something as tricky as an energy policy. In the event, agreement came fast. The reason for that is now clear: like the finest snake-oil, the new policy promises something for everyone.

For countries worried about global warming, there is a target to reduce EU greenhouse-gas emissions by at least a fifth of their 1990 level before 2020. For countries less fussed about climate change (some ex-communist newcomers), the policy stresses independence from scary suppliers such as Russia, and asks the rich countries of old Europe to accept the lion's share of greenhouse-gas curbs.

Countries with lots of coal will doubtless be gratified by talk of clean coal plants, and of carbon capture and storage. Farmers get a potentially lucrative pledge that the EU will use biofuels for a tenth of its transport needs, as long as they are eco-friendly (fierce rows continue about how to judge that). For Europeans opposed to nuclear energy (the biggest source of low-carbon energy in the EU), the portmanteau places a huge bet on technologies such as wind and wave power, setting a target to triple Europe's overall use of renewable energies by 2020.

Countries determined to subsidise expensive forms of greenery (cloudy Germany loves solar panels, for some reason) will be allowed to carry on. This is sold as a punt on EU innovation, keeping a mix of technologies alive while waiting to see which will sell. The model is Denmark, which subsidised wind turbines for years and now makes a mint exporting them—never mind that wind power itself has to be subsidised.

For fans of market mechanisms, an existing European scheme for trading carbon-emissions quotas will be tightened up and a separate trading scheme created to set up a market in renewable power certificates among EU members. That would allow Britain—a crowded and expensive island with strong planning laws—to pay for new wind farms in Romania, say. With traded certificates, the power generated by Transylvanian windmills would be credited to Britain's renewables account, while Romania would get cash and clean electricity. Free-traders, in principle, ought to be pleased. Renewables such as windmills

promote trade and market integration by prodding governments to link up national grids, says Peter Brun of the Danish wind-energy firm, Vestas. Otherwise, on blustery days you risk swamping your own grid, and on calm days going short.

European officials predict that their policy will redistribute wealth to poor neighbours. These may include non-Europeans, as long as renewable energy produced by them is imported back to Europe. Thus Italy could build solar arrays in north Africa, as long as it laid undersea cables to bring back the electricity.

Europe has "so much to gain", enthuses a Eurocrat: energy security, jobs, technological gains, you name it. There will be new industries "to replace older industries that will increasingly have trouble surviving in a carbon-constrained environment".

But that is where the clashes start. The French president, Nicolas Sarkozy, complains that if EU policies drive heavy polluters to countries with laxer carbon regimes, that would be "neither efficient, nor fair, nor economically sustainable". To France, it is "indispensable" to fight back with import tariffs on goods from countries that resist binding curbs on greenhouse emissions (trade war, anyone?).

One minister says it is "stupid" to pin such high hopes on renewable energies, because boosting them is not the same thing as cutting carbon emissions. If Europeans want to have global impact, he says, they should invest heavily in clean coal technology. "There is no way you can sort out China with wind power."

## **Energy = much confusion, squared**

By far the loudest grumbling, though, is being prompted by specific targets that tell each government how big a slice of their energy mix must be renewable by 2020. Countries with feeble records on renewable energy (such as Britain) will be required to make astonishing leaps: in Britain, renewables are supposed to rise sevenfold, from less than 2% of the energy mix to around 14%. Class swots on renewable energy are just as cross, because past efforts have been ignored in setting new targets. Sweden, which currently gets about 40% of its energy from hydro power and so on, will be asked to find more than half its energy from renewables, pushing it into unknown territory at unknown cost.

For Connie Hedegaard, the Danish climate and energy minister, the commission's refusal to acknowledge past efforts is bad politics. Europe "should show that sometimes being a front-runner is worthwhile". Looking ahead, countries that miss targets should also visibly "pay in some way or other". After all, one of Europe's main problems, she argues, is that pledges are not kept, and policies are never implemented properly.

That, of course, is the problem with issuing so many pledges. The energy package pursues objectives that range, depending on your point of view, from the laudable and visionary to the quixotic and crazily expensive. The sheer length of the wish-list helped secure a deal last spring. But the multiple goals are a muddle. If Europe wants to show the world it is serious about climate change, its leaders need to agree which objectives really matter. If not, their energy policy may be beyond any remedy.



## Northern Rock

## Running out of time

Jan 17th 2008

From The Economist print edition

**After months of prevarication Gordon Brown must settle the bank's fate**

Illustration by David Simonds

[Get article background](#)

IF FINANCE were art, the slow-motion demise of Northern Rock would surely belong to the surrealist school. Magritte's enigmatic picture of a smoker's pipe, captioned "This is not a pipe", deserves pride of place at the mortgage lender's Newcastle head office. This is a bank, after all, that is supposedly still in private hands and solvent, even though it is propped up by breathtaking amounts of public money. The painting also merits a place at Downing Street, as ministers chase in diminishing circles to maintain the surrealist tease that "This is not a publicly owned bank".

An extraordinary—in both senses of the word—meeting of Northern Rock's shareholders on January 15th added a scene from the theatre of the absurd. Held at Newcastle's Metro Radio Arena, which was playing host later in the week to the "Ultimate Fighting Championship", the meeting was an attempt by two hedge funds, which own 18% of the bank, to assert shareholders' interests. Their goal was to restrict the board's ability to resolve Northern Rock's difficulties by issuing new shares or selling assets. In the event, only one of their four resolutions was adopted.

Even as shareholders voted, however, the stockmarket was passing judgment on their brazen assumption that they were still in charge. In February last year Northern Rock's share price touched £12.58 (\$24.77), valuing the bank at more than £5 billion; on the day of the meeting the price fell by 16% to 69p. And with reason. Shareholders' shrivelled equity is now worth less than £300m, whereas public financial backing for Northern Rock—£25 billion in lending by the Bank of England and another £30 billion in Treasury guarantees—totals £55 billion. Taxpayers' total exposure amounts to at least half of Northern Rock's balance sheet.

By refusing to handcuff the bank's board, shareholders kept open the possibility of a private-sector rescue, which Alistair Darling, the chancellor of the exchequer, said again on January 15th was his preferred option. Yet that evening Gordon Brown, the prime minister, gave his strongest hint so far that Northern Rock might be nationalised. Its share price slipped further the following day.

The government faces this stark choice—between finding a fully financed private-sector saviour (which now looks increasingly elusive), taking the bank into public ownership or just letting it go bust—because

it failed to prepare for a banking belly-flop in a changed financial world. Not so long ago the Bank of England could have orchestrated a rescue by Britain's top banks. But today's more open and competitive financial environment requires a new way of dealing with banking emergencies.

Britain is the only country in the G7 club of leading economies without a special public mechanism for grabbing control of a failing bank and ensuring that depositors get their money without delay. The government is now planning to give such powers to regulators at the Financial Services Authority, but these will come too late to help Northern Rock. If it were to become insolvent, deposits could well be frozen despite the Treasury's guarantees.

This failure to reform before banking disaster struck is now costing the government dear. Private-sector saviours are proving thin on the ground. Several firms, including J.C. Flowers, an American private-equity company experienced in sorting out ailing financial institutions, initially expressed interest in this one. But only two contenders are still in the ring. One is a consortium led by Sir Richard Branson's Virgin Group, which would take a controlling interest in the bank. The other is Olivant Advisors, a private-investment firm headed by Luqman Arnold, formerly the boss of a rival bank, Abbey National. Olivant proposes taking a minority stake in Northern Rock and turning it around through better management.

Both would-be rescuers are stumbling over the same hurdle, however. Each has promised swift repayment to the Bank of England of a sizeable chunk of its lending: Virgin has promised £11 billion and Olivant between £10 billion and £15 billion. But the money must be borrowed to fulfil that pledge, and the financial crisis of the past few months has left banks both short of capital and leery of risk, especially as the mortgage market turns down.

Time is now running short. Mr Darling has set a deadline of February for any private-sector solution, in part because European Union approval for the current package of state support lasts for only six months. At the end of last year the Treasury asked Goldman Sachs, an investment bank, to explore whether it could raise the necessary private finance where others had failed. Goldman's apparent delay in presenting a final report suggests that it has been unable to crack the nut.



That leaves nationalisation as the only remaining remedy, and it is an unpalatable one. The government has been preparing the ground: on January 12th it emerged that Ron Sandler, who sorted out the Lloyds's of London insurance market a decade ago, will take charge of Northern Rock if it is nationalised. Taking the bank into public hands would nonetheless be politically embarrassing for Mr Brown, who has been as keen as Tony Blair for Labour to shed its reputation as the party of state ownership. And it would probably mean breaking one of his self-imposed fiscal rules, as at least half the bank's liabilities would move on to the public books. But where Northern Rock is concerned, a dose of realism is long overdue.

## Party-funding scandal

### Here we go again

Jan 17th 2008

From The Economist print edition

#### Political donations attract controversy once more

IF SEX was the richest source of scandal under the last Conservative government, money has taken its place under Labour. Its first major controversy, in 1997, involved a donation from Bernie Ecclestone, a motor-racing tycoon. Tony Blair's final year as prime minister was dogged by a police investigation into whether peerages had been offered in return for loans. Last November the party's general secretary resigned over donations received from a property developer through third parties.

The latest uproar involves Peter Hain, secretary of state both for Wales and for work and pensions. He campaigned last year for Labour's deputy leadership but came fifth of six candidates. On November 29th Mr Hain admitted that he had failed to register a £5,000 (\$9,800) donation to his campaign. Four days later, after it emerged that a gift in kind by another donor had not been declared either, he promised to study his records and produce a full list of undeclared donations. On January 10th he revealed that there were 17 of these, amounting to over £103,000.

Murkier still is the role played by an obscure think-tank, the Progressive Policies Forum (PPF), in channelling £55,000 to the campaign. Set up in December 2006, three months after Mr Hain said he would run for the post, it employs no staff and has published no research.

Mr Hain blames the failure to declare the donations on sloppy campaign staff, and notes that the money came from legal sources. But critics insist that an oversight on this scale is unforgivable in a politician entrusted with running two departments. Even more troubling, they say, is the PPF. Many assume the think-tank was used to mask the identity of donors, but Mr Hain says he was not involved in setting it up.

Mr Hain's future rests on the outcome of inquiries launched by the Electoral Commission (EC) and the parliamentary commissioner for standards. He is seen as a capable minister, but his vaulting ambition (his profligate campaign included an expensive full-page advertisement in a national newspaper) and lack of socialist roots (he was a Liberal before joining Labour) have denied him a base in the party. Support from the prime minister is also nuanced: on January 15th Gordon Brown absolved his minister of "corruption", attributing his mistake to "incompetence".

The Conservatives' own funding controversies have contained that party's glee at Mr Hain's troubles. It was revealed on January 14th that David Cameron, the Tory leader, had failed to declare to the EC three free flights in 2005 (though they were declared in the parliamentary Register of Members' Interests). The day before, George Osborne, the shadow chancellor, was hit by the revelation that he did not declare more than £487,000 in donations in the register (though he did to the EC). Donors had given the money to the Tories' central budget but expressed a wish that it be used to support Mr Osborne.

The cases are different. Mr Hain did not report his donations at all; Mr Osborne reported his to the EC, and it is not clear that they should have been declared in the parliamentary register as well. Guidance solicited from the registrar in December by the Tories' chief whip, Patrick McLoughlin, was taken to mean that the donations needed to be recorded only with the EC. The registrar then backtracked, prompting Mr McLoughlin to ask the Parliamentary Committee on Standards and Privileges on January 11th for clarification. But Labour MPs ask why the Tories waited 11 months after they began receiving the contributions to seek advice. The parliamentary commissioner for standards said on January 17th that he was investigating a complaint against Mr Osborne by two Labour MPs, who have also asked the EC to look into whether 80 Tory MPs have disclosed other types of donation properly.

A badly needed cross-party consensus on reforming political-party funding has yet to emerge. The latest controversies should prompt agreement at least on the need for simplicity, however. The parallel existence of the EC and the parliamentary register, each with its own rules, ensures confusion. The sex scandals of the 1990s may have been seedy, but they were rarely the result of a misunderstanding.



## Biofuels

## Sugar in the tank

Jan 17th 2008

From The Economist print edition

## Worries over biofuels could work to Britain's advantage

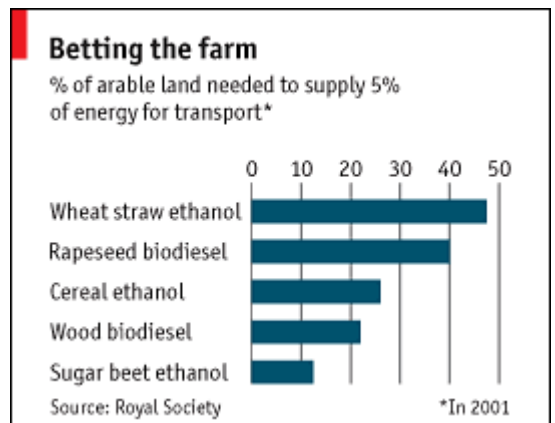
SIR RICHARD BRANSON, the bearded billionaire who founded Virgin Atlantic, is fond of surprises. Next month his airline plans to test-fly an aircraft that is partly powered by biofuels, something most experts thought was years away. From April Sir Richard's countrymen will begin filling their cars with a blend of petrol and biofuel, as part of the government's plan to ensure that 5% of Britain's transport runs on fuel made from plants by 2010.

Transport accounts for around 20% of Britain's planet-warming carbon emissions. In theory biofuels produce low net emissions of carbon dioxide, since burning them merely recycles atmospheric carbon absorbed by the plant as it was growing. Others like them for different reasons. Farmers hope that growing crops to put in petrol tanks will be more profitable than growing them to put on dinner tables, and the prospect of domestic production appeals to politicians who are worried about energy security.

Yet even as their star has risen at Westminster, biofuels have been raising doubts among greens. Friends of the Earth and Greenpeace, two environmental-lobbying groups, have given warning that biofuels may not be as eco-friendly as they seem. On January 14th a more august body took a similar line. The Royal Society, Britain's national science academy, published a report that analysed the bewildering range of biofuels on the market. It concluded that, thanks to carbon emissions from fertilisers and processing, some biofuels may cause more climate change than petrol. That raises the risk of a spectacular official own-goal: if targets encourage people to use the wrong sort of fuel, transport may get dirtier, not cleaner. The Royal Society wants ministers to specify targets not for biofuel consumption but for greenhouse-gas reduction. The government says it may do that after 2010.

Hopes that biofuels could boost farmers' income and improve energy security seem even more ephemeral. Dank, cloudy and small, Britain is ill-suited to mass production of the fast-growing crops favoured by the biofuel industry. For crops to provide even 5% of the fuel used in transport would require using huge swathes of arable land (see chart). "As far as actually growing things is concerned, I don't think it'll ever be big in Britain," says Lord Oxburgh, the head of D1 Oils, a biofuels firm.

Even if Britain can't farm its way to green transport, some businessmen hope to turn a profit on biofuels by drawing on more reliable British skills. The Royal Society argues for a strict worldwide certification system, similar to that used for eco-friendly wood, to let consumers know just how green a particular biofuel is. Developing such a system would require exhaustive analysis of every step of a firm's supply chain. That's just the sort of thing that the City's legions of auditors and accountants would be good at—if they can get countries such as America and Brazil, both fiercely protective of their indigenous biofuels industries, to agree.



## Children's television

## School's out

Jan 17th 2008

From The Economist print edition

## Why teenagers are losing out to younger viewers

BBC

[Get article background](#)

FOR fans, it is the biggest scandal since Gonch Gardner made off with Mr Bronson's toupee at the swimming pool. "Grange Hill", a BBC children's television drama about an inner-city school and its raucous pupils, is getting a makeover as it celebrates its 30th anniversary this year. Formerly stuffed with edgy teenage storylines—drugs, gangs, pregnancy and so on—the next series will instead follow a younger cast, pitching more innocent plotlines to an audience of under-12s. Blasphemy, according to the programme's creator, Phil Redmond, who says it would be better for the series to "hang up its mortar board".

The squeezing out of original programming for teenage viewers is one unexpected early consequence of the arrival of multi-channel digital television. Children are among the most eager adopters of digital TV, and now spend 82% of their viewing time on specialist digital channels rather than the old analogue five. Their parents are happy to indulge them: 90% of households with children have multi-channel television, against 76% of childless homes. More channels have meant lots more choice: some 113,000 hours of children's programmes were broadcast in 2006, compared with 20,000 in 1998.

But there is a catch: nearly all of this is either imported or repeated. By 2006 only 1% of children's broadcasting consisted of original material made in Britain. Increased competition for viewers from the new channels, as well as bans on advertising junk food during children's shows, has made it unprofitable to commission expensive new children's programmes. Britain's main commercial broadcasters have halved their investment in children's shows since 1998.

Pre-schoolers are getting the lion's share of what is left, partly because they are more likely to watch with their parents, whom advertisers will pay more to reach. The BBC, which is funded by a tax on households with televisions, has managed to increase its spending on children's programmes—yet it too seems to be focusing on younger kids. Its children's service, which used to cater for under-16s, was redefined in 2006 to attract under-12s away from competitors such as Disney and Nickelodeon. Programmes for older children, such as "Grange Hill", are having to soften their content accordingly. A new teenagers' brand, BBC Switch, was launched in October, but its output is slim and mainly on the web, where Beeb bosses reckon teenagers now lurk. The television-minded among the over-12s are increasingly left to watch adult-oriented programmes or imports for children.

Does it matter if young people come to consume almost exclusively television programmes that are made abroad? It might. "Grange Hill" and its ilk tackle awkward subjects that foreign series tend to shy away from, and in a British context that makes them more real to British children. And television helps to

mould national identity. Most Britons under 40 can remember “Grange Hill” teachers as vividly as their own, and in some circles few things garner more respect than a “Blue Peter” badge. (*The Economist*’s own Bagehot has one, though he is too modest to wear it.) Finally, exporting programmes is a form of soft power. Big Bird is more famous than Condoleezza Rice; Britain’s best ambassadors could well be the Teletubbies.



## Public-sector pay disputes

## The pedagogues are revolting

Jan 17th 2008

From The Economist print edition

## Teachers want more; everyone else wants what they are having

[Get article background](#)

AFTER a decade of generous pay rises, teachers found the three-year pay deal proposed on January 15th by Ed Balls, the schools secretary, distinctly underwhelming. On offer is 2.45% extra in 2008-09 and 2.3% in each of the following two years. This is far short of the 4% teaching unions had said they needed to keep pace with retail-price inflation—"in effect a pay cut", growled Steve Sinnott, who leads the National Union of Teachers. His executive will be meeting to discuss the offer next week and he expects a "robust response".

The teaching unions' response may be robust; their actions are likely to be less so. The deal was better than teachers feared it might be. Gordon Brown had called for pay restraint; a "difficult year" for the public purse, said the chancellor, Alistair Darling. He urged public-sector pay deals of 2%, the government's target for consumer-price inflation, its preferred measure.

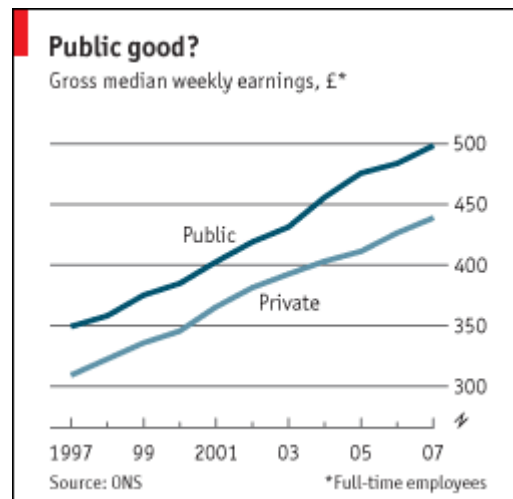
And teachers are doing well: their median pay has risen by almost a fifth in real terms over the past decade; most can retire on a full, final-salary pension at 60; and holidays are longer than in almost any other job. Another fact the unions do not tend to point out when making comparisons with the private sector, or sweeping statements about pay cuts, is that in any given year half of all teachers get much more than the headline deal. This is because they move up the teachers' pay scale, which boosts their pay packet by another £1,000 or so. And then there are the sweeteners that have proliferated in recent years: retention allowances; golden hellos in shortage subjects; performance-related bonuses; extra payments for pastoral duties or for working in the big smoke.

Although teachers may (just about) have been bought off, their pay offer could backfire on the government by causing anger in other parts of the public sector, where disputes over last year's pay settlements are turning into running battles. The bodies reviewing pay for police, prison officers and nurses all recommended rises of 2.5% in 2007. Unaffordable, said Mr Brown, and phased in the awards, with a mere 1.5% added to salaries for the first six months and an additional 1% afterwards, bringing their value down to 1.9% overall.

Nurses grumbled, and secured some concessions—only in England was the award not eventually paid in full—but concern about patients' welfare meant that their hands were tied. Prison officers were less quiescent. They pulled out of a voluntary no-strike agreement in protest, and at some prisons held wildcat strikes—the first in their association's 68-year history. The justice secretary, Jack Straw, has threatened to make it illegal for prison officers to strike unless the agreement is reinstated.

Angriest of all are the police. Historically, the ban on police strikes has been rewarded by the government's willingness to honour the recommendations of the body that reviews their pay. The Police Federation plans a protest rally in Westminster on January 23rd and a ballot of members on whether they want the right to strike. "I have no doubt the teachers' ability to take strike action influenced the government's decision to pay in full the recommendation of their pay-review body," says Jan Berry, the chairman of the federation. More than 200 MPs, mostly Labour backbenchers, have signed a House of Commons motion calling for the government to give police officers the 2.5% increase in full.

On January 16th the government published the recommendations of yet another pay review—this time the one that looks at MPs' salaries. The country's elected representatives are worth 2.56% more than last



year, it said. Mr Brown demurs. He wants his right honourable friends to set an example to all public servants and settle for a more modest 1.9%, paid in two stages. But he cannot force them to do so: MPs have a free vote on their own pay (although not for much longer, as the government has asked a senior civil servant to recommend a less inflammatory alternative).

That vote is due to be held on January 24th. Its result—far more than a fraction of a percentage point for teachers or police officers—will set the tone for pay negotiations right across the public sector.

**Equality v jobs****Robbing Peter to pay Pauline**

Jan 17th 2008

From The Economist print edition

**Equality for low-paid women means some will lose their jobs**

IT IS not just teachers' pay that is putting pressure on school budgets as government largesse runs out. An attempted raid on school reserves in the name of sexual equality could make things worse. For years councils have paid cleaners, dinner ladies and teaching assistants less than men for jobs that are now regarded as requiring similar skills. That will no longer be possible.

The saga started in 1997, when local councils thrashed out an agreement with unions to review wages and start paying workers in female-dominated jobs as much as those in male-dominated ones. (School cleaners, for example, mostly women, have long earned less than street cleaners, who are mostly men.) The process was supposed to have been finished by mid-2007, but fewer than half of all councils had completed even their reviews by the year's end.

Some 700,000 local-government workers have probably been treated unfairly. Closing the gap in wages and reaching some agreement about the six years of back pay to which women may be entitled will cost councils at least £3 billion, says the Local Government Association. The bill could be even higher if it proves impossible to negotiate union-wide deals. Large numbers of women might then go to employment tribunals: 50,000 cases are waiting to be heard.

The battle has pitched union sisters against their brothers. Some of the latter will see their pay reduced to match that of women doing comparable jobs. One group of women has already taken their union to a tribunal, alleging that a desire to protect men's jobs and pay led it to pull its punches in talks with councils. They lost, but no-win, no-fee lawyers are touting for more such business.

Other natural alliances have also frayed. On January 14th the Equality and Human Rights Commission withdrew its support for another set of women who want the council they work for to equalise pay right away, rather than protecting men's pay and closing the gap gradually. Further support for their case would be "throwing petrol on this legal forest fire", says the commission's boss, Trevor Phillips.

Whitehall has washed its hands of the problem. It has allowed councils to borrow more than normal to help them pay, although nowhere near enough to cover the bill. So, noting that schools employ around 30% of the staff in line for compensation, councils are eyeing schools' reserves covetously. Head teachers are outraged. Most reserves are earmarked for refurbishments, they say, and it was councils, not schools, that set the discriminatory pay rates.

With teachers' pay protected by national agreements and a legal requirement to put a trained teacher in front of every class, other staff will have to bear the brunt of school funding cuts. Some low-paid women may get their compensation along with their redundancy notices. And if the number of teaching assistants plummets, so too will any hope for education that is truly "personalised" to suit each child.

## Sprucing up cities

## The regeneration game

Jan 17th 2008

From The Economist print edition

## Why cities' plans for renewal often sound strangely familiar

A STROLL through the centre of most British cities is much prettier now than it was a decade ago. Though output in the north has grown more slowly than elsewhere, its cities have beautified themselves: *boulevards* and public sculpture liven up formerly deserted bits of Leeds; the seafront at Hull boasts a futuristic new aquarium. A year of civic jollification has just begun in Liverpool, named "European Capital of Culture 2008" and given a big dollop of European Union cash. This week Sheffield presented plans for a new high-tech "digital square mile", complete with suitably jazzy new buildings.

The cranes on provincial skylines are encouraging. But followers of regeneration, as the business of boosting down-at-heel neighbourhoods is now known, might notice that many cities seem to be thinking alike. Sheffield's digital square mile will complement what neighbouring Leeds calls its own "digital cluster"; over the Pennines, Salford is beavering away on a "digital-industries hub". And though Liverpool is the official capital of culture, places such as Gateshead (where the huge Baltic flour mill is now an arts centre) and Wakefield (which is due to open a new Barbara Hepworth gallery in the winter of 2009) have similar hopes.

Why do city councils have the same ideas about how to grow? One reason is that they have the same people advising them. Since Labour moved regeneration up the agenda in 1997, creating a spider's web of regional-development bodies and arming them with cash to dish out, a regeneration-consulting industry has sprung up. *Regeneration & Renewal*, a weekly trade magazine, lists scores of organisations happy to advise councils on how to bid for, and spend, the money. Following the advice of one such consultant, Sheffield now wants to club together with Leeds and Manchester to form a single "super-city". Last year the same outfit advised Glasgow and Edinburgh, which are engaged in a similar collaborative effort.

If consultants can spread good ideas and not just recycle tired ones, so much the better. But the homogeneity of city-development strategies also owes much to the British government's enduring top-down approach to local government. In England a great deal of regeneration work is steered by nine Regional Development Agencies (RDAs), whose members are appointed by, and report to, central government. This has encouraged uniformity: "Once a minister identified a sector as important, it tended to trigger a herd mentality among RDAs," says Dermot Finch of the Centre for Cities, a think-tank. Following a minister's remarks about the brilliance of creative industries a few years ago, every regional agency began overstating the contribution of the creative sector to its economy. Other notable recent fads include biotechnology, financial services and exploiting the 2012 Olympics.

But the RDAs are getting less herd-like, Mr Finch reckons, and local authorities are being given a bit more freedom. So far, cities have tended to follow the lead of regional agencies, partly because they hold important purse strings, but also because cities are inexperienced at making their own assessment of the best way to grow. The Treasury has spotted this problem, and in July proposed that local authorities should be forced to spend more time examining the needs of their economies, in return for being given more say over how cash is spent. With luck, better-tailored, more varied strategies might emerge. Having long promoted regional agencies as the best means of regenerating deprived areas, it would be good if the government put some power back into the hands of the regeneratees themselves.

Bagehot

## The Scottish Obama

Jan 17th 2008

From The Economist print edition

**The link between British and American politics is less obvious than it looks**

Illustration by Steve O'Brien



THE British attitude to America tends to oscillate between snootiness and awed self-deprecation. In the past few weeks, the political class has opted for a collective swoon. Like threadbare housewives dreaming of American nylons after the war, MPs and others have gazed covetously at the televised primaries, with their drama, diverse candidates and balloons. "There is an unpredictability, optimism and openness," laments one columnist, "that many on this side of the Atlantic will envy." In short: we laughed, we cried, it was better than "The West Wing".

The self-flagellation has often been accompanied by another humbling idea: that the outcome of the presidential election will influence, even somehow determine, the course of British politics too. "If you want to predict Britain's political future," advises another commentator, "just look at America." This starstruck fatalism is mistaken. American politics does not supply an automatic pattern or prophecy for Britain—and it never has.

## Never have been slaves

The argument that it now does relies in part on an analogy between the two main Democratic contenders, on one hand, and Gordon Brown and David Cameron, the Tory leader, on the other. There is something to it: like Hillary Clinton, the prime minister is a kind of political dynast, having inherited his premiership from his long-term political partner; his pitch, like hers, rests on his avowed experience. The other, slightly less convincing part of the analogy sees Mr Cameron, with his relative youth, relatively gifted oratory and intermittent hope-mongering, as a sort of Etonian Obama. Mr Cameron encouraged the comparison before New Hampshire; since then he has been enthusiastic about John McCain and Mrs Clinton too.

The parallel is superficially plausible because post-war American and British politics have indeed tended to mirror each other. Bill Clinton and Tony Blair; Reagan and Margaret Thatcher; before them, Eisenhower and Macmillan, and JFK and Wilson: the two countries' political cycles have often overlapped, and like-minded leaders (albeit less schmaltzy in Britain) have coincided. There is a longstanding transatlantic trade in tactics and policy ideas, and in consultants, pollsters and other political mountebanks. Mr Brown and his fellow New Labourites are known to have studied Mr Clinton's victorious 1992 campaign; but the phenomenon goes back at least to the influence of Nixon's 1968 advertising on the Tories. (It is not exclusively west-to-east: witness the Tory-influenced Republican attacks on Mr

Clinton in 1992, and, maybe, the speech his wife made on a John Major-esque soapbox in New Hampshire.)

But the relationship is not—as some comment implies—a causal one. Mr Clinton's rise did not cause Mr Blair's; Mrs Thatcher's election did not determine Reagan's. Rather, both sets of leaders emerged from political circumstances (the cold war and its end, economic turbulence) that were themselves similar. Quite apart from the doubtful idea that in Britain posh is the new black, the main reason the latest analogies don't work is that, socially and politically, Britain and America have diverged.

To simplify, Britain has not had George Bush. The issues dominating the primaries—how to get out of Iraq; how to revive the country's reputation; how to govern less divisively—don't resonate in the same way in Britain. The underlying social rifts—between religious and secular voters, and over the culture wars that began in the 1960s—do not apply. The '60s happened in Britain too, but most people were inside having a cup of tea.

So, perhaps temporarily, British and American politics have decoupled. Insofar as there is a superficial resemblance, it may be because American parties face imperatives of a kind that British ones have already confronted. As the enthusiasm of some Conservatives (the “Obamacons”) for Mr Obama suggests, the old correspondence between the Tories and the Republicans has broken down—but it seems likely that the Republican Party, as a number of its members are already urging, will have to embrace environmentalism and cuddly economics as the Tories were forced to. Look closely at the Democrats, meanwhile, and they seem to be promising more or less what Labour has been offering: capitalism with a more human face, better health care and so on. A facetious observer might describe Mr Brown as the Scottish Obama—or Mr Obama as “the Black Gordon”.

As for the idea that Britain could use more of that American drama: it is true that more town-hall meetings and debates among leaders, and open “primaries” in constituencies, would enliven elections. But the reality is that Britain's parliamentary system, in which voters face narrower choices, can never replicate the thrills and surprises of presidential campaigns.

However, another complaint made by the starstruck—that British politicians are boringly homogeneous—is unfair. Britain's history, like its political system, is different from America's: in particular, race is not the schismatic issue in Britain that slavery and segregation make it in America. But class plays something like the same historical role—and from a class perspective, Britain's recent leaders have been impressively eclectic. Mr Major's father was a circus artist; Lady Thatcher (who, to remind, is also a woman) was the daughter of a shopkeeper. Mr Cameron is the poshest leader the Tories have dared to pick for more than 40 years, so far has anti-toff prejudice (see Etonian references above) replaced the old upper-crust hegemony. Meanwhile another minority—Mr Brown's Scots—is now as over-represented in government as the toffs once were.

So, Bagehot submits, Britain has had its quiet equivalents of the Mormon, Evangelist, war hero, woman and black candidates who are currently on tour in America. But then, as American visitors may have noticed, occasional jingoistic spasms such as this one are as characteristic of the British as self-deprecation.



## Measuring liberty

## When freedom stumbles

Jan 17th 2008

From The Economist print edition

**Civil and democratic rights are in retreat, says an organisation with strong, though not uncontested, views on the matter**

AP



OVER the past half century, it often seemed that the advance of democracy and basic freedoms—the right to speak and write without fear of persecution, to demand political change, and so on—was ineluctable. First the Europeans let their colonies go. Then the Soviet empire fell, and with it the communist monopoly on power in eastern Europe. And apartheid ended in South Africa.

Recently, though, freedom's progress may have come to a halt, or even gone into reverse. That, at least, is the conclusion of Freedom House, an august American lobby group whose observations on the state of liberty are a keenly watched indicator. Its report for 2007 speaks of a "profoundly disturbing deterioration" in the global picture, with reversals seen in 38 countries—nearly four times as many as are showing any sign of improvement.

Using the think-tank's long-established division of the world into "free", "partly free" and "not free" countries, the planet is still a better place than it was a quarter-century ago. In other words, there are still net gains from the fall of communism, at least in central Europe, and the decline of militarism in Latin America. But the short-term trends seem worrying. Last year was the second in a row when liberty, as defined by Freedom House, inched back.

An especially disturbing sign, says the organisation, is the number of countries in all regions of the world where a previously hopeful trend has gone into reverse. They include Bangladesh (where the armed forces took over last year), Sri Lanka (whose civil war flared up) and the Philippines. Other backsliders included Nigeria and Kenya, accounting for more than one sub-Saharan African in four between them, plus the Palestinian territories and Lebanon. In both Georgia and Kyrgyzstan, former Soviet republics whose "colour revolutions" were warmly encouraged by Freedom House, there was regression. Only two countries, Thailand and Togo, made a clear leap forward last year, going from "not free" to "partly free".

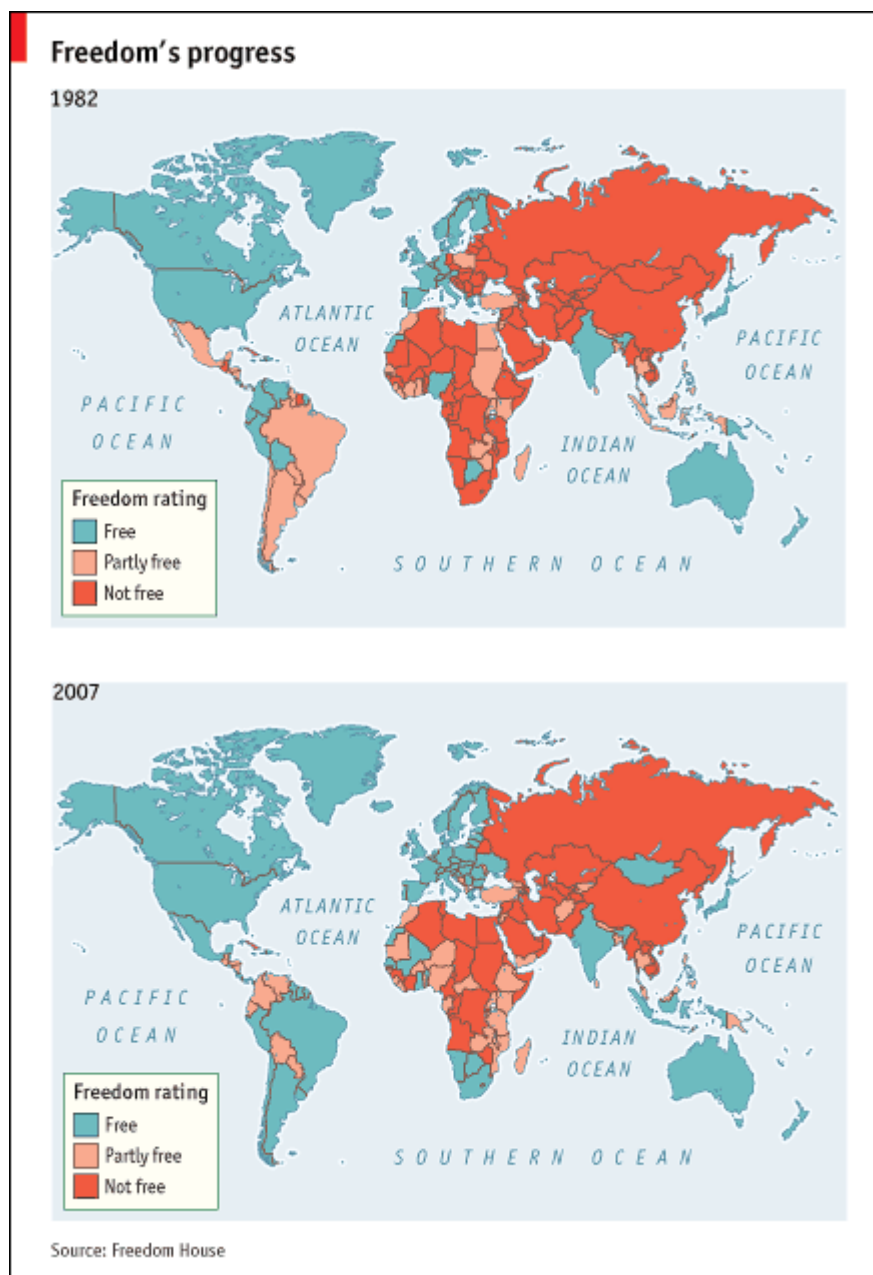
No country joined the top "free" group, and a total of 43 countries, representing 36% of the world's population, now languish in the "not free" group. None of the eight "worst of the worst"—Cuba, Libya, North Korea, Myanmar, Somalia, Sudan, Turkmenistan and Uzbekistan—was credited with any sign of improvement.

Of course, not all the targets of Freedom House's ire will feel embarrassed by their low scores. For example, Cuba's envoys to the United Nations have angrily denounced the organisation as a blatant



instrument of “interventionist activities” by dark forces in Washington. And in slightly more respectable quarters (on America's academic left, for example) the analysts at Freedom House have been criticised for hewing too close to their home country's foreign policy.

So where exactly does Freedom House come from? It was founded in 1941 by Wendell Willkie and Eleanor Roosevelt, as a counter to Nazism. During the cold war it “fought the good fight” against Soviet-backed tyrannies but also had harsh words for dictators on America's side of the stand-off. At least in American terms, its bosses and trustees have covered a broadish range of Republicans and Democrats. James Woolsey, a former CIA director, once served as its chairman. Past trustees have included Donald Rumsfeld, an ex-defence secretary, and Paul Wolfowitz, another Republican luminary who held high office at the Pentagon. But board members have also included Lane Kirkland, a Democrat who led America's labour movement for 16 years.



Freedom House not only watches the state of liberty, it also calls itself a “catalyst” for the peaceful advancement of civil and democratic rights through “analysis, advocacy and action”. But it has firm ideas about which country is best placed to promote these ideals: it has formally stated that whatever their differences, all trustees are agreed that “American leadership in international affairs is essential to the cause of human rights and freedom.” When America attacked Iraq in 2003, Freedom House wished the campaign well.

Nor does the organisation conceal its financial ties to the American government, which supplies about 80% of its income. But it strongly denies that it acts as an arm of the government, or that it holds back from criticising America and its friends when that is warranted. And it would be hard to argue that

diplomatic friendship with the United States has ever guaranteed a country a free pass from the think-tank. Israel, a close American friend, used to get relatively poor grades—a 2 for political rights and a 3 for civil liberties on a descending scale of 1 to 7. In recent years, Israel has improved its scores, but only in 2005 did its civil-liberty rating rise to 2.

Japan, another American ally, has also struggled to keep up its grades at Freedom House. Having started with a 2 for political rights and a 1 for civil liberties, it got top marks throughout the 1980s, only to slip back to a grade 2 in both categories in the early 1990s. Since 1995, it has been getting a grade 1 for political rights, but still only a 2 for civil liberties. Meanwhile some of America's strategic allies, such as Saudi Arabia, Pakistan and Egypt, have seen virtually no rise in their ratings since the September 2001 terrorist attacks despite their role as partners in the “war on terror”. All have continued to languish at or near the bottom of the pile.

Insiders say that in years past, there was some internal debate at Freedom House over whether or not economic welfare, which affects the range of choices people can make, should be included in the calculus of liberty. But the decision has been to keep economic factors out. This helps to explain why China, in the midst of the horrors of its Cultural Revolution when the surveys began, has hardly managed to improve on its early, rock-bottom ratings. Its “civil liberties” are still assessed at a dismal 6.

Russia, too, has been rated on the basis of its worsening human and political rights with no account taken of rising living standards. It was awarded a relatively good 3 for both political rights and civil liberties in 1991, bringing it within a whisker of membership of the “free” group, but is now locked again in the “not free” camp.

How much freer do people feel when they have a few roubles or yuan in their pocket (and access to other goodies like computers and compact discs)? That is an endlessly debatable question. By contrast the sort of liberties and non-liberties measured by Freedom House (multi-party elections, due process and so on) are relatively tangible and easy to assess. That alone may be quite a good argument for having at least one index whose stated purpose is to assess formal freedoms—to vote, speak, assemble and so on. That does not imply that other factors, such as prosperity, have no bearing on how free people feel.

In any event, critics of Freedom House will soon have fresh material which they can test for pro-American bias: a special report on civil liberties in the United States is to be published, probably in March.

## The World Bank

## Lin's long swim

Jan 17th 2008

From The Economist print edition

## An economist with an unusual past

THIRTY years ago China's leaders used to call the World Bank a tool of imperialism. Now China is one of the bank's top borrowers, and in December it became a donor, on a small scale.

China may soon make a big contribution to the bank's intellectual ranks. According to whispers at the institution, its new chief economist will be a Chinese citizen. Justin Yifu Lin is the director of the China Centre for Economic Research at Peking University. He has twice won his country's top economic honour, the Sun Yefang award, and he has published in the leading journal of his profession, the *American Economic Review*. But this brilliant record masks an unlikely past. He was born not in China but in Taiwan. He defected to the mainland after serving in the Taiwanese armed forces.

After earning a master's degree in political economy from Peking University, at a time when it was still steeped in Marxism, he earned an economics doctorate from the University of Chicago, where the market reigns. So his intellectual portfolio is perfectly hedged. That will serve him well in his new post. His adopted land has become an inspiration to many poor countries, especially in Africa. Their policymakers argue that China's path to prosperity defies and discredits the simple formulas propagated in Washington.

Mr Lin is a student of China's economic reforms. But his scholarship, like his past, straddles ideological gaps. He believes governments go wrong when they defy the law of comparative advantage, promoting heavy industries in countries where capital is scarce and labour abundant. The government's first duty, he argues, is "to remove all possible obstacles for the function of free, open and competitive markets". Spoken like a Chicago man.

But Mr Lin also says government has a second duty. As an economy develops, the state should coax firms into more sophisticated industries. This prodding may be needed for several reasons. To cite one: firms may not know which industries are viable, and which are not. So the government should subsidise pioneers who break a path for others.

Washington's financial institutions were once notorious for their dogmatic prescriptions. Now they prefer piecemeal reforms and eclectic advice. That is a tide Mr Lin can probably swim with.

## Broadband

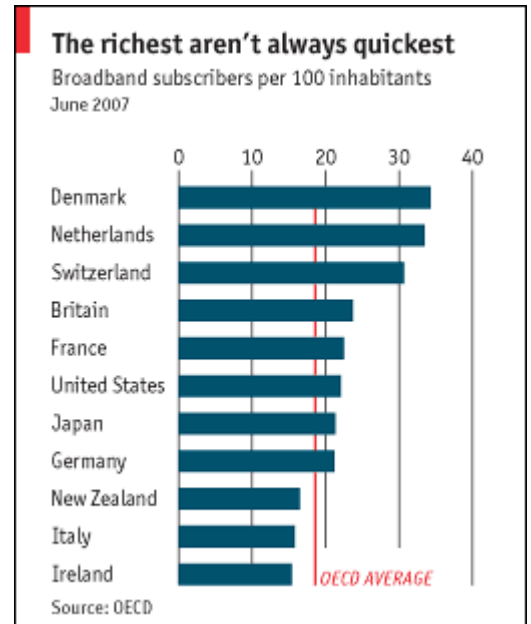
## Open up those highways

Jan 17th 2008 | TOKYO  
From The Economist print edition

## Rapid internet services are a boon. But not all regulators understand them

IN ERAS past, economic success depended on creating networks that could shift people, merchandise and electric power as efficiently and as widely as possible. Today's equivalent is broadband: the high-speed internet service that has become as vital a tool for producers and distributors of goods as it is for people plugging into all the social and cultural opportunities offered by the web.

Easy access to cheap, fast internet services has become a facilitator of economic growth and a measure of economic performance. No wonder, then, that statistics show a surge in broadband use, especially in places that are already prosperous. The OECD, a rich-country club, says the number of subscribers in its 30 members was 221m last June—a 24% leap over a year earlier. But it is not always the most powerful economies that are most wired. In Denmark, the Netherlands and Switzerland, over 30% of inhabitants have broadband. In America, by contrast, the proportion is 22%, only slightly above the OECD average of just under 20%.



In terms of speed, Japan leads the world. Its average advertised download speed is 95 megabits per second. France and Korea are ranked second and third, but are less than half as fast, and the median among OECD countries is not much more than a tenth. America's average speed is supposed to be a bit above the median, but most users find that it isn't, or that the faster speeds are vastly more expensive. A New Yorker who wants the same quality of broadband as a Parisian has to pay around \$150 more per month.

What accounts for the differences among rich countries? Two or three years ago demography was often cited: small, densely populated countries were easier to wire up than big, sparsely inhabited ones. But the leaders in broadband usage include Canada, where a tiny population is spread over a vast area. The best explanation, in fact, is that broadband thrives on a mix of competition and active regulation, to ensure an open contest.

A lack of competition-boosting oversight is one reason for the poor record of the United States (and indeed for New Zealand, another unexpected laggard). Most Americans have a choice of only two broadband providers, either a telecoms or a cable operator. This virtual duopoly suits both sorts of provider, and neither has raced to offer its customers faster access. In some American states, prices have risen; in most other countries they have dropped.

In theory, America's 1996 Telecoms Act obliged operators to rent out their lines to rivals; in practice, a regulatory decision and then a court ruling (in 2003 and 2004 respectively) have made it easy for operators to keep competitors out. The supposed aim of these decisions was to force new firms to build their own infrastructure, instead of piggybacking on facilities set up by older outfits. But new entrants have found it hard to join the fray.

In any event, those American rulings may have been based on a faulty idea of how competition works in this area. As Taylor Reynolds, an OECD analyst, puts it, innovation usually comes in steps: newcomers first rent space on an existing network, to build up customers and income. Then they create new and better infrastructure, as and when they need it.

In France, for example, the regulator forced France Télécom to rent out its lines. One small start-up firm benefited from this opportunity and then installed technology that was much faster than any of its rivals'. It won so many customers that other operators had to follow suit. In Canada, too, the regulator mandated line-sharing, and provinces subsidised trunk lines from which smaller operators could lease capacity to provide service.

In South Korea, where half the population lives in flats, each block owns its own internal cabling and allows rival operators to put their equipment in the basement; each tenant then chooses which to use. In Japan, politicians put pressure on the dominant operator, NTT, to connect people's homes by high-speed fibre lines. And this week the communications ministry indicated that it will make NTT open those fibre connections to rivals.

As broadband grows more popular, the political mood may change in many countries. At present, consumers are often misled by the speeds that operators promise to deliver. Soon regulators can expect to face pressure to ensure truth in advertising, as well as to promote easier access.

Pressure will also come to correct another problem: most operators cap the amount of traffic users may send and receive each month, and nearly all provide far less speed for sending than for receiving. In other words, broadband doesn't really offer a two-way street. This will matter more as users turn into creators of content, from videos to blogs, and ask to be treated with due respect.

## Just good business

Jan 17th 2008

From The Economist print edition

**Corporate social responsibility, once a do-gooding sideshow, is now seen as mainstream. But as yet too few companies are doing it well, says Daniel Franklin (interviewed [here](#))**

Illustration by Ian Whadcock



IN THE lobby at the London headquarters of Marks & Spencer, one of Britain's leading retailers, the words scroll relentlessly across a giant electronic ticker. They describe progress against "Plan A", a set of 100 worthy targets over five years. The company will help to give 15,000 children in Uganda a better education; it is saving 55,000 tonnes of CO<sub>2</sub> in a year; it has recycled 48m clothes hangers; it is tripling sales of organic food; it aims to convert over 20m garments to Fairtrade cotton; every store has a dedicated "Plan A" champion.

The M&S ticker says a lot about the current state of what is commonly known as corporate social responsibility (CSR). First, nobody much likes the CSR label. A year ago M&S launched not a CSR plan but Plan A ("because there is no Plan B"). The chief executive's committee that monitors this plan is called the "How We Do Business Committee". Other companies prefer to describe this kind of thing as "corporate responsibility" (dropping the "social" as too narrow), or "corporate citizenship", or "building a sustainable business". One Nordic executive glories in the job title of director, accountability and triple-bottom-line leadership. All this is convoluted code for something simple: companies meaning (or seeming) to be good.

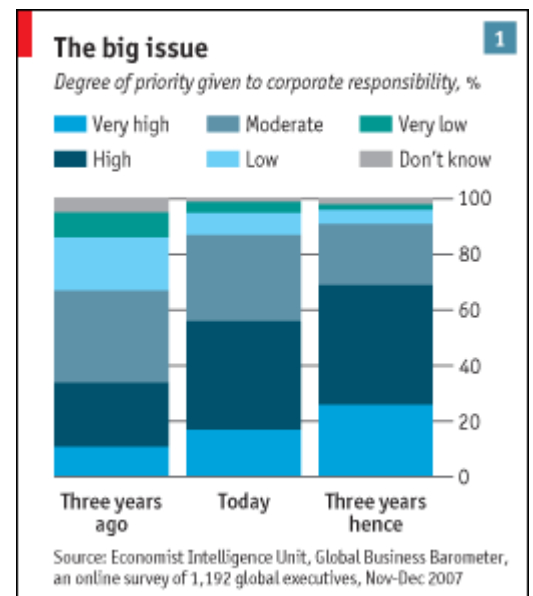
Second, the scrolling list shows what a vast range of activities now comes under the doing-good umbrella. It spans everything from volunteering in the local community to looking after employees properly, from helping the poor to saving the planet. With such a fuzzy, wide-ranging subject, many companies find it hard to know what to focus on.

Third, the M&S ticker demonstrates that CSR is booming. Whether through electronic screens, posters or glossy reports, big companies want to tell the world about their good citizenship. They are pushing out the message on their websites and in advertising campaigns. Their chief executives queue up to speak at conferences to explain their passion for the community or their new-found commitment to making their company carbon-neutral. A survey carried out for this report by the Economist Intelligence Unit, a sister company of *The Economist*, shows corporate responsibility rising sharply in global executives' priorities (see chart 1).

None of this means that CSR has suddenly become a great idea. This newspaper has argued that it is often misguided, or worse. But in practice few big companies can now afford to ignore it.

Beyond the corporate world, CSR is providing fertile ground for think-tanks and consultancies. Governments are taking an ever keener interest: in Britain, for example, the 2006 Companies Act introduced a requirement for public companies to report on social and environmental matters. And the United Nations promotes corporate responsibility around the world through a New York-based group called the Global Compact.

Business schools, for their part, are adding courses and specialised departments to keep their MBA students happy. "Demand for CSR activities has just soared in the past three years," says Thomas Cooley, the dean of New York University's Stern Business School. Bookshelves groan with titles such as "Corporation Be Good", "Beyond Good Company" and "The A to Z of Corporate Responsibility".



Why the boom? For a number of reasons, companies are having to work harder to protect their reputation—and, by extension, the environment in which they do business. Scandals at Enron, WorldCom and elsewhere undermined trust in big business and led to heavy-handed government regulation. An ever-expanding army of non-governmental organisations (NGOs) stands ready to do battle with multinational companies at the slightest sign of misbehaviour. Myriad rankings and ratings put pressure on companies to report on their non-financial performance as well as on their financial results. And, more than ever, companies are being watched. Embarrassing news anywhere in the world—a child working on a piece of clothing with your company's brand on it, say—can be captured on camera and published everywhere in an instant, thanks to the internet.

Now comes concern over climate change, probably the biggest single driver of growth in the CSR industry of late. The great green awakening is making company after company take a serious look at its own impact on the environment. It is no surprise, therefore, that 95% of CEOs surveyed last year by McKinsey, a consultancy, said that society now has higher expectations of business taking on public responsibilities than it did five years ago.

Investors too are starting to show more interest. For example, \$1 out of every \$9 under professional management in America now involves an element of "socially responsible investment", according to Geoffrey Heal of Columbia Business School. Some of the big banks, including Goldman Sachs and UBS, have started to integrate environmental, social and governance issues in some of their equity research. True, the finance industry sends mixed signals: it demands good financial results above all else, and in parts of the financial world—notably the private-equity part—scepticism on CSR still runs deep. But private equity itself is having to respond to public pressure by agreeing to voluntary codes of transparency.

As well as these external pressures, firms are also facing strong demand for CSR from their employees, so much so that it has become a serious part of the competition for talent. Ask almost any large company about the business rationale for its CSR efforts and you will be told that they help to motivate, attract and retain staff. "People want to work at a company where they share the values and the ethos," says Mike Kelly, head of CSR at the European arm of KPMG, an accounting firm.

## Too much of a good thing?

Since there is so much CSR about, you might think big companies would by now be getting rather good at it. A few are, but most are struggling.

CSR is now made up of three broad layers, one on top of the other. The most basic is traditional corporate philanthropy. Companies typically allocate about 1% of pre-tax profits to worthy causes because giving something back to the community seems "the right thing to do". But many companies now feel that arm's-length philanthropy—simply writing cheques to charities—is no longer enough. Shareholders want to know that their money is being put to good use, and employees want to be actively involved in good works.



Money alone is not the answer when companies come under attack for their behaviour. Hence the second layer of CSR, which is a branch of risk management. Starting in the 1980s, with environmental disasters such as the explosion at the Bhopal pesticide factory and the *Exxon Valdez* oil spill, industry after industry has suffered blows to its reputation. Big pharma was hit by its refusal to make antiretroviral drugs available cheaply for HIV/AIDS sufferers in developing countries. In the clothing industry, companies like Nike and Gap came under attack for use of child labour. Food companies face a backlash over growing obesity. And “Don’t be evil” as a corporate motto offers no immunity: Google was one of several American technology titans hauled before Congress to be grilled about their behaviour in China.

So, often belatedly, companies respond by trying to manage the risks. They talk to NGOs and to governments, create codes of conduct and commit themselves to more transparency in their operations. Increasingly, too, they get together with their competitors in the same industry in an effort to set common rules, spread the risk and shape opinion.

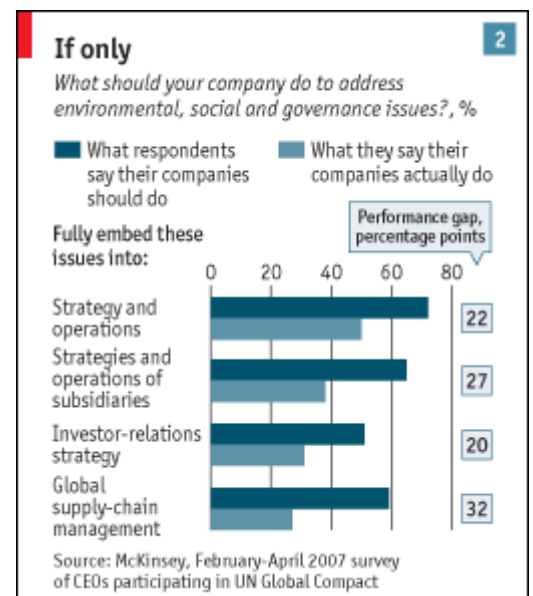
All this is largely defensive, but companies like to stress that there are also opportunities to be had for those that get ahead of the game. The emphasis on opportunity is the third and trendiest layer of CSR: the idea that it can help to create value. In December 2006 the *Harvard Business Review* published a paper by Michael Porter and Mark Kramer on how, if approached in a strategic way, CSR could become part of a company’s competitive advantage.

That is just the sort of thing chief executives like to hear. “Doing well by doing good” has become a fashionable mantra. Businesses have eagerly adopted the jargon of “embedding” CSR in the core of their operations, making it “part of the corporate DNA” so that it influences decisions across the company.

With a few interesting exceptions, the rhetoric falls well short of the reality. “It doesn’t go very deep yet,” says Bradley Googins, executive director of the Boston College Centre for Corporate Citizenship. His centre’s latest survey on the state of play in America is called “Time to Get Real”.

There is, to be fair, some evidence that companies’ efforts are moving in a more strategic direction. The Committee Encouraging Corporate Philanthropy, a New York-based business association, reports that the share of corporate giving with a “strategic” motivation jumped from 38% in 2004 to 48% in 2006. But too often corporate strategy is not properly joined up. In the car industry, Toyota has led the way in championing green, responsible motoring with its Prius hybrid model, but it has lobbied with others in the industry against a tough fuel-economy standard in America. Surveys point to a big gap between companies’ aspirations and their actions (see chart 2). And even corporate aspirations in the rich world lag far behind how much the public expects business to contribute to society.

According to Mr Porter, despite a surge of interest in CSR, in most cases it remains “too unfocused, too shotgun, too many supporting someone’s pet project with no real connection to the business”. Dutch Leonard, like Mr Porter at Harvard Business School, describes the value-building type of CSR as “an act of faith, almost a fantasy. There are very few examples.”



Perhaps that is not surprising. The business of trying to be good is confronting executives with difficult questions. Can you measure CSR performance? Should you be co-operating with NGOs, and with your competitors? Is there really competitive advantage to be had from a green strategy? How will the rise of companies from China, India and other emerging markets change the game?

This special report will look in detail at how companies are implementing CSR. It will conclude that, done badly, it is often just a figleaf and can be positively harmful. Done well, though, it is not some separate activity that companies do on the side, a corner of corporate life reserved for virtue: it is just good business.

## The feelgood factor

Jan 17th 2008

From The Economist print edition

### Helping others to help yourself

WHEN catastrophic floods hit Bangladesh last November, TNT's emergency-response team was ready. The logistics giant, with headquarters in Amsterdam, has 50 people on standby to intervene anywhere in the world at 48 hours' notice. This is part of a five-year-old partnership with the World Food Programme (WFP), the UN's agency that fights hunger. The team has attended to some two dozen emergencies, including the Asian tsunami in 2004. "We're just faster," says Ludo Oelrich, the director of TNT's "Moving the World" programme.

Emergency help is not TNT's only offering. Volunteers do stints around the world on secondment to WFP and staff are encouraged to raise money for the programme (they generated €2.5m last year). There is knowledge transfer, too: TNT recently improved the school-food supply chain in Liberia, increasing WFP's efficiency by 15-20%, and plans to do the same in Congo.

### Balm for the soul

Why does TNT do these things? "People feel this is a company that does more than take care of the bottom line," says Mr Oelrich. "It's providing a soul to TNT." In a 2006 staff survey, 68% said the pro-bono activities made them prouder to work at the company. It also helps with recruitment: three out of four graduates who apply for jobs mention the WFP connection. Last year the company came top in the Dow Jones Sustainability Index.

TNT's experience illustrates several trends in corporate philanthropy. First, collaboration is in, especially with NGOs. Companies try to pick partners with some relevance to their business. For TNT, the food programme is a good fit because hunger is in part a logistical problem. Standard Chartered, a bank, is working with the Bangladesh Rural Advancement Committee on microfinance and with other NGOs on a campaign to help 10m blind people.

Coca-Cola has identified water conservation as critical to its future as the world's largest drinks company. Last June it announced an ambitious collaboration with WWF, a global environmental organisation, to conserve seven major freshwater river basins. It is also working with Greenpeace to eliminate carbon emissions from coolers and vending machines. The co-operation is strictly non-financial, but marks a change in outlook. "Ten years ago you couldn't get Coca-Cola and Greenpeace in the same room," says Neville Isdell, its CEO.

Second, what used to be local community work is increasingly becoming global community work. In the mid-1990s nearly all IBM's philanthropic spending was in America; now 60% is outside. Part of this involves a corporate version of the peace corps: young staff get one-month assignments in the developing world to work on worthy projects. The idea is not only to make a difference on the ground, but also to develop managers who understand how the wider world works.

Third, once a formal programme is in place, it becomes hard to stop. Indeed, it tends to grow, not least because employees are keen. In 1996 KPMG allowed its staff in Britain to spend two hours a month of their paid-for time on work for the community. Crucially for an accountancy firm, the work was given a time code. After a while it came to be seen as a business benefit. The programme has expanded to half a day a month and now adds up to 40,000 donated hours a year. And increasingly it is not only inputs that are being measured but outputs as well. [Salesforce.com](http://Salesforce.com), a software firm, tries to measure the impact of its volunteer programmes, which involved 85% of its employees last year.

All this has meant that straightforward cash donations have become less important. At IBM, in 1993 cash accounted for as much as 95% of total philanthropic giving; now it makes up only about 35%. But cash still matters. When Hank Paulson, now America's treasury secretary, was boss of Goldman Sachs, he was persuaded to raise the amount that the firm chipped in to boost employees' charitable donations. Now it

is starting a philanthropy fund aiming for \$1 billion to which the partners will be encouraged to contribute a share of their pay. No doubt that is good for the bank's soul.

## The next question

Jan 17th 2008

From The Economist print edition

### Does CSR work?

Illustration by Ian Whadcock



"THE theological question—should there be CSR?—is so irrelevant today," says John Ruggie of Harvard University's Kennedy School of Government. "Companies are doing it. It's one of the social pressures they've absorbed." Three years ago a [special report](#) in *The Economist* acknowledged, with regret, that the CSR movement had won the battle of ideas. In the [survey by the Economist Intelligence Unit](#) for this report, only 4% of respondents thought that CSR was "a waste of time and money". Clearly CSR has arrived.

Mr Ruggie and others claim that the real question about corporate responsibility today is "not whether but how". But the debate has not entirely vanished, and it is worth pausing to consider some of the arguments of those who question the whole point of it.

Within companies, the few sceptics still matter, especially since they seem to be found disproportionately at the top end of management. And from time to time the debate surfaces noisily in public. Last summer, for example, Robert Reich, a former labour secretary under Bill Clinton, now at the University of California at Berkeley, launched a broadside against CSR in his book, "Supercapitalism". The CSR industry had learnt to shrug off criticism from free-marketeers such as Milton Friedman (whose seminal critique of the concept, "The social responsibility of business is to increase its profits," appeared in the *New York Times Magazine* in 1970) or, for that matter, this newspaper. But here was a cruel cut from a Clintonite.

More importantly, those who doubt whether CSR is worth having raise points that have a significant bearing on how it is done. Take three of the main objections: that it encroaches on what should be the proper business of government; that CSR is a sideshow; and that it involves playing with other people's money.

Mr Reich argues that the energy spent on CSR diverts attention from establishing rules that advance the common good—rules that help to prevent oil spills, say, or protect human rights abroad. In a democracy, he says, that should be the job of elected governments, not profit-maximising companies. It is easy to see the potential for a corrupt bargain: lobby groups find it more rewarding to put pressure on corporate executives because they respond faster than governments; governments are only too happy to duck the issue or let business pick up the bill.

In practice, however, it is often the absence of government rules that makes firms feel they have to fill the void—for example, by cutting carbon emissions or setting labour standards. And as businesses go global, they face a complicated patchwork of rules. Mr Ruggie, who serves as the UN secretary-general's

special representative for business and human rights, is particularly concerned about parts of the world where conflict or corruption means there is no effective government to do the rule-setting. Still, it is surely right to keep a wary eye on whether the things firms do in the name of good citizenship are truly in the best interests of society as a whole.

The “sideshow” objection takes issue with the assumption, all too common among executives and activists alike, that the pursuit of profitable business is not a socially responsible thing in its own right. Yet there is nothing wrong with making money: more than anything else, that is how companies do good. The welfare they create in the form of jobs, products and innovation dwarfs anything firms are likely to do explicitly in the name of CSR.

In 2004-05 Oxfam, an agency devoted to poverty relief, and Unilever, an Anglo-Dutch consumer-goods company, jointly conducted a detailed study of the economic impact of Unilever's operations in Indonesia. The conclusions were eye-opening, especially for Oxfam. Unilever in Indonesia supported the equivalent of 300,000 full-time jobs across its entire business, created a total value of at least \$630m and contributed \$130m a year in taxes to the Indonesian government. The lesson for firms is that they have been far too defensive about their contribution to society. If efforts to do good become a distraction from the core business they may actually be downright irresponsible. After all, a socially conscious but bankrupt business is no good to anyone.

## Spending other people's money

The most fundamental criticism of CSR is that what executives spend on it is other people's—ie, shareholders'—money. They may mean well, and it may give them satisfaction to write a cheque for hurricane victims or disadvantaged youth, but that is not what they were hired to do. Their job is to make money for shareholders. It is irresponsible for them to sacrifice profits in the (sometimes vain) pursuit of goodness.

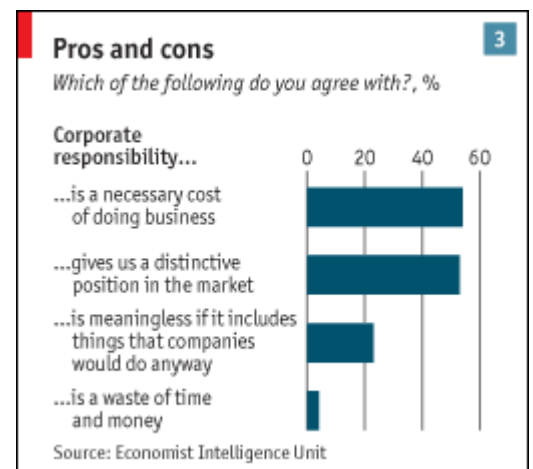
Thoughtful practitioners of CSR understand this. Executives overseeing the environmentally minded Plan A at M&S stress they are running a business, not a green charity. Marc Benioff, the boss of [salesforce.com](https://www.salesforce.com), is an evangelist for corporate philanthropy but keeps a clear sense of priorities: “First and foremost my shareholders are the most important thing.”

The simple solution is that businesses should concentrate on the sweet spot where initiatives are good for both profits and social welfare. This is the sort of “win-win” situation that executives love to talk about: the smart thing to do as well as the right thing to do. Green policies currently offer lots of opportunities for win-wins, which is why so many firms are eagerly embracing them: cut fuel costs and you help both the planet and the bottom line; expand your range of organic food and increase your market share. The same logic should lead senior management, faced with a bewildering spectrum of socially worthy activities, to select those that are most relevant to their business.

Yet people on both sides of the barricades tend to dismiss this argument. Sceptics say it renders CSR meaningless. If it amounts to nothing more than good management, it does not count. NGO activists, too, often look for some element of sacrifice on the part of business, if only to demonstrate a degree of moral commitment—without which, they fear, a company's worthy programmes may disappear with the next downturn.

Both arguments are too narrow. If corporate antennae are more keenly tuned to social trends and sensitivities, alerting managers to risks and opportunities they might not otherwise have spotted, so much the better for business. As for the activists, they of all people should like the idea of “sustainability”: if a business benefits from a CSR initiative, it is more likely to last, and its involvement may be more dynamic and innovative too.

To be fair, attitudes are changing, both in business and among NGOs. A growing number of companies are working with NGOs, especially those with operations on the ground and a commitment to getting things done. Both sides now see CSR as offering what Mr Porter calls “shared value”: benefits for both





business and society. Georg Kell, the director of the UN Global Compact, says that the case for engagement has changed from a moral to a business one.

On this view, the best form of corporate responsibility boils down to enlightened self-interest. And the more that firms embracing it are seen to be successful—through astutely managing risks and recognising opportunities—the more enlightened their leaders will be perceived to be. But do such policies really help to bring success? If not, the whole CSR industry has a problem. If people are no longer asking “whether” but “how”, in future they will increasingly want to know “how well”. Is CSR adding value to the business?

## An inconvenient truth

At present few companies would be able to tell. CSR decisions rely more on instinct than on evidence. But a measurement industry of sorts is springing up. Many big firms now publish their own sustainability reports, full of targets and commitments. The Global Reporting Initiative, based in Amsterdam, aspires to provide an international standard, with 79 indicators that it encourages companies to use. This may be a useful starting point, but critics say it often amounts to little more than box-ticking; worse, it can provide a cover for poor performers.

Sustainability rankings and indices of various kinds also help to concentrate corporate minds by shaming firms or helping them shine. But they also point to a problem. Two of the best-known indices—the Dow Jones Sustainability index and the FTSE4Good—underperform the market. AccountAbility, a British think-tank, admits to the inconvenient truth that its 2007 ranking of the *Fortune* Global 100 companies by their progress on building sustainability into their business shows no connection with their financial performance.

Even so, interest in socially responsible investment (SRI) is on the rise, along with the general surge in interest in anything to do with climate change. The signs are many: more executive time spent on managing relations with SRI investors; financial institutions with over \$10 trillion under management signing up for the UN's Principles for Responsible Investment; an “explosion of interest” in related research, according to Peter Kinder, the president of KLD Research & Analytics, which specialises in benchmarks for social investing.



A new, exhaustive academic review of 167 studies over the past 35 years concludes that there is in fact a positive link between companies' social and financial performance—but only a weak one. Firms are not richly rewarded for CSR, it seems, but nor does it typically destroy shareholder value. Might cleverer approaches to CSR in future produce better returns?

“There is no evidence that ESG [environmental, social and corporate governance] or SRI investing on their own add value,” say analysts at Goldman Sachs. But they reckon that by incorporating an ESG perspective into their long-term industry analysis they can beat the market. Their model, called GS SUSTAIN, includes ESG analysis as “a good overall proxy for the management of companies relative to their peers”, hence indicative of their chances of long-term success. But these factors need to be put into the context of companies' financial performance and the circumstances of individual industries. A company's attention to environmental, social and corporate-governance issues is only one factor among others in determining its long-term success.

The Goldman Sachs model is an intriguing attempt to capture the complex interaction between social-responsibility issues and the many other things that businesses worry about in the real world. An integrated view of the role of CSR happens to be what leading companies are striving for too.

## A stitch in time

Jan 17th 2008

From The Economist print edition

### How companies manage risks to their reputation

BUSINESS leaders embrace corporate responsibility for a number of reasons. Lee Scott, the CEO of Wal-Mart, was converted to it by the aftermath of Hurricane Katrina (which showed his company's full potential to serve "not just our customers but our communities, our countries and even the world"). Others are lured by the glamour of making pledges at the Clinton Global Initiative. For some, though, it is public embarrassment and lawsuits that concentrate the mind.

Take Yahoo!, a technology company that ran into difficulties over the jailing of two Chinese dissidents after the company handed data on them to the Chinese authorities. In November Yahoo!'s chief executive, Jerry Yang, and its top lawyer had to listen to Tom Lantos, a congressman, denounce them as technology giants but moral pygmies. The following week Yahoo! reached an out-of-court settlement with the families of the jailed men.

Trouble seems to come in waves, pounding industry after industry, each time for a different reason. It has hit the oil business because of spills and explosions. Mining companies have come under attack for collusion with corrupt governments. Clothing companies have faced scandals over the use of sweatshop or child labour. The petfood industry was pilloried after cats were killed by tainted imports from China. Mattel and other makers had to recall millions of toys made in China on safety grounds.

Most of the rhetoric on CSR may be about doing the right thing and trumping competitors, but much of the reality is plain risk management. It involves limiting the damage to the brand and the bottom line that can be inflicted by a bad press and consumer boycotts, as well as dealing with the threat of legal action.

In America, the legal instrument of choice (as in the Yahoo! case) is the Alien Tort Claims Act, which allows companies to be taken to court in America for violating human rights abroad. Under international law only states can be held responsible for violating human rights, but allegations of complicity in state abuse can provide a hook for legal claims against companies. Even if it does not get as far as a trial, this can be embarrassing and costly for companies.

Three years ago Unocal, a Californian oil company, settled out of court (reportedly for some \$30m) over allegations of complicity in abuses by government soldiers against villagers in Burma during the construction of a pipeline in the 1990s. However, the company denied any responsibility. Another oil company, Talisman Energy, discovered that being Canadian was no protection against a legal claim in the United States. It was facing a lawsuit by the Presbyterian Church of Sudan alleging complicity in genocide in Sudan, where Talisman had invested in the Greater Nile Oil Project—even though Talisman, under pressure from human-rights groups, had sold its stake back in 2002.

Time and again companies fail to see the problems coming. Only once they have had to deal with, say, a lawsuit or strong public pressure do they start to change their thinking. The CSR industry believes that a broader understanding of the world in which they operate can help companies manage these risks better (and, if they are lucky, grasp some opportunities too). "Much of the work we do is to get big incumbents to recognise a different future," says John Elkington of SustainAbility, a consultancy.

What might the next wave of trouble be? Corporate corruption, perhaps, speculates Toby Webb, the editor of *Ethical Corporation* magazine. In South Africa, for example, corruption is very much part of the CSR agenda. At two of Germany's biggest companies, Siemens and Volkswagen, heads have rolled

Illustration by Ian Whadcock





because of corruption scandals. Mr Webb reckons this could become a much bigger trend over the next couple of years.

## Chain reaction

For the moment, though, the biggest problem many companies have to deal with is something that has sprung from rapid globalisation. It is the risks associated with managing supply chains that spread around the world, stretching deep into China, India and elsewhere. For some, this is a challenge on a grand scale: Nike's contractor network, for example, involves some 800,000 workers.

Firms can set standards of behaviour for suppliers, but they do not find it easy to enforce them. Unscrupulous suppliers may cheat, keeping two sets of records, one for show, one for real. Others, under intense pressure to keep costs low, may cut corners—allowing unpaid overtime, for example, or subcontracting work to other firms that escape scrutiny.

And on top of the need to guarantee labour standards and product safety across an extended network, a new demand is starting to emerge: companies have to consider the environmental “sustainability” of their suppliers too. So inspection regimes are set to intensify, at a time when audit fatigue has already become a problem for suppliers. Surveys suggest that a typical garment factory may expect to be inspected 25 times a year. Levi Strauss, Timberland and others in the industry are starting to collaborate on inspections to reduce the burden on suppliers.

Each industry has its own specific issues, but there are some common themes in how firms are approaching the risk-management side of CSR. One is to put in place proper systems for monitoring risk across the supply chain, including listing who the suppliers are, having well-established channels of communicating with them and auditing their compliance with ethics codes. Basic as it sounds, even many big companies fail to do this: 60% of the 2,000 large companies surveyed recently by Integrity Interactive, a risk consultancy, said they did not require suppliers to enforce a code of conduct. Only 42% regularly assessed ethics risk in the supply chain, and just 12% had a web-based portal for their suppliers.

Beyond the basics, prudent companies include a CSR perspective when considering new projects. In such cases CSR is not a public-relations exercise but part of systematic due diligence for new investments. The social and economic impact of the firm's existing operations is also closely monitored to reduce the risk of a backlash from local communities, activists or national governments.

Anglo American, a mining company, is among the most sophisticated in its approach to managing its social impact. It has developed a “socio-economic assessment toolbox” to identify local stakeholders, see how projects affect them and draw up plans to improve the outcome and develop trust. The company says this provides a better understanding of local interests and helps it to avoid potential conflicts. Last October Cynthia Carroll, Anglo's CEO, announced at the annual conference organised by Business for Social Responsibility in San Francisco that “as a contribution to spreading good practice” it would make the basic version of its toolkit publicly available.

Involvement in social programmes, especially in poor parts of the world, is an increasingly fashionable way for a company to burnish its brand and, with luck, protect itself from attack. Which self-respecting CEO these days wants to be caught doing nothing for Africa? But sometimes these programmes also have a clear business rationale. Anglo American, for example, says the \$10m a year it spends on HIV testing and treatment in Africa is starting to pay for itself through reduced absenteeism and longer lives for skilled workers.

The big drugs companies, for their part, were greatly embarrassed by accusations of ignoring the needs of Africans dying from HIV/AIDS, so GlaxoSmithKline and others decided to make HIV drugs available for no profit. Merck has entered an innovative partnership to fight AIDS with the Bill & Melinda Gates Foundation and the government of Botswana, where the proportion of sufferers being treated is now the highest in Africa. Since 1987 Merck has also donated 1.8 billion tablets to treat river blindness, reaching more than 60m people a year in Africa, Latin America and the Middle East. All this helps to quieten the critics. The involvement in emerging markets may even prove a

good investment in future growth.

Novo Nordisk, a Danish company that supplies a big share of the world's insulin, has written the "triple bottom line"—that is, striving to act in a financially, environmentally and socially responsible way—into its articles of association. It reckons that having the creed anchored so firmly is making it more alert to both risks and opportunities.

## Comfort in numbers

But risk management can be a lonely business. Mattel's monitoring of its suppliers is said to have been state-of-the-art, but that did not save it from costly embarrassment in China. With the best will in the world and the most energetic efforts to create codes, talk to stakeholders and support hospitals and schools, companies can still find themselves uncomfortably exposed, especially as what is expected of them can vary so much from country to country.

The answer, many have decided, is to spread the risk. Groups of them are getting together to agree on codes of conduct—usually within a particular industry, but also across industries and in consultation with governments, UN agencies and NGOs. This has become one of the most striking recent trends in CSR.

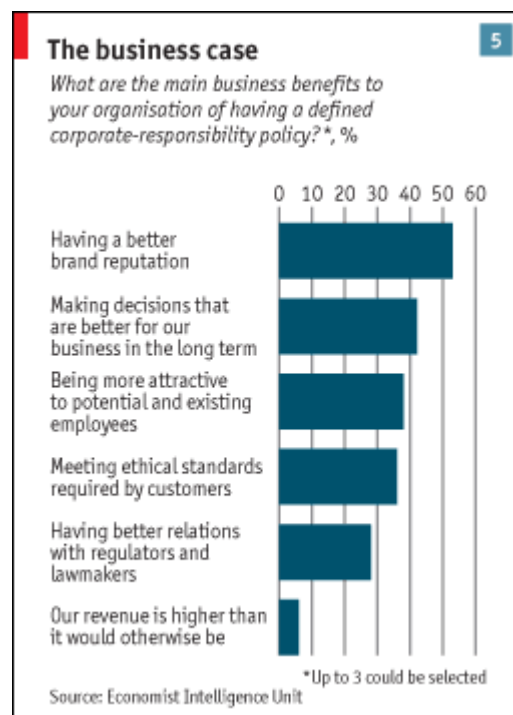
The mining industry, for example, has joined with governments in the Extractive Industries Transparency Initiative (EITI), launched in 2002 by Tony Blair, then Britain's prime minister, to tackle the problem of government corruption in resource-rich countries. Britain, America, Norway and the Netherlands, together with a number of NGOs and big energy and mining companies, have signed up to a set of Voluntary Principles on Security and Human Rights. The finance industry has adopted the Equator Principles, a benchmark for managing social and environmental issues in project financing.

There's more. Diamond producers encouraged the Kimberley Process, a certification scheme to combat trade in blood diamonds. The Forest Stewardship Council provides certification for the forestry industry and its products. A group of companies that want to find pragmatic ways of applying human rights in global business have formed the Business Leaders Initiative on Human Rights (BLIHR), which now has 14 members. Technology companies in America are working on a code of conduct on human rights, not least to avoid the sort of trouble that Yahoo! encountered in China. In Britain the Ethical Trading Initiative brings together retailers, trade unions and NGOs to support corporate codes that improve working conditions across global supply chains.

Such "multi-stakeholder initiatives" tend to involve companies that have elevated CSR to a strategic level. Some initiatives will not work: sitting down with competitors, let alone NGOs, is not easy. But the effort can be worth it. When Gap encountered a problem over child labour in India last October, the damage proved a "two-day wonder", according to Mary Robinson, the president of Realising Rights: The Ethical Globalisation Initiative. She reckons this was due to Gap's swift response and its involvement in initiatives like BLIHR (which she chairs). When Gap joined BLIHR three years ago it admitted it had some problems—and found itself winning praise for transparency rather than being pounced on for its transgressions.

Whether these initiatives always serve wider interests (as opposed to those of particular firms) is harder to tell. Some companies may benefit more than others: for De Beers, for example, the Kimberley Process reduced a threat to the industry and if anything increased its own brand's dominance. The introduction of more humane conditions for textile workers in places like Bangladesh risks losing them their jobs unless productivity can be improved at the same time, stresses Alex MacGillivray of AccountAbility, a think-tank involved in a multi-stakeholder initiative called the MFA Forum. As for the EITI, there is some evidence that it has reduced corruption in Nigeria, according to Mr MacGillivray, though it may be just shifting the graft to other ministries. Some NGOs would prefer hard law rather than the "soft" rules involved in many of these initiatives.

How committed are companies to the rules they claim to live by, whether their own or an industry-wide code? "What concerns us," says Daniel Feldman of Foley Hoag, a law firm with a CSR practice in



Washington, DC, “when most corporate-responsibility effort is on PR and communications, is that we don't know whether firms are actually implementing the rules.” Is there a reporting requirement? Is the CEO keen?

For a few companies that want to be leaders in the world of corporate citizenship, the answer to those questions is clearly yes. And even if such companies first discovered CSR the hard way, by suffering a knock to their reputation, many now see it as more than just a tool of risk management; they are convinced that it can be a competitive advantage and a source of growth in its own right.

Nike, for example, came to the subject in defensive mode: it was attacked in the early 1990s, when the idea of corporate responsibility had barely surfaced. Now Hannah Jones, the vice-president of corporate responsibility (who reports to the chief executive), talks of “return on investment squared”: to investors and to the community. She sees corporate responsibility as providing a fresh source of innovation. She no longer bothers to attend CSR conferences full of other corporate folk; these days she prefers to network with social entrepreneurs. And like many in the CSR world she has high hopes for more emphasis on “sustainability”.

## A change in climate

Jan 17th 2008

From The Economist print edition

### The greening of corporate responsibility

AL GORE has done a wonderful thing for corporate bosses. By helping to propel climate change to the top of the global agenda, he has opened up a world of new opportunities for them. Opportunities for rhetoric, for a start. The green theme allows chief executives to adopt a planetary perspective. "It's what survival will be about in the 21st century," proclaims Coca-Cola's Neville Isdell, talking of his company's plans for water conservation. Over at PepsiCo, Indra Nooyi stresses the importance of companies embracing "purpose" as well as performance, with products that "contribute positively and responsibly to human civilisation".

Beyond the lofty talk, reducing a company's output of greenhouse gases and encouraging "responsible" use of resources can also mean cutting waste and saving money. Whether it is discouraging the use of plastic bags in a supermarket or switching off a law firm's computers at night, there are plenty of quick wins for most companies. This is doubly satisfying—doing well and doing good—and therefore extremely popular.

For some companies the gains to be had from cutting waste and improving energy use are very large. United Technologies Corporation (UTC), whose products range from aerospace to air-conditioning systems, has reduced its carbon footprint by 19% over the past ten years even as it has doubled its output, according to George David, the CEO. "We've had an explosion of doing more with less," he says. In 2008 UTC is aiming for growth of 10% while cutting carbon emissions by a further 5%.

Looking ahead, some companies think the demand for efficient and clean energy use is an opportunity not just for savings but for growth. Mr David thinks that in 30 years' time conservation and related areas could make up 30% of the company's business, from nothing today. DuPont, a chemicals giant, is starting to set targets for increasing revenue from "non-depletable" products and services. At the Clinton Global Initiative last September Standard Chartered, a bank with big operations in emerging markets, pledged to spend \$8 billion-10 billion over five years on financing renewable energy projects in Asia, Africa and the Middle East. Peter Sands, the chief executive, says that since enormous amounts of money will have to be deployed in this area in the coming years, "we want to be active leaders."

### Sootless in Seattle

But leadership on "sustainability" is not easy. Some of the companies that set themselves the goal of becoming carbon neutral by 2010 or 2012 will struggle to find a way to do it. For those that are serious about changing their impact on the planet, it will be something of a voyage of discovery. The starting point is to find out the size of their current carbon footprint. "We find with energy and greenhouse gases, if you start to measure, people reduce the usage," says Linda Fisher, the chief sustainability officer at DuPont. Measuring is not a simple task, but once a company has a proper baseline it can see what can be changed. Commitment from the top is crucial.

What are the truly committed companies doing? Three examples—an outdoor-goods business, a logistics company and one of the world's biggest conglomerates—give an idea of what is happening at the cutting edge.

Illustration by Ian Whadcock



If your business is equipping people for outdoor adventure, then careful stewardship of the environment seems a natural. Sure enough, outdoor-goods companies such as Patagonia (“every day we take steps to lighten our footprint and do less harm”) and Timberland (“our love for the outdoors is matched by our passion for confronting global warming”) are among the most ardent champions of sustainability. The same goes for Seattle-based REI, America’s biggest consumer co-operative with over 3m members and 80-plus stores.

As a co-op, REI enjoys the luxury of not having to worry about Wall Street’s expectations each quarter. It can think long-term. Four years ago it decided it had to aim to be climate-neutral and brought in consultants to establish a baseline and help produce a plan. The target date is 2020, with a one-third reduction by 2009 against the 2006 baseline.

REI was shocked to find that more than a quarter of its carbon emissions came from flights associated with the adventure travel it organises, so it started to buy carbon offsets for these trips. One-fifth of its emissions comes from electricity consumption, so it shopped around for renewable sources, such as hydro power in Washington state. It opened a second distribution hub in Pennsylvania to cut energy waste in transport. It also looked at ways to reduce greenhouse-gas emissions from employee commuting, which account for about a fifth of the total, so it is providing incentives for its people to cycle to work. “Our team is really getting granular,” says Sally Jewell, REI’s chief executive.

The company is also working on the carbon footprint of its buildings, its use of paper, its packaging and the eco-friendliness of its products. Together with other manufacturers, it is looking at eco-sensitive materials, which need to be natural but also to do the job in hand well. Green labelling will follow.

The lesson from REI is that going seriously green involves a lot more than setting a target date for zero emissions. It requires measuring and managing. That turns out to be hard, intricate work which stretches right across a company’s operations, and perhaps beyond. At present, REI counts the carbon once it owns a product: for example, it takes responsibility for its own brands’ transport from the factory. It does not include its suppliers’ operations in its carbon calculations because it has yet to work out how to do it. “But I think that’s coming,” predicts Ms Jewell.

Illustration by Ian Whadcock



## The non-flying Dutchman

You know a boss is serious when he gives up his private jet, swaps his Porsche for a hybrid Prius and drives rather than flies all the way from Amsterdam to Davos. Peter Bakker believes that being on top of the climate-change issue is a prime business need for TNT, the Dutch logistics company he heads. He thinks customers may well shorten their supply chains to stop shipping so many parts around the world by air. Regulators may impose new rules, such as a carbon tax or carbon labelling, which could affect TNT’s business model. Investors are asking questions about sustainability. “Only those companies that can make the shift to manage this as an integral part of the business will be able to respond fast enough,” he says.

Last year Mr Bakker launched “Planet Me”, a campaign to change the company’s carbon trajectory. TNT’s carbon footprint has been measured, targets for reducing it will soon be set and efforts will be made to help employees lead greener lives both at work and at home. For starters, the travel budget is being cut by 20% (a saving of €3.2m a year, which more than covers the €2.8m spent on installing state-of-the-art desktop video-conferencing systems). In 2010 TNT will move its headquarters to what is designed to be a carbon-positive building that will be producing green energy to spare.

TNT intends to monitor its carbon emissions assiduously, giving customers a tracker to show CO<sub>2</sub> emissions of the services they are buying. Reporting on emissions will follow the same rules as financial reporting, so there could be warnings of poor performance just as a company might issue profit warnings. Bonus schemes will be linked to this.

But there is no escaping the fact that, as a global transport company with a big fleet of aeroplanes and trucks, TNT churns out greenhouse gases. In 2006 it produced 826 kilotonnes of CO<sub>2</sub>. To cut down on emissions from the trucks, it is introducing hybrids and electric vehicles. The 44 aeroplanes are trickier. They account for half of all TNT's emissions, and there is little the company can do but try to run these as efficiently as possible. It says it is prepared to invest in promising aircraft technologies.

Its fleet includes two Boeing 747s which fly back and forth between Liège in Belgium and Shanghai, accounting for half the company's fuel consumption. "Two years ago we didn't think of climate change when buying 747s," says Mr Bakker. "Today it would be a main item if we were considering buying two more." But would TNT really forgo increasing its business with China?

The logistics industry provides the arteries of globalisation, and TNT's experience suggests that pressure for more responsible strategies on carbon emissions will spread through those arteries. Some of TNT's customers in Scandinavia, for example, have started to inquire about the carbon impact of transporting their parts. TNT is asking its own suppliers and subcontractors to be committed to the environment too, and selects them with that in mind.

The list of big companies that have put the environment or other aspects of CSR at the heart of their strategy is not very long, but one name usually tops it: GE. In 2005 it launched "ecomagination", a vigorous push to invest in green technology and expand sales of products and services with measurably better environmental performance. Products range from light bulbs to gas turbines to railway and jet engines and have to offer a sustainability improvement of at least 10% to be included.

## General Eclectic

Like most such initiatives, ecomagination is partly a packaging and public-relations job, bringing together a number of things the company was doing anyway. Some say it is not even particularly ambitious, given the gains in energy efficiency that technology is producing across the board. Part of the plan involves a cut in greenhouse-gas emissions in 2012 of 1% compared with the 2004 baseline—not bad for a company that also expects to grow strongly over that period, but hardly stretching. Sure enough, GE is beating its targets, with emissions already down by 4%. There are no targets yet for saving water (though GE says these are on their way).

Still, GE is big, and ecomagination has scale. R&D investment in cleaner technologies is to rise from \$700m in 2005 to \$1.5 billion in 2010. By then the company expects revenues from ecomagination products to be at least \$20 billion.

This is turning out to be a good bet. "We've sold out in eco-certified products to 2009," says Bob Corcoran, the vice-president for corporate citizenship. You can't buy a GE wind turbine before 2010. Employees like the green focus and have come up with initiatives of their own that are worth some \$70m a year in energy savings. All this has helped to polish GE's reputation. The company still gets bad marks for its response to the toxic mess it poured into New York's Hudson river long ago, but it now has fans among environmentalists too.

GE has not forgotten that it is in the business of making money, not doing social work. "No good business can call itself a good corporate citizen if it fritters away shareholder money," says Mr Corcoran. GE has 6m investors, and "it's their money too." The company is simply moving in the direction in which it thinks social pressures will push it anyway.

In doing so, it is also behaving in ways that would have been hard to imagine a few years ago. It has joined together with other big companies and NGOs to form the US Climate Action Partnership to lobby for national legislation in America to cap carbon emissions. Europe already has a cap-and-trade system, and GE would like a more uniform set of rules across the world.

There is no doubt that the greening of corporate responsibility rings a bell with many companies. They can cut costs, delight employees and burnish their brand. By preparing their business for the expected

demands of customers and regulators they may also be giving themselves a competitive advantage. But if it is to involve much more than public relations, it will be long, hard work. As companies' claims of green virtue multiply, so will the efforts by organisations such as Climate Counts to monitor them and hold them to account. Few customers will buy green at the expense of price or quality, and it is early days for much of the research and investment in clean technologies. Besides, the demand for sustainability varies greatly from place to place. Europe and Japan have mostly been ahead of America. And in China the dash for growth comes first.



## The good consumer

Jan 17th 2008

From The Economist print edition

### Buying ethical is not as straightforward as it seems

WHAT'S a label worth? A lot, it seems, when it comes to towels in an upmarket New York shop. In 2005 ABC Home Furnishings allowed two Harvard University researchers, Michael Hiscox and Nicholas Smyth, to conduct an experiment on two sets of towels. One lot carried a label with the logo "Fair and Square" and the following message:

These towels have been made under fair labour conditions, in a safe and healthy working environment which is free of discrimination, and where management has committed to respecting the rights and dignity of workers.

The other set had no such label. Over five months, the researchers observed the impact of making various changes such as switching the label to the other set of towels and raising prices. The results were striking: not only did sales of towels increase when they carried the Fair and Square label, they carried on increasing each time the price was raised.

No wonder companies are keen to appeal to ethically minded consumers, whether on labour standards or green credentials. Timberland, a New Hampshire outdoor-gear company, is introducing detailed "Green Index" labels on its shoes. Sainsbury's, a British supermarket, now sells only Fairtrade bananas, with the assurance that poor farmers have received a decent price, and all its own-brand paper products come from sources approved by the Forest Stewardship Council. Tesco, M&S and Wal-Mart have all launched initiatives that bet on the rise of the ethical consumer.

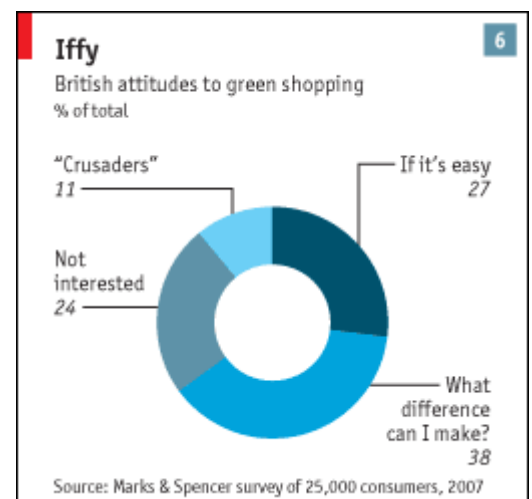
On greenery, M&S reckons that British consumers divide into four broad groups. About one in ten is passionately green and will go out of their way to shop accordingly. At the other end of the spectrum one-quarter are not interested. In-between are those who care but want green consumption to be easy, and those who are vaguely concerned but don't see how they can make a difference (see chart 6). In M&S's view, that represents an opportunity: three-quarters of British consumers are interested in the green theme in some way.

But even the keenest ethical consumer faces complicated trade-offs, and sometimes the apparently obvious ethical choice turns out to be the wrong one. Surely it must be greener for Britons to buy roses from the Netherlands than ones air-freighted from Kenya? In fact, a study at Cranfield University showed the carbon footprint of the Dutch roses to be six times as large because they had to be grown in heated greenhouses.

Consumers are right to be suspicious of the ethical claims made for many products. A recent study of the labels of 1,018 products in big stores in North America by TerraChoice, an environmental marketing agency, found that almost all of them were guilty of some form of "greenwashing". They did not tell outright lies, but nor did they tell the whole truth.

### A conditional shade of green

Joel Makower, the executive editor of [GreenBiz.com](http://GreenBiz.com), says that, given a choice, most consumers will be happy to choose the greener product—provided it does not cost any more, comes from a trusted maker, requires no special effort to buy or use and is at least as good as the alternative. "That's a high hurdle for any product," he notes.



So shoppers will still flock to shops that sell cheap products of decent quality, without asking how these are made. They will often buy more if a product is attractively presented, never mind that the packaging may be wasteful. And when companies try to do the right thing, consumers will not always go along with them. Airlines that invite their customers to buy carbon offsets have seen only minimal uptake.

The lesson for companies is that selling green is hard work. And it is no good getting too far ahead of the customer. Half a step ahead is about right, according to Stuart Rose, the chief executive of M&S. Much more, and you won't sell. Any less, and you won't lead.

## Going global

Jan 17th 2008

From The Economist print edition

### CSR is spreading around the world, but in different guises

"THE British brand of corporate responsibility is seen as the gold standard," says Julia Cleverdon, chief executive of Business in the Community, which for 25 years has been championing the cause in Britain. And it is true that Britain, especially London, has been a hive of innovation in CSR since the mid-1990s, thanks to a creative cluster of think-tanks, NGOs, consultancies and inventive bosses. But according to Simon Zadek of AccountAbility, a think-tank that has been part of the cluster, this is also a repeat of a familiar British business story: superb innovation, poor implementation.

By contrast, when American firms get serious about CSR—Wal-Mart on sustainability, for example—the execution is generally impressive. The Japanese, for their part, see the roots of CSR in the traditions of Japanese business, such as *shobaido* (the way of doing business) and *shonindo* (the way of the merchant), and Japanese firms pay a lot of attention to the environment and to relations with local communities. The lead on CSR could even shift from the rich world to the big emerging markets, each with its own traditions and priorities.

For global companies this means that a one-size-fits-all approach to corporate responsibility may not work. What is right for Europe may not be appropriate for India. Such differences in priorities (see table 7) are bound to grow in importance as the BRIC countries—Brazil, Russia, India and China—and other emerging markets gain in economic clout and confidence.

The things that matter						
Which issues will be the most important in the next five years? Select three:						
Global rank	Issue	United States	Britain	Germany	China	Brazil
1	The environment	2	1	2	2	1
2	Safer products	5	4	6	3	2
3	Retirement benefits	4	2	1	4	7
4	Health-care benefits	1	5	8	1	8
5	Affordable products	6	3	3	5	3
6	Human-rights standards	8	8	9	9	4
7	Workplace conditions	9	10	4	7	6
8	Job losses from outsourcing	3	6	5	13	13
9	Privacy and data security	7	7	7	6	10
10	Ethically produced products	10	9	10	8	9
11	Investment in developing countries	16	11	14	12	5
12	Ethical advertising and marketing	12	12	16	11	11
13	Political influence of companies	11	14	12	14	14
14	Executive pay	15	16	11	10	15
15	Other	13	13	15	16	12
16	Opposition to freer trade	14	15	13	15	16

Source: McKinsey survey, September 2007

Among the BRICs, Russian companies seem the least interested in the idea of corporate citizenship, but Brazil has a lively CSR scene. Some 1,300 companies are members of Instituto Ethos, a network of businesses committed to social responsibility. "We are developing a unique process in Brazil," says Ethos's founder, Oded Grajew. Ethos tries to influence public policy and corporate behaviour "to establish a socially responsible market". A few Brazilian firms—such as Natura, a cosmetics company, and Aracruz, a pulp and paper producer—are widely known for their CSR efforts.

India has a long tradition of paternalistic philanthropy. Big family-owned firms such as Tata are particularly active in providing basic services, such as schools and health care, for local communities. For the rich, who have prospered as the economy has boomed in recent years, generous philanthropy is also

a way of heading off a backlash against business. A broader culture of ensuring decent working conditions has been slow to spread.

## One BRIC at a time

China has become the new frontier for the CSR industry. Ms Cleverdon says Chinese visitors are piling into her organisation's London offices. Aron Cramer, the CEO of Business for Social Responsibility, a San Francisco-based lobby group, points out that his outfit has increased its representation in China from two to ten people over the past 18 months. Call Mr Zadek on his mobile phone and he answers in Beijing, where he is talking to Chinese think-tanks about CSR and trade policy.

It is still early days. For Chinese companies that serve the home market, the relentless focus on growth leaves little room for worrying about the niceties of corporate citizenship. And the lack of political freedom means there is no network of NGOs to persuade them to do more. Yet pressure to take corporate responsibility more seriously is nevertheless growing.

From above, the government is starting to make noises about environmental responsibilities. From outside come the codes and inspections of foreign investors and global companies that want to apply their ethical standards across their supply chain. And from within, Chinese companies that want to go global themselves are starting to realise that they will have to pay attention to CSR as part of their effort to gain acceptability and build their brand. It was a shock for China National Offshore Oil Corporation to see its plans to buy Unocal, a Californian oil firm, scuppered by American politicians; and, more recently, for PetroChina to find itself targeted by campaigners for disinvestment in Sudan.

The first signs of a fledgling corporate-responsibility industry are beginning to appear. A few Chinese companies have started to issue CSR reports ("beautiful books, not much inside," says a Chinese critic). In Shanghai in October 2007, 13 foreign and domestic companies launched the Chinese Federation for Corporate Social Responsibility. These are baby steps, but the Chinese are quick learners.

"I would bet that within five years they'll be deeply involved in the management of standards," predicts Mr Zadek. "Then they'll build their own, and they'll become exporters of standards." If so, China may in time begin to challenge Western ideas of CSR. Mr Cramer reckons that Chinese companies will want to redefine corporate responsibility in ways that suit their own priorities.

Competing models of CSR are already at work in Africa. Chinese investment is pouring in to secure access to raw materials needed for China's turbocharged economy. The Chinese may show little interest in the rights of workers or opening a dialogue with "stakeholders", but they build roads and other infrastructure. To some African leaders, this no-strings approach has its attractions. Western companies, under closer scrutiny from activists, have to be mindful of codes of behaviour and transparent reporting. Sometimes pressure from NGOs on Western companies has the perverse effect of forcing them out of countries such as Sudan in order to stop alleged complicity with government abuse—only to be replaced by Chinese or Indian companies that do not give a damn about human rights.

But NGOs can also be a conduit for corporate responsibility in emerging markets, working closely with business to reach what C.K. Prahalad of the University of Michigan's Ross School of Business calls "the bottom of the pyramid". There is a convergence of interests between NGOs trying to improve lives in poor communities and companies keen to reach consumers in markets with huge growth potential.

Many NGOs have moved beyond acting merely as watchdogs to co-operating with big companies on joint projects. And some, as Mr Prahalad and Jeb Brugmann, a sustainable-development specialist, noted last year in the *Harvard Business Review*, are setting up innovative joint businesses as an effective way of providing services and reaching consumers.

They point to examples such as BP's arrangements with NGOs to distribute stoves in rural India and ABN

Illustration by Ian Whadcock



AMRO's collaboration on microfinance in Latin America with ACCION International, an NGO that is itself beginning to develop a multinational business. "CSR started as a way for companies to gather intelligence about NGOs and manage their reputations," they write. "It has wound up providing them with the tools they need to pursue business opportunities in untapped markets."

So will influence in CSR continue to trickle down from rich countries to poorer ones, or could it even be the other way round? Emerging countries might bridle at simply importing an agenda from the rich world, carrying echoes of colonialism. And as more investment flows to developed countries from Russia, China and the Middle East, this may colour attitudes in Western boardrooms too. How much will sovereign wealth funds care about corporate responsibility?

Amid so much uncertainty, multinational companies yearn for predictability and want to see the global playing field levelled, as they are so fond of saying. Yet they do not want intrusive rules either. When NGOs supported binding global norms for firms' human-rights responsibilities, businesses objected and the effort collapsed. Instead, since 2005 John Ruggie, the UN secretary-general's special adviser on business and human rights, has been carrying out a painstaking consultation with all the parties concerned.

Mr Ruggie is due to make his final recommendations in June. He says he wants "effective outcomes, not feelgood outcomes." For governments, that may mean a reminder of their legal responsibility to protect human rights. For companies, it could mean further encouragement and greater accountability for the sort of "soft law"—such as voluntary codes and multi-stakeholder initiatives—that has helped to improve the behaviour of companies running into trouble for various abuses.

## **A forest of figleaves**

Companies can select from an extensive menu of standards and guidelines to remain up to scratch, on human rights and much else. There are guidelines from the ILO and the OECD, as well as standards such as ISO 14001 (for the environment) and SA 8000 (for human rights). A very soft "guidance standard" on social responsibility, ISO 2600, is in the works.

A soft code that is proving popular is that of the UN's Global Compact. To sign up, companies need only commit themselves to ten broad principles—such as promoting environmental responsibility and working against corruption—and report on their progress once a year. Yet the compact is toothless. Critics say it just provides cover for companies from China and elsewhere which cheerfully sign up to it and then even more cheerfully ignore it.

But on one thing Georg Kell, the compact's perky executive director, is no softy. CSR is a child of openness, he says. Corporate responsibility in recent years has been driven by globalisation. If markets stay open, it will continue to spread. But openness should not be taken for granted: "The day markets close, CSR is over."

## Do it right

Jan 17th 2008

From The Economist print edition

### Corporate responsibility is largely a matter of enlightened self-interest

THE CSR industry, as we have seen, is in rude health. Company after company has been shaken into adopting a CSR policy: it is almost unthinkable today for a big global corporation to be without one. Climate change has added further impetus. Investors are taking an ever greater interest. New and surprising sorts of co-operation are springing up: with NGOs, with competitors, with other companies. The message is moving across supply chains and spreading around the world.

What has helped to make all this possible is globalisation—which has also been responsible for much of the general wealth-creation through which companies, let it not be forgotten, make their main contribution to society. A sudden bout of protectionism, which is by no means out of the question, could put it at risk. So activists who press for various forms of protection should be careful what they wish for. An economic recession would also be bad news for the CSR industry, parts of which might be seen as a luxury companies could live without.

But assuming that corporate goodness continues to flourish, how will things evolve? The next wave, some believe, will be one of disruptive innovation, featuring a new breed of “social entrepreneur” that will take over from the established big companies as the driving force. Mr Benioff of [salesforce.com](http://salesforce.com) reckons that social entrepreneurs have “cracked the code” of the next generation of corporate responsibility: it will be for-profit and self-sustaining. Mr Benioff himself plumbed philanthropy into his company right from the start by committing 1% of equity, profits and employees' time as a contribution to the community.

The extraordinary wealth-creation of recent years has produced a large number of extremely rich people, many of them from the software and finance industries, who are interested in a new kind of philanthropy: a smart, capitalist kind. It involves using money for maximum impact by investing in potentially disruptive technologies (in the environmental field, for example) and in social enterprises that can be scaled up as required.

This kind of enterprise has several advantages over established big business. It has focus, rather than being a sideline, as CSR often is for large companies. It involves people who are using their own money and are interested in measurable results: “real good” not “feelgood”. It brings financial rigour as well as an appetite for risk, and it can teach the big companies a thing or two about how to measure the success of social investments.

The sums involved are not trivial. That is partly thanks to Bill Gates, who in June will leave his full-time job at Microsoft to work at his fabulously rich charitable foundation. This will aim to be giving away \$3 billion a year by 2009, more than any other foundation anywhere. Money also pours in through innovative charities such as Absolute Return for Kids in London, which invests donors' money with entrepreneurs on the ground in developing countries.

The entrepreneurial model of tackling social and environmental problems is likely to stir up the CSR world. It may over time produce transformative technologies and creative new business models. But for now it is still big businesses that can make a difference. Large companies will find ways of working with—and sometimes absorbing—successful social ventures. In the next few years CSR will be mainly about “how large corporations steer a sustainable growth strategy in a very complex environment”, as Jane

Illustration by Ian Whadcock





Nelson of Harvard University puts it.

## **Few leaders, many laggards**

This report has looked at some of the companies that are doing interesting things, both to manage their risks and to exploit opportunities. But such examples are relatively scarce: the same few familiar names pop up again and again. Like most industries, the corporate-responsibility business has a handful of leaders, a large number of followers and many laggards.

You can recognise the leaders partly from the way they are grappling with particularly tricky issues, such as how to apply codes of practice across global supply chains or how best to convey accurate environmental information on product labels. The leaders typically have a committed CEO who champions the policy, a chief officer for corporate responsibility—or sustainability or whatever—who reports to the boss, and a cross-functional board committee to ensure that strategy is co-ordinated throughout the company. Non-financial measures of progress often play an important part in the overall assessment of the company's performance. These are companies, in short, that are seeking to “embed” CSR in the business.

Not every company can be a leader, nor should they all want to be. Being a high-profile early enthusiast carries the risk of overpromising. First-mover advantage soon passes. After a while, for example, everybody turns green, and the winners are the companies with the best execution. One large consultancy advises its big clients to be number two or three on corporate responsibility rather than number one. Thoughtful firms may pick and choose across the spectrum of CSR activities where to be ahead and where merely to comply with the rules.

The followers in the CSR industry are many. By now they probably produce a glossy report which lists numerous worthy activities—too many, in fact, when it would be better to concentrate on those that really work and benefit the business. The companies concerned may have little idea whether their carbon-offset scheme is effective or their ethical-purchasing plan costs jobs. Their real motive is public relations, and the telltale sign is that the person responsible for CSR sits in the corporate-communications department.

And the laggards? There are two types. Companies in the first group have simply failed to pay much attention to CSR; they risk being attacked as “late adopters”. Those in the second group, more cynically, think they can afford to ignore CSR, at least for now. Perhaps they are in an industry with a low profile, or operate in countries where scrutiny is minimal. They do not mind being viewed as freeloaders by competitors who spend time and money on trying to be good corporate citizens. Over time, though, this could also be risky if they find themselves subject to greater scrutiny or miss out on opportunities.

## **Doing what comes naturally**

One way of looking at CSR is that it is part of what businesses need to do to keep up with (or, if possible, stay slightly ahead of) society's fast-changing expectations. It is an aspect of taking care of a company's reputation, managing its risks and gaining a competitive edge. This is what good managers ought to do anyway. Doing it well may simply involve a clearer focus and greater effort than in the past, because information now spreads much more quickly and companies feel the heat.

So paying attention to CSR can amount to enlightened self-interest, something that over time will help to sustain profits for shareholders. The truly responsible business never loses sight of the commercial imperative. It is, after all, by staying in business and providing products and services people want that firms do most good. If ignoring CSR is risky, ignoring what makes business sense is a certain route to failure.

Illustration by Ian Whadcock

It is the interaction between a company's principles and its commercial competence that shapes the kind of business it will be. A company that is weak on both values and commercial competence is simply a bad business. One that has strong values but is badly run, without proper attention to translating values into profits, will



plainly not do well. In contrast, a company that is highly competent commercially but does not bother with corporate responsibility may work just fine, but it could also prove increasingly risky. Lastly, a combination of a strong commitment to CSR and strong commercial competence gives a good chance of success.

If it is nothing more than good business practice, is there any point in singling out corporate social responsibility as something distinctive? Strangely, perhaps there is, at least for now. If it helps businesses look outwards more than they otherwise would and to think imaginatively about the risks and opportunities they face, it is probably worth doing. This is why some financial analysts think that looking at the quality of a company's CSR policy may be a useful pointer to the quality of its management more generally.

True, much of what is done in the name of CSR is nothing of the sort. It often amounts to little more than the PR department sending its own messages to the outside world. Yet in a growing number of companies CSR goes deeper than that and comes closer to being "embedded" in the business, influencing decisions on everything from sourcing to strategy. These may also be the places where talented people will most want to work.

The more this happens, ironically, the more the days of CSR may start to seem numbered. In time it will simply be the way business is done in the 21st century. "My job is to design myself out of a job," says one company's head of corporate responsibility.

For the moment, though, chief sustainability officers and their ilk remain in high demand. No doubt there will also be growing opportunities for ones that speak Mandarin or Hindi as the fashion for corporate social responsibility spreads around the world. And it will be quite a while yet before they all become redundant.



## Sources and acknowledgments

Jan 17th 2008

From The Economist print edition

In addition to the people named in this report, the author would like to thank the following for their help: Jim Aisner, Mike Barry, Richard Batten, C.B. Bhattacharya, Rosanne Bonanno, Sheila Bonino, Richard Brophy, Ann Cairns, Richard Cellini, Suzanne Chase, Richard Clarke, David Curran, Ian Davis, Michael Evans, Steve Garnett, Lisa ter Haar, Carin ten Hage, Ajay Khanna, Isabel Kelly, C.S. Kiang, Paul Lewis, Simon Lewis, Ernst Ligteringen, Stanley Litow, Daniel Litvin, Gareth Lofthouse, Joshua Margolis, Richard Mills, Charles Moore, Laura Moustakerski, Dambisa Moyo, Andrew Newbery, Jeremy Oppenheim, Amon Rappoport, Yvonne Ryan, Jeffrey Sachs, Jat Sahota, Susanne Stormer, Jeffrey Sturchio, Jeffrey Swartz, Sandra Taylor and Michael Toffel.

### Sources:

#### Books and articles:

Robert B. Reich, "[Supercapitalism: The Transformation of Business, Democracy and Everyday Life](#)", Knopf, 2007.

Bradley K. Googins, Philip H. Mirvis and Steven A. Rochlin, "[Beyond Good Company: Next Generation Corporate Citizenship](#)", Palgrave Macmillan, 2007.

Milton Friedman, "[The social responsibility of business is to increase its profits](#)", *New York Times Magazine*, September 1970.

Clive Crook, "[The good company](#)", *The Economist*, January 2005.

Jeff Bruggmann and C.K. Prahalad, "[Co-creating business's new social compact](#)", *Harvard Business Review*, February 2007.

Michael E. Porter and Mark R. Kramer, "[Strategy and society: The link between competitive advantage and corporate social responsibility](#)", *Harvard Business Review*, December 2006.

Joshua D. Margolis, Hillary Anger Edfenbein and James P. Walsh, "[Does it pay to be good? A meta-analysis and redirection of research on the relationship between corporate social and financial performance](#)", unpublished paper, November 2007.

Goldman Sachs, "[Introducing GS SUSTAIN](#)", June 2007.

### Surveys:

Economist Intelligence Unit, "[Global business barometer: corporate responsibility](#)", November-December 2007.

McKinsey, "[Assessing the impact of societal issues: A McKinsey global survey](#)", November 2007.

McKinsey, "[Shaping the new rules of competition: UN Global Compact participant mirror](#)", July 2007.

Boston College, Centre for Corporate Citizenship, "[The state of corporate citizenship in the US](#)", December 2007.

### Websites:

[Business and Human Rights Resource Centre](#)

[UN Global Compact](#)

News and analysis on corporate responsibility from *Ethical Insight*

AccountAbility

SustainAbility

Business in the Community

Committee Encouraging Corporate Philanthropy

Business for Social Responsibility

## Offer to readers

Jan 17th 2008

From The Economist print edition

Buy a PDF of this complete special report, including all graphics, for saving or one-click printing.

*The Economist* can supply standard or customised reprints of special reports. For more information and to place an order online, please visit the [Rights and Syndication website](#).

## The food industry

## Son of Frankenfood?

Jan 17th 2008 | NEW YORK  
From The Economist print edition



Ben &amp; Jerry

**Produce from cloned animals has won regulatory approval. Now companies must persuade consumers to buy it**

[Get article background](#)

"IT IS beyond our imagination to even find a theory that would cause the food to be unsafe." With that ringing endorsement, Stephen Sundlof, the chief food-safety expert at America's Food and Drug Administration (FDA), this week declared food derived from the offspring of cloned cows, pigs and goats to be safe for human consumption. The decision came just days after the European Food Safety Authority (EFSA) publicly reached the same conclusion.

At first blush this seems likely to lead to a repetition of the controversies that surrounded the arrival of genetically modified organisms (GMOs) in agriculture more than a decade ago. Back then an over-zealous industry (led by Monsanto, an American GMO pioneer) touted the benefits of a novel food technology. Activist groups and parts of the media said GMOs were dangerous and unethical. Scientific bodies on both sides of the Atlantic agreed that GMOs could be used safely, but politics halted their advance in Europe.

Could the same saga unfold with cloning? Once again the biotechnology firms sound a bit brash, much as Monsanto did. James Greenwood, head of BIO, the lobbying arm of the American biotechnology sector, bragged this week to reporters that, thanks to his industry's efforts, animals have now been successfully cloned on six continents. David Faber, the head of Trans Ova, an American firm leading the charge, claims this technology will make possible "elite breeding" that will lead to faster-growing, disease-resistant and genetically superior animals.

To activists opposed to cloned food, meanwhile, the FDA and EFSA decisions mean only one thing: Frankenfoods are on their way. Since the creation of Dolly, a sheep cloned by researchers in Scotland in 1996, they have rallied many thousands to sign petitions and attend protest marches dressed as cloned cows and the like. And on the heels of this week's two big decisions, the anti-cloning crowd is kicking into high gear. Friends of the Earth lost no time in declaring it was organising a boycott of grocers who carry cloned products.

## Spot the difference

So far it all sounds like an identical copy of the fight over GMOs, which remain suspended in controversy in Europe even as they have taken off spectacularly in America, Brazil, India and other countries. The European Commission may well decide to overrule the scientific advice offered by the EFSA for political reasons, particularly if its expert committee, charged with considering the ethical aspects of cloned food, declares the technology objectionable. (At midweek rumours suggested the final report was about to be released.)

But there are three reasons to think that food from clones need not meet the same fate as GMOs. First, despite all the wild-eyed claims, cloning for food is not an especially radical procedure. It stretches credulity to claim, as Joseph Mendelson of America's Center for Food Safety does, that cloning animals for food will prove a "gateway technology" that will inexorably push society down a slippery slope to cloning humans. Drinking a glass of milk from the offspring of a cloned cow is unlikely to inspire you to clone your children.

It is true that cloning can be used as a step in the creation of transgenic animals, but the procedures approved this week do not involve transgenics: no foreign DNA is introduced. "It's just like having an identical twin, born at a different time," says one researcher. This suggests that cloning can plausibly be thought of as just another tool used by animal breeders alongside artificial insemination, in vitro fertilisation and so on. Cloning has long been commonplace in plant breeding.

Moreover, only the milk and meat from the offspring of clones—not food from the clones themselves—will be sold. This matters because cloning remains a difficult process, and many attempts fail. Catherine Geslain-Lanéelle, EFSA's executive director, concedes that "there are issues involved in animal welfare", but is convinced that the food-safety concerns are unsubstantiated. Since only the successful clones go on to reproduce normally, any food produced from the progeny is reckoned by the FDA to be indistinguishable from normal meat and milk.

The second reason cloning may not fall into the GMO trap lies in the simple fact that the food industry appears to have learned some lessons from the Monsanto saga. Despite their exuberance this week, the biotech firms involved in cloning took care to praise the American government's decision to maintain a "voluntary" moratorium on food from the cloned animals themselves. Unlike Monsanto, which tried to ignore such problems, today's genetic pioneers are eager to avoid trade friction. They emphasise their desire to build up stocks of cloned animals slowly (only about 600 exist in America, for example), and emphasise their scheme for tagging and tracking all clones.

The third reason to think cloned food may take off, even in places like Europe where GMOs have fallen flat, is the most straightforward one. Monsanto's Roundup Ready seeds and other early GMO products helped to reduce pesticide use and increase yields, which benefited producers but offered no compelling benefit to consumers. In contrast, if the industry's claims are to be believed, food from clones can be tastier, of higher quality and perhaps even healthier. That is because breeders will be able to use cloned animals to produce meat that is reliably leaner, better marbled or more tender, as customer whims dictate.

That points to an ironic twist. Despite these advantages over GMOs, cloned foods may yet hit a needless snag. Eager to avoid any stigma, the industry has persuaded America's regulator not to require any special labels on food from the progeny of clones. Instead, it says it will label only food that comes directly from clones, should it ever be allowed on sale.

Critics of cloning are predictably displeased. Andrew Barker of Ben & Jerry's (a "socially conscious" ice-cream firm whose co-founder, Jerry Greenfield, is pictured with protesters above) complains that the FDA's decision on labelling "has really created headaches for us with our supply chain". His customers and some foreign markets will reject cloned foods, he says, but he is not sure how he will be able to verify that his dairy products do not contain milk from the progeny of clones.

Yet advocates of cloning could also come to regret the lack of labels. If steaks made using cloning really do turn out to be healthier or tastier, punters who wish to buy them may not be able to identify them in the shops. If the industry is so confident about the merits of its products, it should not be afraid to label them.





## Corporate law

## The battle of StoneRidge

Jan 17th 2008 | NEW YORK  
From The Economist print edition

### America's Supreme Court reduces companies' risk of being sued

SIGHS of relief were audible in boardrooms across America this week at the Supreme Court's long-awaited decision in *StoneRidge Investment Partners v Scientific Atlanta*. At issue were the circumstances in which a company can be sued for "scheme liability". On January 15th the court ruled that a firm could not be held liable for a securities fraud merely because it was a business partner of a company that committed the fraud.

The ruling, regarded as the most important in years on corporate-securities law, related to a case brought by investors in Charter Communications, a cable-television firm. They had sued two companies, Scientific Atlanta and Motorola, arguing that they had helped Charter artificially boost its profits in 2000 through its accounting treatment of set-top boxes they had supplied to the cable firm. The court found that because neither Scientific Atlanta nor Motorola made any statements that had been relied on by the investors, they bore no scheme liability.

Robert Monks, a corporate-governance activist, had predicted that if the court ruled this way it would further reduce the accountability of American business to shareholders. In the past couple of years the Supreme Court has made several rulings favouring corporate defendants over shareholders. One immediate casualty of the *StoneRidge* ruling is likely to be a \$40 billion class-action suit against the financial-services firms that advised Enron. It is also likely to make it harder to bring successful suits against Wall Street advisers and ratings agencies over the subprime-mortgage meltdown.

Corporate lawyers had argued that, if the court found for the investors, it would increase the already excessive litigation risk facing firms, which acts as a deterrent to doing business in America. Though it is arguably the job of Congress, not the Supreme Court, to worry about the competitiveness of America's capital markets, that was clearly on the minds of the majority of the justices, who observed that, had they favoured the investors, "overseas firms with no other exposure to our securities laws could be deterred from doing business here...This, in turn, may raise the cost of being a publicly traded company under our law and shift securities offerings away from domestic capital markets."

## Regulation in Japan

### Crime and punishment

Jan 17th 2008 | TOKYO

From The Economist print edition

#### Errant Japanese firms are sometimes required to suspend their operations

[Get article background](#)

UNTIL January 13th visitors to certain parts of the [website](#) of Mitsubishi Heavy Industries received an odd message in Japanese and English. It explained that “for actions in violation of the Anti-monopoly Act of Japan”, the company had been ordered to suspend part of its domestic construction business. “As operation of the company website is considered one aspect of those activities, sections of the website have been closed.”

Regulators round the world sometimes find it difficult holding businesses to account for their infractions. Firms that fall foul of regulators can be fined, though they can then launch legal appeals that last for years. Forcing a company to shutter its operations for a while is rare in the West. But in Japan it is a popular form of punishment. In recent months it has been imposed upon several food companies and financial-services firms, among others. On January 11th the labour ministry ordered one of Japan's biggest temporary-staffing agencies, Goodwill, to close its branches for two months for placing workers in jobs they were not legally allowed to do, such as building and cargo-handling. Some branches must close for four months.

Financial penalties are considered ineffective, since companies can simply pay a fine and then pass the cost on to their customers in the form of higher prices, with little impact on corporate behaviour. Lengthy legal fights are expensive. And penalising individuals—as American prosecutors have done in recent years in response to a series of scandals—is of little use because of the Japanese ethos of collective responsibility. Executives are only too willing to accept punishment to protect their companies even if they are not directly responsible; meanwhile, bad practices continue unchecked. Threatening a suspension of activity that harms revenues and reputation, the thinking goes, is a better way to deter improper conduct.

There may also be a deeper cultural explanation for what, to Western eyes, seems an unusual approach. Under the Confucian tradition government has an absolute right to regulate all aspects of social and business relations for the common good, says Christopher Wells, a lawyer at White & Case in Tokyo. This may explain why there is no jury system, little right of appeal, and so on. There is a stark contrast with the Western legal tradition, based on individual rights and freedoms, which dates back to the Enlightenment. But in countries with Confucian traditions, such as Japan, Korea, Taiwan, China, Mongolia and Indonesia, the freedom of action of a person or company stems not from a fundamental right, but is based upon the “grant of a benefit” from the state. “A business suspension simply withdraws this grant from the beneficiary,” says Mr Wells.

An official in the Cabinet Office admits that suspensions are being used more frequently. He suggests that the rules surrounding suspensions need to be clarified to prevent the practice being applied too broadly or unfairly, not just by regulators, but by companies themselves. Interpreting such a sanction to include a website—which, for Mitsubishi Heavy Industries, is more akin to a shop window than a cash till—may seem extreme. Yet the company chose to close it of its own accord.

## Italy's violin cluster

## Con brio

Jan 17th 2008 | CREMONA  
From The Economist print edition

## Cremona's violin-makers lead the world once again

BIRTH, growth, decline, death: it is the usual cycle for people, companies and industries. But the story of violin-making in Cremona in northern Italy, which flourished under such master craftsmen as Andrea Amati, Giuseppe Guarneri and Antonio Stradivari from the mid-16th century to the early 18th, suggests that, for industries at least, there may be life after death.

Violin-making in Cremona struggled through the 19th century in the hands of a few carpenters who turned out low-quality instruments. By the 1950s it had died out, says Gio Batta Morassi, a 73-year-old *maestro liutaio* (master violin-maker). Yet today, in workshops overlooking the city's cobbled streets, more than 100 craftsmen cut and plane maple and spruce to make string instruments—more than in any other European city. Cremona is once again the capital of hand-crafted instruments.

A new school to train craftsmen in instrument-making opened in Cremona in 1938, though when Mr Morassi began his studies in 1950 there were just six students on the course, of whom only one other went on to make instruments. But this tenuous revival was sustained by a growing interest in Baroque music in northern Europe in the 1960s and 1970s, says Hildegard Dodel, a German who studied at the school. It created new demand for instruments made in the traditional Cremonese style.

Today Italians are a minority among the school's 150 students; 30 are South Korean, 26 are Japanese, six are from China and three from Taiwan. Some will set up shop in the city: Ms Dodel worked for about ten years restoring and repairing instruments in Germany and the Netherlands before returning to open her own workshop in Cremona in 2003.

Instrument-making is not an easy life. "I often thought of giving up," says Francesco Toto, who moved to Cremona 17 years ago and specialises in making cellos. Wood is expensive, must be seasoned properly and is at risk from woodworm; the maple for a cello costs around €1,500 (\$2,200), for example. Mr Toto was able to raise his prices after winning a competition, but to maintain quality he makes just four instruments a year. Violin-makers can produce perhaps seven top-quality instruments a year. (Cellos made by Cremona's craftsmen typically cost €15,000-35,000, and violins €8,000-20,000.) Having come back from the dead, Cremona's instrument-makers, like many others in Italian industries, hope that an emphasis on quality, tradition and craftsmanship will keep cheaper foreign rivals at bay.

## Spanish-language publishing

## Lost in translation no more

Jan 17th 2008 | GUADALAJARA  
From The Economist print edition

**Sales of books in Spanish are booming, and there is plenty of room for growth**

AT THE Feria Internacional del Libro (FIL), the largest Spanish-language publishing event, held a few weeks ago in Guadalajara, in Mexico, an eager teenager cadged your correspondent's badge at the exit. That young people might want to sneak into book fairs would be the stuff of dreams in many countries, where competition from other media is pushing books aside. But as FIL demonstrates with more than 500,000 visitors, up by 7% from 2006, Spanish-language publishers, and readers, have much to celebrate.

The market for books in Spanish is thought to be the second-largest in the world. It is the biggest for books in translation, which account for about a fifth of the 120,000 Spanish titles published each year. With sales up by 7.5% in 2005—growth is strongest in Argentina, Mexico and Colombia—it is expanding faster than many other book markets. Since many of the world's 400m Spanish-speakers live in developing countries, it has great potential: literacy rates are high and incomes are rising. (Ibero-American publishing, which also includes books in Portuguese, is worth about \$6 billion a year.)

Yet the industry has historically done a poor job of getting books to readers. In the 1970s a period of repression and economic crisis in Latin America concentrated Spanish-language publishing in Spain, where publishers were indifferent to Latin American markets. As a result, Spanish readers have for years had far broader access to Latin American works than have Latin Americans—who have also had little chance to buy books by foreign authors.

Now this is changing. In the past five years big international publishers such as Planeta, Santillana and Random House Mondadori have bought local imprints throughout the Spanish-speaking world. This lets them market books worldwide while selling at local prices, and scout for promising writers. Deals that offer rights across several regions are becoming more common. And although the number of titles published in Spain has declined slightly for the past few years, it is growing strongly in Latin America. Five Latin American countries now have higher rates of book readership than Spain.

Even so, distribution in Latin America remains difficult. As if to underscore this, a container of books was stolen on the way to Guadalajara. Counterfeits are also a problem for publishers. Riccardo Cavallero, boss at Random House Mondadori, the leader in Spanish-language paperbacks, says that in Chile sales of pirated books can equal those of legitimate copies.

There is also a wide variation between Spanish-language markets. Mexico has few bookshops—one for every 82,000 people, or an eighth of the number in Spain. And the enthusiasm at Guadalajara notwithstanding, the industry frets that readers are scarce or, sniffily, that they prefer self-help books to more elevated fiction.

Novelists and poets in Latin America are often prominent public intellectuals. In Mexico writers can still benefit from generous tax breaks, stipends and government appointments. "The idea is that culture generates the nation," says Álvaro Enríque, a novelist. This system may produce fine literature, but the resulting work does not always have broad appeal: a well-received Mexican novel may sell only 5,000 copies worldwide, though political non-fiction can sell 100,000 and be very influential.

Things are better in Argentina, by contrast. It has a bookshop for every 48,000 people, more than 2,000 public libraries, and avid readers. Its publishers produce nearly eight times as many titles as Mexico's, even with less than half the population. The economic crisis six years ago boosted local publishing by making imported books prohibitively expensive. Costs remain low there, and many companies—such as Planeta, which publishes the Spanish translations of "Harry Potter"—print books in Argentina for distribution abroad. The biggest hurdle now, says Daniel Divinsky, who publishes "Mafalda", a children's title that has sold more than 20m copies since the 1970s, is that Argentina's creaking printing

infrastructure is running at maximum capacity.

In some respects, the Spanish-language market is coming to resemble publishing in English. There has not been a strong tradition of blockbusters in Spanish, says Antonia Kerrigan, a literary agent based in Barcelona, but last year *“La Catedral del Mar”*, a first novel, sold 1.5m copies, making it Europe's leading seller and one of the top five in the world. There is also new interest in foreign translations of books written in Spanish. Gabriel García Márquez's *“Love in the Time of Cholera”* was recently a bestseller in America thanks to a Hollywood film, and he was treated like a rock star at FIL. He is not alone: in 2006 Javier Sierra's *“The Secret Supper”* also sold well in English.

Nonetheless, Spanish-language publishing remains structurally distinct: cut-price online booksellers, for example, have not had much impact, since rules in Spain and Argentina limit discounts on books. And in Mexico, Fondo de Cultura Económica, the largest publisher, is state-owned and has a monopoly on the lucrative textbook market. But once a book has made it into a reader's hands, such concerns do not much matter. *“All these things are unimportant,”* says Ms Kerrigan. *“You either write well, or you don't.”*

## Media in America

## Reading the Metro

Jan 17th 2008

From The Economist print edition

## Can free daily newspapers succeed in America?

WHEN Metro International, a Swedish publisher, launched its free tabloid newspapers in New York, Boston and Philadelphia, it seemed a logical move. Metro's papers are, after all, popular in over 100 cities around the world. With small articles and big pictures, they are an easy read on the way to or from work. And they are free: Metro makes money from advertising.

But things have not gone as planned. Henry Scott, a former publisher of *Metro New York*, says free daily papers generally become profitable in their third year of operation. After seven years Metro is still losing money in America: it lost \$4.4m in the third quarter of 2007 alone. Now there are rumours that Metro plans to sell its American business. Mr Scott says the real question is not if Metro will sell, but when.

Why has Metro's model failed in America? In part, its poor results may reflect the surprising strength of paid-for papers. Free papers cannot offer advertisers the mass audiences of larger titles: the *Boston Globe* has a daily circulation of around 380,000, compared with 160,000 for *Metro Boston*. Metro's papers may not be giving American readers what they want. *AM New York*, a free daily that competes with *Metro New York*, has done well by focusing on local coverage. The newer *BostonNOW* is attempting to do the same thing. Metro, by contrast, tends to emphasise national and international news. The free-paper model that works in Europe may need tweaks in other areas, too. In some cities the *Examiner* chain delivers its free papers to homes, which is expensive but may enable such papers to succeed in American cities with limited public-transport networks.

The *Examiner* has trademarked its title in some 70 American cities, but prints in just three so far. Dagsbrun, the Icelandic firm behind *BostonNOW*, has plans for ten American papers. Already, there are more than 40 free dailies around the country. Established publishers are getting involved: the New York Times Company bought a 49% stake in *Metro Boston* in 2005, and *AM New York* belongs to the Tribune Company. Even if Metro fails in America, others may succeed.

## Virtualisation

## The rise of the hypervisor

Jan 17th 2008 | PALO ALTO  
From The Economist print edition

## Is this the most disruptive technology in business computing since the internet?

HISTORY may not repeat itself, but it does sometimes rhyme. In 1980 when IBM asked Microsoft, then an unknown software firm, to provide the operating system for its personal computer (PC), it made the mistake of allowing its supplier to license the software, called DOS, to other hardware firms. DOS quickly became the dominant computing platform for the PC and the basis of Microsoft's might.

Two decades later Microsoft may have made a similarly seminal mistake. In 2002 it balked at paying a high asking price for VMware, then also an unknown start-up. VMware was later acquired by EMC, a big data-storage supplier, but the Silicon Valley firm remained largely independent. This allowed it to develop software that may yet emerge as a dominant platform in its own right—not for single computers, but for the vast warehouses full of machines, known as data centres, where much computing will be done in future.

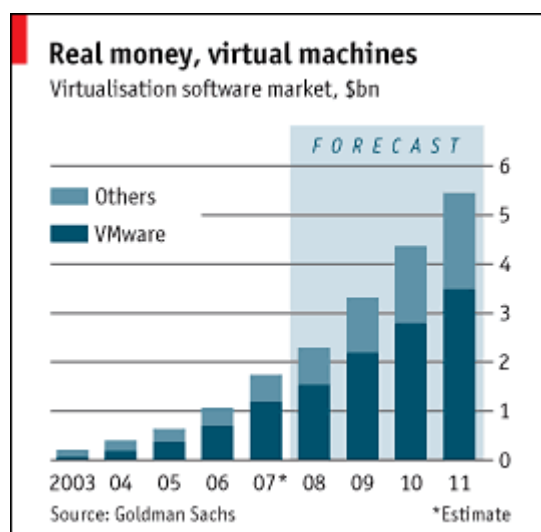
VMware's claim to fame is a technology called virtualisation, originally developed for big computers such as mainframes. It allows computers to split themselves into several "virtual machines", each of which can run its own operating system and applications, in effect separating software from hardware. To do this, VMware developed a small program called a hypervisor, which controls how access to a computer's processors and memory is shared.

Before VMware came along, virtualisation had lingered in obscurity. Rather than splitting up big machines, firms found it easier to use small ones for each new application. For a while, this was a rational strategy. Servers were cheap. Machines that ran more than one application were more likely to crash. Yet the approach led to "server sprawl", turning data centres into complex warrens of understretched hardware that required ever more people, space and power to keep them going. So it is hardly surprising that virtualisation, which allows multiple servers to be consolidated into a single machine, is one of the fastest growing areas in the software industry (see chart). As the software industry matures and consolidates—this week Oracle said it would buy BEA Systems, and Sun said it would buy MySQL—the emphasis has shifted away from fancy new technology and towards tools that cut costs and allow firms to do more with less.

Server consolidation is only the most obvious merit of virtualisation, however. Once computers have essentially become bits of software, getting new ones up and running takes minutes, not weeks. Even more important, servers can be moved around, even when in use. This allows for clever tricks such as concentrating virtual machines on as few computers as possible and switching off the rest to save energy. And particular server configurations can be packaged into downloadable and highly reliable "virtual appliances".

It is not just servers that can be disembodied. Desktop computers are next on the list, because virtualisation allows them to be managed centrally. Operating systems and applications need no longer run on PCs on desks, but can run on virtual machines in the data centre that can be accessed remotely—theoretically from any PC in the world. Storage is also getting more and more virtualised, so that data can be shunted around just as easily.

The ultimate goal of virtualisation is to make a data centre, or even several of them, look like a single pool of computing, storage and networking resources that can be allocated as needed. Thomas Bittman of Gartner, a market-research firm, calls this "real-time infrastructure". Yet for the vision to become





reality, something is still missing: a set of tools to manage all these computing resources—an operating system for the data centre, if you will.

VMware is well on its way to building just that. Founded ten years ago by a bunch of computer scientists and run by Diane Greene, it has become one of the fastest growing software firms, a fact that explains its blockbuster flotation last August (EMC still holds a majority stake). Although VMware is best known for its hypervisor, it now makes more money from a suite of other products, such as software to manage virtual machines. And it has been successful at persuading other computer firms to make their wares work well with its products, thus building an ecosystem around its emerging platform.

How was it possible for a newcomer to leave incumbents such as HP, Microsoft and Sun Microsystems in the dust? One reason was that VMware had the right product at the right time. More important, VMware delivered “a non-disruptive disruptive technology”, as Ms Greene puts it. Customers can install it without having to rejig their existing set-ups. By contrast, other virtualisation efforts were too ambitious and required extensive changes.

Now the industry's heavyweights are fighting back with a vengeance. In recent months they have announced big virtualisation initiatives. HP and Sun want to bring technologies developed for their high-end servers to the rest of the data centre. Microsoft, meanwhile, will integrate its own hypervisor, called Viridian, into the next version of its Windows operating system, essentially giving it away—and raising the spectre of yet another antitrust case. (On January 14th the European Commission opened two new investigations to see whether Microsoft abused its desktop monopolies to restrict competition.)

Yet the most interesting competitor is another newcomer: XenSource. It distributes its hypervisor as free, open-source software but sells related products. Simon Crosby, the firm's technology chief, likens this to giving away an engine in order to sell a car around it. He believes this approach will help to spread virtualisation more quickly and prevent VMware from becoming another Microsoft. XenSource now has the necessary backing, having recently been acquired by Citrix, another software firm, for \$500m. Some people think that if Microsoft fails to catch up with VMware on its own, it will buy Citrix.

Will VMware be able to withstand the collective onslaught? It is unlikely to crumble like Netscape, the most recent start-up to vie to become a new platform, since hypervisors are much harder to replace than browsers. And VMware has already reacted cleverly by slashing the price for its hypervisor and persuading hardware firms to embed it in their machines, putting it on a more equal footing with Microsoft when it comes to distribution.

Whatever happens to VMware, however, the virtualisation technology it has helped to popularise is here to stay—and will transform the economics of computing in the years to come. In particular, computing will be much easier to outsource. Perhaps the best way to understand virtualisation is to view it as an electronic form of globalisation: when borders disappear, everything is up for grabs.

## Face value

## Google's guru of giving

Jan 17th 2008

From The Economist print edition

Reuters

**At last, Larry Brilliant has set Google's philanthropy strategy. Now for the hard part**

"WHAT does a moral person do, given all the problems and suffering in the world? How do you focus?" Larry Brilliant illustrates how difficult this is by recalling a friend's struggle to decide how best to allocate a few rupees among the beggars waiting to die in the Hindu sacred city of Benares, in India. Such a place could hardly be more different from Google's headquarters in Mountain View, California—with its population of geeky 20-somethings, free food, volleyball courts and fake dinosaur—where Dr Brilliant and his 40-strong team have at last agreed a strategy for [Google.org](#), the internet giant's philanthropic arm, which Dr Brilliant leads.

The strategy, unveiled on January 17th, has been a long time coming. The announcement marks the end of the beginning of a mission that began before Google's initial public offering in 2004. As well as adopting the informal company motto, "Don't be evil", the internet search firm's co-founders, Sergey Brin and Larry Page, decided to commit Google to engage in serious philanthropy. Innovative as ever, they created a new sort of philanthropic entity, a division of the company that could pursue its mission through both for-profit investing and making charitable grants. This, they hoped, would one day "eclipse Google itself in overall world impact by ambitiously applying innovation and significant resources to the largest of the world's problems." It would be funded with 1% of the firm's equity, annual profits and employees' time.

In February 2006, after a lengthy search, Dr Brilliant was appointed to run Google.org. Media reports focused on the old hippy's colourful past, not least his spell as a doctor with the Grateful Dead, a legendary 1960s rock band. What attracted his new employers was his unique record of success both in running Silicon Valley tech firms and in implementing large-scale solutions to big social problems. In the 1970s, an appearance in a film featuring the Grateful Dead had taken him to India, and thence to a job with the World Health Organisation, where he helped to lead its successful smallpox-eradication programme. Later he created the Seva Foundation, which has prevented an estimated 3m people in nine developing countries from going blind. As a businessman, he ran two public firms and, in 1985, co-founded [The Well](#), a pioneering online service.

Though he has taken nearly two years to produce a strategy for Google.org, Dr Brilliant has not been taking things easy. He may have added a taste for Hindu meditation to his Detroit Jewish roots (he once shared a guru with Apple's boss, Steve Jobs), but he is a driven man, travelling widely and seeking advice from hundreds of people, pushing himself harder than friends say is wise for a sexagenarian. When he arrived at Google.org he found extraordinarily high expectations, a blank sheet of paper to fill with a strategy, and "microscopic attention" from outside on what it was doing.

Within a short time Google.org had compiled a list of over 1,000 ideas. These were reduced to 11, focused on the world's "biggest, most imminent, least well resourced problems". Each of the 11 was allocated to a different member of the Google.org team, who acted as its advocate in a process of further scrutiny and selection that Dr Brilliant likens to being in court. This led to the five initiatives announced this week. In these deliberations, the focus was on what Google specifically had to offer in each area, given its technological and engineering capabilities, mastery of information, entrepreneurial culture and global reach.

In broad terms, the outcome is not terribly surprising. Google.org will pursue five "core initiatives" in three areas: fighting climate change (a particular obsession of Messrs Brin and Page); economic development (a passion of Sheryl Sandberg, the unseen driving force behind the creation of Google.org); and building an early-warning system for pandemics and other disasters—something Dr Brilliant wished for when he won the 2006 TED Prize, which first brought him to Google's attention.

## **They're feeling lucky**

Accordingly, Google.org has made a \$5m grant to InSTEDD, a non-governmental organisation that is building a rapid-reporting platform to connect people on the ground with those monitoring pandemics. It hopes to raise the quality of public services in poor countries by improving the flow of information both to those who run them and to those they serve. It has big ambitions to help small and medium enterprises in developing countries. It is investing in the development of a plug-in electric car. And it has launched a project called RE<C to develop renewable energy that is cheaper than coal, "within years not decades".

Each of these initiatives is deliberately high-risk and high-return, says Dr Brilliant. If the pilots go well, Google.org plans to scale up fast; at the moment it is spending much less than Messrs Brin and Page promised. Dr Brilliant thinks that being effective demands a narrow focus: this week's announcement was as much about telling people inside and outside the firm what Google.org will not do as what it will. Among other things, it decided against getting involved in microfinance, which Dr Brilliant thinks is now awash with money, or trying to eradicate a disease (something he found especially hard to let go, given his personal history in the battle against smallpox).

In the 1960s Dr Brilliant bought into the anti-corporate zeitgeist, but "I must have been wrong," he says. Now he believes that companies can play a big part in solving the world's problems. Is Google.org, with its innovative mix of for-profit and non-profit strategies and political advocacy, within a corporate structure that denies it some of the tax and regulatory advantages of a traditional foundation, a new model for how a big firm should engage with society? "Let's see how we do first," says Dr Brilliant, showing why he has a reputation for being wise.

## Sovereign-wealth funds

## Asset-backed insecurity

Jan 17th 2008

From The Economist print edition

**Wall Street, the flagship of capitalism, has been bailed out by state-backed investors from emerging economies. That has people worried—for good reasons and bad**

Illustration by Daniel Mackie



IN REYKJAVIK almost two years ago the Norwegians were throwing their weight around and the locals were furious. Having spotted that an Arctic boom was about to end, a government-owned fund from Oslo must have thought it had found an easy way to make money in a market it knew well. It began to sell short the bonds of Iceland's over-stretched banks. Only common sense, you might argue.

Halldor Asgrimsson, then Iceland's prime minister, did not see things quite like that. Why was the Norwegian state investing hundreds of millions of dollars to undermine Iceland's economy? Had not both countries signed a Nordic mutual-defence pact against financial destabilisation? "We must protest against this action," he told *Morgunbladid*, a newspaper.

On Wall Street in the past few weeks, the sums have been bigger and the actions more benign—at least so far. This week Merrill Lynch and Citigroup became the latest to get the sovereign-wealth treatment, picking up a further \$6.6 billion and \$14.5 billion respectively, much of it from governments in Asia and the Middle East (see [article](#)). Sapped by the subprime crisis, rich-world financial-services groups have been administered nearly \$69 billion-worth of infusions from the savings of the developing world in the past ten months, according to Morgan Stanley.

Norse raiders one year and white knights the next, sovereign-wealth funds are as hard to grasp as shadows. In principle everyone welcomes foreign investment. But when the money belongs to other governments, people—especially politicians—are not always so sure. America's Congress has uttered barely a squeak as Wall Street's titans have taken foreign cash. But when credit was loose it was alarmed at the state-backed acquisitions of oil companies and ports.

Some funds, such as Norway's, behave as capitalists bent on making as much money as they can. Others may have "strategic" goals—to nurture national champions, say, or to galvanise regional development. Sovereign-wealth funds are a way to help recycle emerging-market surpluses. And yet suspicion about their motives could make their money much less welcome: rather than accepting investment from sovereign-wealth funds, countries could turn to financial protectionism.

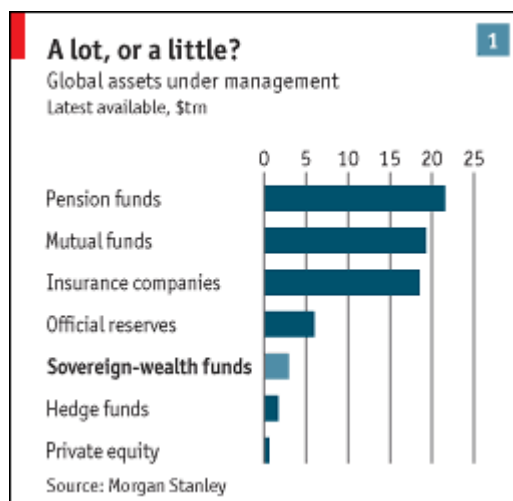
You can see why a call from Canada's Alberta Heritage Savings

Trust Fund may strike you differently from an offer by Venezuela's Investment Fund for Macroeconomic Stabilisation. The question of what to do with other governments' money is becoming more urgent by the month. The 29 sovereign-wealth funds monitored by Stephen Jen, an economist at Morgan Stanley who has followed them closely, are now worth about \$2.9 trillion (see table).

His list contains a wide range of funds. The Abu Dhabi Investment Authority, of the United Arab Emirates, worth \$875 billion, is biggest. But the table also includes the China Investment Corporation (CIC), which last year was sent into the world with \$200 billion in its back pocket; and Alaska's \$38 billion Permanent Fund, based on the state's mineral wealth.

Although sovereign-wealth funds make up only 2% of the world's \$165 trillion-worth of traded securities, they have a lot of firepower: more equity than private equity and more funds than hedge funds (see chart 1). In a paper for RGE Monitor, a research firm, Brad Setser and Rachel Ziemba conclude that the Gulf rivals China as a "new financial superpower".

Moreover, sovereign wealth is growing fast. Mr Setser and Ms Ziemba reckon that the Gulf's big funds could gain another \$300 billion to manage this year alone. If you combine that with Asia's surpluses and the marvels of compound interest, you soon get to some large numbers. Simon Johnson, the IMF's chief economist, thinks sovereign-wealth funds will be worth \$10 trillion by 2012. Mr Jen has pencilled in \$12 trillion for 2015. But even at that rate of growth, the funds will probably still account for less than 3% of global traded securities.



## League of nations

Sovereign-wealth funds  
Latest

Country: name	Assets* \$bn	Inception year
UAE: Abu Dhabi Investment Authority	875.0	1976
Norway: Government Pension Fund - Global	380.0	1996
Singapore: GIC	330.0	1981
Saudi Arabia: various	300.0	na
Kuwait: Reserve Fund for Future Generations	250.0	1953
China: China Investment Corporation†	200.0	2007
Singapore: Temasek Holdings	159.2	1974
Libya: Oil Reserve Fund	50.0	2005
Qatar: Qatar Inv. Auth.	50.0	2005
Algeria: Fond de Régulation des Recettes	42.6	2000
US: Alaska Permanent Fund Corporation	38.0	1976
Brunei: Brunei Inv. Auth.	30.0	1983
Other	171.4	-
<b>Total</b>	<b>2,876.3</b>	-
<i>of which oil- and gas-related</i>	<i>2,103.4</i>	-

\*Estimated, excluding Norway  
†Includes Central Huijin Investment Co.  
Source: Morgan Stanley

## Golden guano

The idea that governments should put something aside for a rainy day has a long and respectable history. Kiribati, a Pacific island country that mined guano for fertiliser, set up the Kiribati Revenue Equalisation Reserve Fund in 1956. Today the guano is long gone, but the pile of money remains. If it manages a yield of 10% a year, the \$400m fund stands to boost the islands' GDP by a sixth. Many oil producers now run similar schemes for similar reasons. Today's windfall is too big to spend in one go at home without waste and inflation. It is wiser to save for times when oil prices are low or for the generations who will come after the oil runs out.

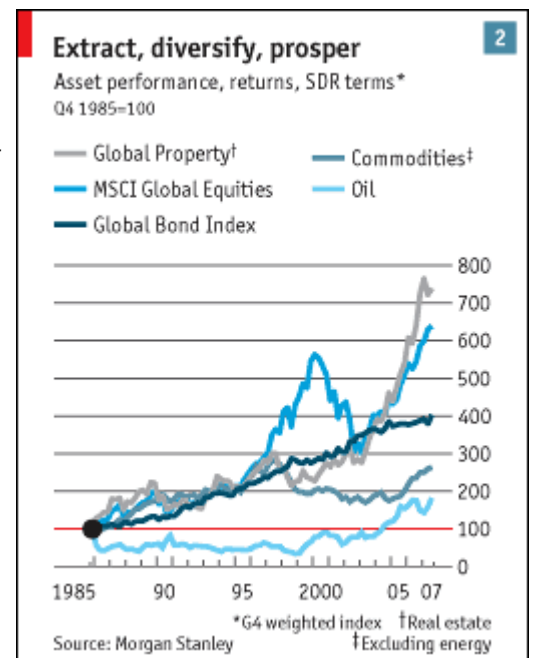
In addition, returns on a portfolio of assets are likely to be higher than on a single commodity. Chart 2 shows, for instance, by how much equities outdid oil between 1985 and 2007. Better for an exporter to sell as much oil as it can today and invest the proceeds, than to leave the stuff in the ground in the hope of spreading production over the decades. The recent run-up in the price of oil and other commodities only adds to the attraction of producing now while the going is good.

Commodities are not the only source of sovereign wealth. Many



Asian emerging markets have been running current-account surpluses at the same time as they have been managing their exchange rates. As they have mopped up dollars, using government bonds, they have accumulated reserves. At first these went into safe, liquid assets like American Treasury bonds—the Asian financial crisis of 1997-98 was still a recent memory and many countries were keen to amass reserves. But economies like China, South Korea and Taiwan now have more reserves than they need to defend themselves against shocks. Their governments understandably want to earn a higher return than Treasury bonds will pay, so they create a fund to manage their assets.

Like other sovereign funds, these tend to invest government money, often abroad and for long periods, in relatively risky assets. Yet the funds do not only come from a wide array of countries; they also have a variety of motives. Norway sees its stash as a pension fund. Russia and Iran have stabilisation funds, to counter the volatility of energy prices. China and South Korea want returns—and possibly access to markets, ideas and technology.



## Things that go bump

Whatever their motives, sovereign-wealth funds are sure to influence prices and markets. Mr Jen expects them to cast their money broadly across industries and economies. Hence they will buy assets priced in Japanese yen and emerging-market currencies; their governments' foreign-exchange reserves tend to be concentrated in dollars and euros. Mr Jen reckons about 40% of the funds' assets will be in dollars, compared with 60% of their countries' reserves. By contrast, he thinks a fifth of the funds' assets will be in yen, against just 2% of reserves.

As they spread their money around the world, sovereign-wealth funds will usually be greeted with open arms. Often, however, they will be treated with suspicion. Already, even as private-equity and hedge funds have retreated in the face of the credit crunch, they are being set up as the next villains of international finance.

For some, the nub of it is that governments are less interested in money than in power. Kevin Hassett of the American Enterprise Institute illustrates the worries by imagining that China bought Citigroup. What if America sought to take sides in a conflict with Taiwan and China and then threatened to shut the bank down? Or, less apocalyptically, suppose that Venezuela bought Alcoa and set about closing its aluminium smelters in the United States in order to move production to Latin America, as part of a strategy for development.

Others are worried for precisely the opposite reason: that the funds are interested chiefly in making money. This would not matter much but for the sheer size that some funds have now attained. They are big enough to shift markets—as the Norwegians and Icelanders discovered. The 21st century's successors to George Soros, who made a killing from sterling's ejection from the European exchange-rate mechanism in 1992, may not be a private fund-manager but the agents of foreign powers.

Yet, for all these imagined fears, it is hard to find examples of sovereign-wealth funds abusing their power. As with private-equity groups and hedge funds, the anxieties owe less to reality than to a mix of secrecy and suspicion. With a few exceptions, like Norway, which opts for disclosure, you cannot tell what a sovereign-wealth fund's objectives are, precisely how much money it manages and where it has made its investments. Already the funds use the full range of investment options, including hedge funds and private equity, which further covers their tracks.

Investing abroad for profit is hard enough: recall Japanese companies' bubble-era forays into Hollywood and New York. Running a business non-commercially is a recipe for huge losses rather than world domination: look at the history of France's *Crédit Lyonnais* or China's state-owned banks. Criticism of sovereign funds' investments has by no means all come from recipient countries. China's CIC seemed to have scored when it paid \$3 billion for a stake in Blackstone, a private-equity group that listed its shares. Today its holding is worth closer to \$2 billion and CIC has been lambasted in Beijing.

All this raises the question of who has the upper hand on Wall Street now. Are the investment banks selling cheaply, out of necessity? Or have the sovereign investors been seduced by Wall Street hustlers?

There are benefits on both sides, but maybe the American side is happier. The investment banks are getting much-needed capital. Most likely, their new shareholders will want to stay around for a while—or will find it hard to sell a lot of shares quickly if they do not. And via the new investors, Wall Street may enjoy better access to emerging markets. Certainly, American politicians have been glad enough to see emerging-market governments bail out their banking system—with funds that, Mr Setser impishly points out, have been flowing faster than IMF aid ever did to emerging markets in crisis.

## **Keep out**

Mutual admiration is not the rule. The first sovereign-wealth fund, the Kuwait Investment Office, created in 1953, ran into trouble in Britain two decades ago. In 1987 it bought more than 20% of British Petroleum, then recently privatised. The British government, headed by Margaret Thatcher, was in no mood to see so much of a national treasure owned by a foreign government—and an oil producer at that. Never mind the free market: the Kuwaitis had to sell more than half their stake.

In the United States more recently, controversy has centred on state-owned companies rather than acquisitive sovereign-wealth funds. The efforts of China National Offshore Oil Corporation to buy Unocal, a Californian oil company, in June 2005 roused opposition. And when DP World, a port operator owned by the government of Dubai, sought to take over P&O's business in America, which included terminals in New York and New Jersey, a huge fuss broke out about Arab ownership of strategic infrastructure.

Elsewhere, sovereign-wealth funds themselves have hit obstacles. In 2006 Singapore's Temasek sparked a row in Thailand by buying the family telecoms business of the then prime minister, Thaksin Shinawatra. Thais disliked Mr Thaksin's use of a loophole to avoid paying tax on the \$2 billion his family raised in the sale. But they also objected to Temasek as a buyer, because it is owned by Singapore's government. Temasek has also had trouble in Indonesia, over stakes in two telecoms companies bought by firms majority-owned by Temasek. At the time, Indonesia, smarting from the Asian crisis, was grateful for Singapore's capital. Now that telecoms is thriving again, Temasek seems no longer as welcome. Wall Street's sovereign investors, take note.

Such examples point to the greatest reason for concern about sovereign-wealth funds: although the risk that the funds may abuse companies and markets is theoretical, the danger of financial protectionism is all too real. The idea that secretive foreign governments are up to no good exerts a powerful hold on the collective imagination. Nicolas Sarkozy, the French president, and Angela Merkel, the German chancellor, have both issued warnings. A former American official, speaking on condition of anonymity, says that Washington is even now in a state of "high alert". He thinks the public debate about sovereign-wealth funds is the prelude to action against them and that the "kindling is dry".

A broad, politicised hostility to foreign direct investment would come at a high cost. Such investment spreads financial capital, know-how and technology. It helps the world economy adjust to imbalances and gives countries stakes in each other's prosperity. By contrast, as the dispute over DP World showed, conflicts over one investment can rapidly become generalised to others—either directly or through bodies like the Committee on Foreign Investment in the United States, which weighs up the implications of takeovers on national security. That spreads uncertainty, which could even spill over into the trade of goods and services. The European Union, for instance, now wants such a committee of its own.

Even now, suspicion of sovereign-wealth funds comes at a price. The investments in Wall Street have helped to stabilise the banking system, making this an ideal moment for active shareholders to be crawling all over the banks, asking what went wrong in the credit crunch and how to prevent the next. Instead, the banks have taken on large, friendly, long-term shareholders who cannot easily kick up a fuss. If the new investors were to become disgruntled, they may find it costly to sell in a hurry. And most of the funds know that if they cause trouble, people in Washington will soon get to hear about it.

## **Sovereign guarantees**

Moreover, a scandal of one sort or another is almost inevitable. With thousands of investments by hundreds of fund managers wielding trillions of dollars, someone, somewhere is going to do something



corrupt or foolish. That is why it makes sense to minimise the risk of conflict now.

Last summer Clay Lowery, an American treasury official, proposed that the IMF work on a code of conduct for sovereign-wealth funds. It is devising a scheme to make them more transparent. Shedding light on their strategy and investments should ease suspicion. But transparency alone gets you only so far: it does not, for example, stop abuse or protectionism.

Hence the importance of the OECD, which is looking at how host countries treat sovereign investors. It can draw on existing rules that are already widely accepted. Most countries, for example, limit who can own banks, because governments often guarantee deposits and because confidence in banks underpins the financial system. Similarly, most countries curb ownership of defence technology and utilities. You do not need a handbook of new restrictions. And you do not need to make sovereign-wealth funds a special case: instead, you have clear, predictable rules that apply to everyone.

The hope is that both host countries and sovereign-wealth funds see that their interest lies in building confidence. The hosts stand to benefit from the funds' capital. Meanwhile the funds are ruled by the politics of the places where they invest. You are sovereign only at home; abroad, someone else wields the power.

That is one reason why the managers of sovereign-wealth funds say they want only minority stakes. It is also a reason for them to have modest ambitions. Joshua Aizenman and Reuven Glick, in a note for the Federal Reserve Bank of San Francisco, point out that with such large sums to invest the funds should chiefly aim to keep pace with an index, rather than to invest strategically. Sometimes that will make sense politically, too. The former official advises: "If you want to invest in the US, be boring...Try to look like everyone else."

Sovereign-wealth funds are large and growing fast. Secretive and possibly manipulative, they are almost designed to raise suspicions. That is why the chief threat they pose is of financial protectionism. And it is why today's grand rescue on Wall Street is likely to lead to a backlash in Washington tomorrow.

## Global inflation

## A delicate condition

Jan 17th 2008 | HONG KONG AND WASHINGTON, DC  
From The Economist print edition

**Global inflation is rising even as the world economy is slowing. How much should policymakers worry?**

Illustration by Satoshi Kambayashi



HAVING a little bit of inflation is like being a little bit pregnant. Is that old adage worth bearing in mind as consumer prices across the globe accelerate? Even as America flirts with recession, figures released on January 16th showed that consumer prices were 4.1% higher in December than a year earlier, up from 2.5% in 2006. In the euro area, inflation is running at 3.1%, the fastest pace since the euro notes and coins began circulating. China's inflation rate, at 6.9%, is the highest in 11 years.

According to an index produced by Goldman Sachs, global inflation was 4.8% in the year to November, two percentage points up from the previous year (see chart). Prices accelerated in 80% of the countries that Goldman tracks.

By historical standards, this is all small beer. An inflation rate of 5% hardly marks a return to the double-digit price increases that haunted rich countries in the 1970s and emerging economies for far longer. (For much of the 1990s, the average inflation rate in poor countries was 50%.)

Nonetheless, the upswing is broad enough to pose awkward questions. With ever more signals, from weak retail sales to rising joblessness, pointing to an American recession, is the world headed for a bout of stagflation-lite? And will stubborn price pressures constrain the marked easing of monetary policy that America's central bankers now promise?

The answers depend on what has been driving inflation up and whether those pressures persist even as economies slow. Ultimately, inflation is a monetary phenomenon, so responsibility lies with central bankers. Pessimists point out that monetary conditions have been loose in recent years, with real interest rates low and credit growth rapid, particularly in emerging economies.

Others worry that the task of central bankers has become harder as globalisation has shifted from being a disinflationary phenomenon to an inflationary one. The downward price pressure from cheap Chinese



goods may be abating while the developing world's rampant demand for resources may continually drive commodity prices higher.

There is some truth to these arguments, but none offers a complete explanation of recent price trends. In some emerging economies monetary laxness is clearly fuelling inflation—in the Gulf states, for instance, as the direct consequence of their dollar pegs.

But elsewhere the picture is less clear. Take China, where fears of social unrest have made inflation one of the government's top concerns and have led it to impose various price controls over the past week. The accumulation of vast foreign-exchange reserves has fuelled domestic money growth and the inflation rate has tripled in the past year. But that rise is almost entirely due to a jump in food prices, particularly of pork. Core inflation (excluding food, but including oil) is running at only 1.4%. Pig disease deserves more blame for China's recent inflation than loose policy. What's more, China's monetary conditions are tightening fast.

Nor is China's deflationary effect on global tradable-goods prices about to end. To be sure, Chinese wages are accelerating, up by 19% in the year to September, the fastest pace for five years. But those official figures, which include only state-sector workers, almost certainly exaggerate overall wage increases. More important, China's productivity is growing faster, by 20% a year, according to America's Conference Board, a research organisation. That means overall unit costs are still falling.

It is true that the prices of American imports from China are rising after several years of decline. But that has more to do with the weakness of the dollar than with increasing Chinese production costs. And even if the prices of Chinese goods rise, they could still dampen inflation in richer economies, because they are much cheaper than domestically produced equivalents and are gaining market share. As China produces higher value items, it will push down prices of domestically produced goods in ever more industries.

A more direct link between developing countries such as China and inflationary pressure comes through commodity prices. The prices of many raw materials have surged in the past 12 months. *The Economist's* dollar-based commodity-price index is up by 26% from a year ago. The food index is up by almost 50%. The price of oil has risen almost 80%. These jumps are the main cause of higher inflation across the globe. They are also related, at least in part, to structural changes in the global economy.

The world economy is increasingly powered by countries, such as China and India, whose growth is far more energy- and commodity-intensive than that of rich countries. Since 2001, China has accounted for about half of the increase in the world's demand for metals and almost two-fifths of the increase in oil demand.

This shift means that the usual relationship between America's business cycle and commodity prices may change. Past American recessions have sent the prices of oil and other resources down. That may no longer be so. Economists at HSBC say that the correlations between industrial output and commodity prices began to fall apart a few years ago.

But that does not mean commodity prices will continue to surge. Emerging economies may be more resilient to an American recession than hitherto, but they are unlikely to grow faster. At the margin, therefore, the demand for commodities will slow. And in the longer term, higher commodity prices will eventually lead to greater supply. Much of the surge in raw-material prices in recent years reflects the fact that few foresaw the pace of emerging-market growth. All of which suggests that, even if commodity prices don't fall, their rate of increase will ease, and the biggest driver of recent global price pressure will weaken.

## **The weight of expectation**

So is it time to stop fretting about inflation? Not quite. For a start, a pick-up in underlying inflation suggests that price pressure has seeped beyond commodities. According to Goldman's index, core consumer prices, which exclude the volatile categories of food and fuel, are rising in some 70% of countries. Second, economic weakness does not immediately suppress underlying price pressure. Goldman's economists point out that during the 2000-02 global downturn, core inflation in G7 countries peaked more than a year after growth started to weaken. The rich world could easily face a prolonged period of weaker growth and persistent price pressure.

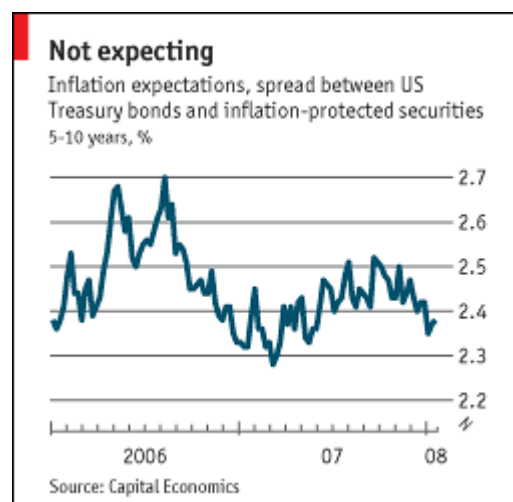
How much to worry depends on whether this combination affects people's expectations of future inflation.

Academic evidence suggests that low, stable inflation expectations are the main difference between today and the 1970s. Because central banks have earned a reputation as inflation fighters and people expect long-term inflation to remain low, price shocks—even on the scale of the recent commodity-price surge—need not translate into persistently higher inflation. Were workers and firms to expect higher inflation, and set wages and prices accordingly, central bankers would face a big problem.

That concern is haunting the European Central Bank (ECB). Judging by its survey of professional forecasters, long-run inflation expectations remain stable: the seers predict 1.9% in five years time. But consumers' expectations of price rises over the next year have risen quite sharply. What is more, unemployment is low and, judging by the unions' opening bids in pay negotiations from Germany to Italy, workers are demanding hefty wage increases. The risk of a wage-price spiral, albeit a modest one, is not negligible. The ECB's hawkishness—including threats that interest rates might have to rise—is designed to stamp it out.

The Fed has more leeway, though inflation has picked up faster in America than in the euro zone. Judging by the spread between American Treasury bonds and Treasury Inflation-Protected Securities, investors' expectations of inflation between five and ten years hence have been falling (see chart).

Given the American backdrop, the Fed's recent decision to step up the pace of interest-rate cuts is understandable. The weak economy poses a bigger danger than inflation. But there are risks. Even if commodity-price inflation wanes, the falling dollar means America faces other inflationary threats. And if overall price pressure remains stubbornly elevated, inflation expectations may yet rise. If that happens, the Fed will face the unenviable task of curtailing its easing or even raising rates while the economy is weak.



## Bank losses

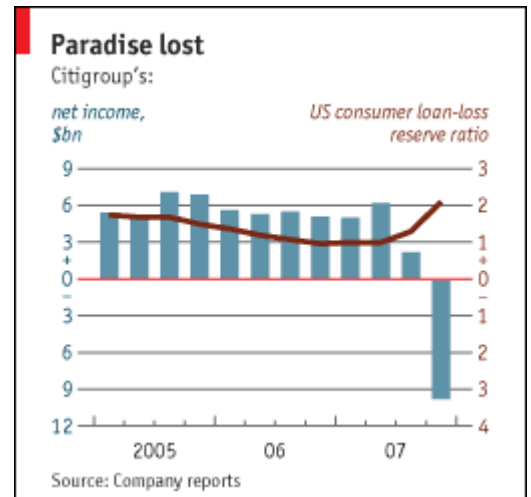
## A Citi situation

Jan 17th 2008 | LONDON AND NEW YORK  
From The Economist print edition

## The mother of all write-downs is unlikely to mark a turning-point

IT HAS a fearful symmetry to it. A year ago Wall Street banks were taking turns to chalk up record profits. Now they are sheepishly making history writing down curdled mortgage investments. Citigroup, the world's biggest bank by assets, is no longer by market value, plumbed new depths this week, reporting a \$9.8 billion fourth-quarter loss (see chart). It cut the value of collateralised-debt obligations (CDOs) and other nasties, already marked down heavily, by a further \$18.1 billion.

Citi's newish boss, Vikram Pandit, has a plan: a \$14.5 billion capital infusion from sovereign-wealth funds and others (including Citi's *éminence grise*, Sandy Weill), a dividend cut, and the jettisoning of "non-core" businesses and people. Bold stuff, but it was not enough to reverse the recent decline of bank shares or the overall stockmarket, which is growing increasingly alarmed about the prospect of a recession.



The good news is that fresh equity is available for capital-strapped banks. (Merrill Lynch, which was expected to announce a big write-down after *The Economist* went to press, also secured a large dollop this week.) They have also been cheered by the return of interbank lending rates to more normal levels, thanks to liquidity injections by central banks.

The first piece of bad news is that banks' prospects are just as murky as they were in August. Perhaps the most depressing aspect of Citi's results was the tone of remarks by its chief financial officer, Gary Crittenden. Valuing CDOs and the like "all gets extremely complex", he told analysts, and "it is very difficult to forecast exactly where all this is going." It does not help that there is no uniformity of valuation methods across the industry. Some banks rely heavily on the ABX index, which references mortgage-backed securities, as a benchmark. Others, including Citi, stick to their own models.

Worse, it is no longer just mortgages that plague banks (see [article](#)). Credit cards and other retail-finance businesses are fading with the American consumer. Citi reported a rise of \$4.1 billion in credit costs in its American retail business, the source of 30-40% of its profits in recent years. Other results this week from JPMorgan Chase and Wells Fargo told a similar story. Analysts at CreditSights, a research firm, think the picture will keep getting worse until late this year, though they do not expect credit-card and car-loan defaults to break records.

Provisions for bad loans are likely to grow fast as the extent of the contagion becomes clear—and as those banks that have squirreled away the least, such as Washington Mutual, catch up. Recent changes in accounting rules will amplify this, because it has become harder for banks to spread the building of reserves over the cycle. They must now wait to identify specific weak loans. As a result, provisions have become more pro-cyclical, says CreditSights, rising more sharply from low levels when markets turn.

Europeans should temper any *Schadenfreude* at the tales of woe across the Atlantic. American banks' write-downs may be bigger (Switzerland's UBS being the dishonourable exception) but analysts complain that standards of disclosure are worse in Europe. Hypo Real Estate, a German lender, shocked investors on January 15th by revealing a charge of €390m (\$570m) on its holdings of CDOs. The bank's share price fell by a third.

More bodies will doubtless be uncovered when European banks start reporting their year-end results in a couple of weeks. The economic headwinds are gentler than in America, but there are some familiar-

sounding worries: unwinding housing booms, falling commercial-property prices and rising defaults. And Wall Street banks are not the only ones hunting for cash. Capital needs, on some measures, are greater in Europe than in America; so is dependence on the wholesale markets for funding. On January 14th Crédit Agricole, a French bank, said it would sell its 2.1% stake in Suez, a utility, to help shore up its balance sheet. That more will follow is one of the few safe bets around.

## Buttonwood

## Finding default

Jan 17th 2008

From The Economist print edition

## What isn't known about bad debts

WHEN the American housing market turned, subprime borrowers started defaulting. The result was some nasty surprises for investors who had bought "structured" products that were exposed, in complex ways, to those housing loans. Now the overall American economy is flirting with recession, are similar surprises awaiting investors who have bought other types of consumer and corporate debt?

The best way to answer the question is to borrow Donald Rumsfeld's famous epistemological definitions. Defaults and delinquencies are known to be rising: companies like Citigroup and American Express have said so. But, given that consumer debts are high relative to GDP and that American house prices are falling nationwide for the first time since the second world war, might the level of bad debts be higher in this cycle? This can be classed as a "known unknown".

What happened in the subprime market was more of an "unknown unknown". There were several layers of middlemen between investors and house-buyers, most of whom had an incentive to overstate either house prices or a borrower's ability to repay. The effect was that mortgage-backed securities were less diversified than investors thought, since they were all exposed to the same risk—lax lending practices. That in turn was a problem when those bonds were carved up into collateralised-debt obligations, or CDOs: the risk of default affected the senior tranches of those products as well as the most junior.

Experts generally agree that the same problems should not occur in other parts of the debt markets. There has already been a consolidation into a limited number of experienced lenders in markets such as credit cards and auto loans. Those lenders are able to look back at consumer behaviour over several economic cycles for a reference point.

Moreover, other consumer-debt products are less complex than subprime. For example, there is no real "reset" problem outside the residential-mortgage market. Subprime borrowers were attracted by teaser loans, which offered low interest rates in the first two years, jumping sharply over the rest of the loan. As those teaser rates end, and without the possibility of refinancing, default rates are expected to rise further this year.

Credit cards have been subject to some unusual influences over the past two years, but the result has been historically low, rather than high, default rates. The explanation lies in a change in the American bankruptcy law in October 2005, which made going bust less attractive for borrowers. The result was a sharp rise in bankruptcies (and credit-card defaults) before the change came into effect, and an ever sharper fall thereafter. More than 600,000 Americans filed for bankruptcy in the fourth quarter of 2005, but barely 100,000 did so in the first three months of 2006. Since then credit-card delinquency rates have been rising steadily but remain well below the historic average.

Of course, worries about these other parts of the debt market remain. In recent years struggling consumers have been able to consolidate their credit-card debts into their mortgage loans; that option is no longer open. Will that affect default rates? And car companies have relied on cheap financing rates to maintain sales. Has that led to a decline in lending standards?

Then there is the corporate-loan market. Early last year the use of "covenant-lite" loans was a sign of the growing power of borrowers. In the past lenders often insisted on financial covenants when companies took out loans; breach of those covenants gave the lenders the right to take action. The idea was to spot troubled companies at an early stage of their decline, so that creditors had more hope of getting their money back. Covenant-lite loans removed some of those safeguards, creating the risk that default, when it occurred, would be more painful for creditors.

It may turn out that way, but it is rather too early to tell. Even relatively dodgy borrowers take time to



run through their money and come back to the market; Standard & Poor's, a rating agency, says that although more people will have to seek refinancing this year, the real peak will not occur until 2011-14.

Moody's, another rating agency, says it was less worried by the absence of covenants last year than by the more aggressive use of borrowed money (in particular, bank debt) in private-equity deals. A severe downturn in the economy that ate into business profits would be bad for such companies. But that risk is also well known: severe economic downturns were causing debt crises long before bankers learned to spell CDO.

## Indian IPOs

## Power play

Jan 17th 2008 | DELHI  
From The Economist print edition

## India plugs into the biggest IPO in its history

[Get article background](#)

IN OTHER countries, companies must keep quiet for a decent interval before they flog their shares to the public for the first time. But reticence is not the Indian way. In the run-up to Reliance Power's initial public offering (IPO)—which opened at 10am on January 15th and was oversubscribed by 10.01—the conglomerate missed no chance to drum up interest.

"Power on. India on," proclaimed the billboards and the newspaper adverts, trumpeting the virtues of a company that plans to build six power stations, generating over 7,000 megawatts (MW) of electricity, with the record 115 billion rupees (\$2.9 billion) it is raising. "Power on. India on," bleated Reliance mobile phones in the moments before a call was answered. Even Mumbai's renowned *dabbawalas*—the army of 5,000 men who ferry home-cooked meals to the desks of downtown office workers—handed out application forms alongside the lunchboxes.

"It's like a frenzy," says Arun Kapoor, a Delhi textile merchant. "They've created so much hoop-la in the market." He is sitting in the office of his broker, Amit Bhayana, who hangs his shingle from a crumbling balustrade overlooking Chandni Chowk, one of the city's busiest markets. Reliance Power has promised to reserve 30% of its offering for retail investors. Mr Kapoor is not buying, but Gouri Shankar, who sells "fancy printed saris" from a shop nearby, has asked for 225 shares, the maximum allowed. So have his friends and family. If he gets any, they will be the first shares he owns.

Indian stocks have a long history of hoop-la. A century ago, eager investors lined up "like Londoners waiting for first-night seats in the pit" to buy shares in the Tata Iron and Steel company. But 2008 promises to be extraordinary. In the first half of the year, as many as 34 companies may list, raising over \$14 billion, according to Thomson Financial, compared with \$4.6 billion in the same period of 2007. And on January 14th state-owned BSNL, India's biggest telecoms operator, said it hopes to offer the public a 10% stake, which might raise a whopping \$10 billion.

Can the Reliance frenzy be justified? As the company points out, India is desperately short of electricity. In November 2007 it could meet only 87% of its peak demand, and that demand is projected to double, more or less, in the next ten years.

By tradition, Indians have pretended to pay for their electricity and the utilities have pretended to supply it. Black-outs and brown-outs are part of life. In Chandni Chowk, the chugging of generators drowns out the growl of cars and auto-rickshaws. Perhaps 20% of electricity is still stolen or doled out by politicians in return for votes. Another 15% is lost in transmission. Collapsing overhead wires and other accidents killed 422 people and 583 animals in Gujarat in the 2006 fiscal year.

But India's Electricity Act of 2003 has stiffened the penalties for theft and sharpened the incentives for reform. Ajay Dwivedi of CRISIL, a rating agency, says that the government is geared up to do "whatever it takes to maintain the country's economic momentum".

Reliance Power has generated a lot of buzz. It has yet to generate a single watt of electricity. "It is just a



**How to spend almost \$3 billion a minute**

conception they are selling," says Mr Bhayana. The first plant will not begin production until the end of 2009 at the earliest. The biggest project of the six, an "ultra-mega power project" in Madhya Pradesh, has coal at its doorstep and 14 committed customers. But some of its other projects have yet to secure buyers or fuel supplies.

However, Reliance, the larger group of which Reliance Power is part, does have a track record of building power plants. For example, it has finished a 600MW project in Haryana in just 27 months, compared with the usual 45. Certainly, its new offshoot should be able to move faster than the state-owned generating companies, which have always fallen far short of the ambitions set out for them in the government's five-year plans.

These considerations hardly matter to the sari merchants and other retail investors who flocked to the company's offering this week. "All Reliance companies give good growth to shareholders," Mr Shankar says. His sceptical neighbour, Mr Kapoor, is less sure: "I'd rather wait and watch."

## Portuguese banks

**Millennium bug**

Jan 17th 2008

From The Economist print edition

**A banking pot-boiler comes to an end, for now**

FOR those who find the subprime crisis too arcane and like their banking dramas to have a bit more meat on them, events at Millennium BCP offer hearty fare. On January 15th shareholders in Portugal's largest listed bank voted at an emergency general meeting to install a new management team, hoping to put months of infighting and intrigue behind them. Boardroom harmony may prove hard to sustain, however.

The saga's roots lie in an embarrassingly public power struggle between Jorge Jardim Gonçalves, the bank's founder and recently departed chairman, and Paulo Teixeira Pinto, the man picked by Mr Jardim Gonçalves to succeed him as chief executive. Their disagreements over strategy, not least over BCP's failed €5.3 billion (\$7.2 billion) attempt to buy Banco BPI, a local rival, were echoed among shareholders as each man rallied supporters to his cause.

First blood went to the old guard—Mr Teixeira Pinto fell on his sword in August, to be replaced by Filipe Pinhal. But since then BCP's newer shareholders have fought back hard. Mr Jardim Gonçalves, weakened by accusations of illicit lending to his son, left the bank in December. A second scandal, this time involving alleged offshore trading by the bank in its own shares, increased pressure on Mr Pinhal. Another round of public fighting, and more damage to BCP's image, loomed.

That prospect was enough for Portugal's central bank to step in. A clean break with the past was needed, it intimated. Mr Pinhal and other board members grudgingly withdrew their candidacy for a renewed mandate. Shareholders nominated a brand new list of executives, headed by Carlos Santos Ferreira, who resigned as boss of state-owned Caixa Geral de Depósitos (CGD) to run BCP and now becomes the bank's third head in five months.

Peace in our time? Perhaps. Mr Santos Ferreira is an outsider to BCP, who won the support of both the warring shareholder factions. He is not tarred by the scandals of the past. Nor is he a neutral figure. The intervention by the central bank and his ties to the country's ruling Socialist Party have had the effect of politicising his appointment. A rival slate of candidates, headed by a former finance minister in the main opposition party, failed to win support from BCP's big shareholders at the meeting but did win favour among smaller investors. Mr Santos Ferreira will need to distance himself from the government if one type of factionalism is not to be swapped for a much broader kind.

Older, strategic headaches are also likely to return. Past attempts to hook up with Banco BPI (which later countered BCP's hostile bid with a merger proposal of its own) made plenty of sense, and not just because of the cost savings a deal would offer. BCP's domestic growth opportunities are limited, particularly now that Portugal's economic recovery is weakening and funding has become more expensive. According to Kato Mukuru, an analyst at Citigroup, a combined bank would have both a striking international footprint, taking in fast-growing markets in Poland, Greece and Angola, and the financial strength to expand further.

The immediate prospects of a return to the negotiating table are dim: Mr Santos Ferreira did not give up his old job at CGD in order to hand over power at his next one. Shares in BCP dropped sharply on January 16th as investors started to discount the possibility of dealmaking. But the realities of the Portuguese market will eventually reassert themselves. Mr Santos Ferreira has the backing of his shareholders for now, but it will not last for ever.

## American house prices

## Baby boom and bust

Jan 17th 2008 | ANN ARBOR, MICHIGAN  
From The Economist print edition

## The housing market has a new problem: ageing Americans

IN THE first years of the 21st century, no area of the American economy has excited more emotion than the property market. First came the excitement of soaring prices. Then spirits came crashing down with the subprime crisis, and now homeowners are agonising over how far values could fall. An even bigger story, however, may be yet to come.

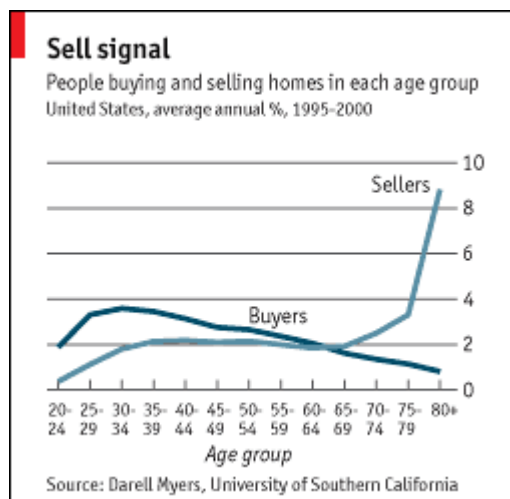
America should be bracing itself for the end of the “generational housing bubble”, according to a new study by Dowell Myers and SungHo Ryu of the University of Southern California. As the country's 78m baby-boomers retire, the report argues, the housing market will change dramatically.

For three decades baby-boomers have helped push prices up: they settled down, then bought bigger houses and second homes. But as the first of them celebrate their 65th birthdays in 2011, this may change. The old sell more homes than they buy, according to data covering 1995-2000 (see chart). The ratio of old to working-age people is expected to grow by 67% over the next two decades. Will the younger generation be able to buy all the homes on the market?

Young adults make up the bulk of new demand, with most purchasing homes when they reach their early 30s. The flood of elderly people selling their homes, Mr Myers suggests, may lead to a drawn-out buyers' market. Prices may fall further as younger people, perceiving a downturn, delay purchasing.

This phenomenon will unfold differently across the country. Some states will begin the sell-off later than others. In 15 southern and western states—including the retirement magnets of Florida and Arizona—the elderly do not become net sellers until their 70s. Expensive states such as California and the cold states of the midwest and north-east are likely to lose them more quickly. The mismatch between buyers and sellers may be most acute in the rustbelt, where numbers of young people and immigrants are rising slowly, if at all, says William Frey of the Brookings Institution, a think-tank.

Of course, there may be other outcomes. Suburbs, which swelled with the baby-boomers, may begin to decline. If the building industry contracts, home prices may remain more stable. Or developers may switch to serving the old, building more compact housing near amenities. Towns may make new efforts to attract immigrants, who already accounted for 40% of the growth in homeownership between 2000 and 2006. Among these unknowns, one thing is more certain: the housing market is about to enter a long period of transition. The youngest baby-boomers will not turn 65 until 2029.



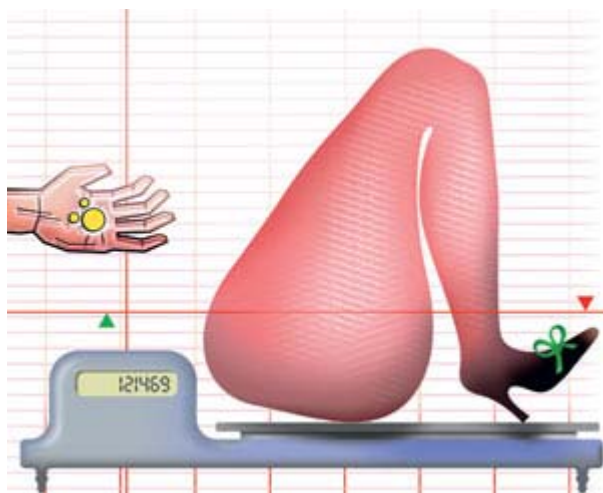
**Economics focus****Selling sex**

Jan 17th 2008

From The Economist print edition

**Economists let some light in on the shady market for paid sex**

Illustration by Jac



IT IS all too easy to become a lost soul in New Orleans. The annual meeting of the American Economic Association this month was part of a huge gathering of social scientists sprawled across the city. Each venue itself was a warren of meeting rooms. Take a wrong turning and a delegate seeking an earnest symposium on minimum wages might innocently end up in the conference session devoted to the market for paid sex.

The star attraction there was Steven Levitt, an economics professor at the University of Chicago and co-author of "Freakonomics", a best-selling book. Mr Levitt presented preliminary findings\* from a study conducted with Sudhir Venkatesh, a sociologist at Columbia University. Their research on the economics of street prostitution combines official arrest records with data on 2,200 "tricks" (transactions), collected by Mr Venkatesh in co-operation with sex workers in three Chicago districts.

The results are fascinating. Almost half of the city's arrests for prostitution take place in just 0.3% of its street corners. The industry is concentrated in so few locations because prostitutes and their clients need to be able to find each other. Earnings are high compared with other jobs. Sex workers receive \$25-30 per hour, roughly four times what they could expect outside prostitution. Yet this wage premium seems paltry considering the stigma and inherent risks. Sex without a condom is the norm, so the possibility of contracting a sexually transmitted infection (STI) is high. Mr Levitt reckons that sex workers can expect to be violently assaulted once a month. The risk of legal action is low. Prostitutes are more likely to have sex with a police officer than to be arrested by one.

Pricing strategies are much like any other business. Fees vary with the service provided and prostitutes maximise returns by segmenting the market. Clients are charged according to their perceived ability to pay, with white customers paying more than black ones. When negotiating prices, prostitutes will usually make an offer to black clients, but will solicit a bid from a white client. There are some anomalies. Although prices increase with the riskiness of an act, the premium charged for forgoing a condom is much smaller than found in other studies. And attractive prostitutes were unable to command higher fees.

By chance, the authors were able to study the effects of a demand shock. As people gathered for the July 4th festivities around Washington Park (one of the neighbourhoods studied), business picked up by around 60%, though prices rose by just 30%. The market was able to absorb this rise in demand partly because of flexible supply. Regular prostitutes worked more hours and those from other locations were

drawn in. So were other recruits—women who were not regular prostitutes but were prepared to work for the higher wages temporarily on offer.

One controversial finding is that prostitutes do better with pimps—they work fewer hours and are less likely to be arrested by the police or preyed on by gang members. The paper's discussant at the conference, Evelyn Korn of Germany's University of Marburg, said that her favourite result from the study was that pimps pay “efficiency wages”. In other words, pimps pay above the minimum rate required by sex workers in order to attract, retain and motivate the best staff. Mr Levitt said that a few prostitutes asked the researchers to introduce them to pimps.

A separate paper\*\* on sex workers in Ecuador echoed some of these findings. As in Chicago, the paid-sex market in Ecuador is tiered, with licensed brothel workers earning more per hour than unlicensed street prostitutes. These gradations might reflect different tastes: brothel workers tend to be younger, more attractive and better educated. They are also slightly less likely to have an STI. Condom use is the norm: 61% of street prostitutes surveyed used a condom in the previous three transactions. In Chicago, condoms were used in only a quarter of tricks.

## What about the johns?

These studies contribute to our understanding of the suppliers of paid sex, but tell us little about their customers. The session's organiser, Taggart Brooks of the University of Wisconsin, attempted to fill this gap in knowledge. He shed light on the sex industry's demand side in his analysis† of men who attend strip clubs. He argued that habitués of strip clubs featuring nude or semi-nude dancers are in search of “near-sex”—an experience of intimacy rather than sexual release. They are aware that paid sex is on offer elsewhere, should they desire it.

Strip-club patrons are more likely to be college-educated (cue some uneasy seat shifting from conference delegates), to have had an STI, and to have altered their sexual behaviour because of AIDS, than non-patrons are. They are typically unmarried, relatively young (against the stereotype of old married men) and are characterised as “high-sensation seekers”.

Although all speakers at the session were careful not to draw very strong conclusions from preliminary findings, a few broad themes nevertheless emerged. In many respects, the paid-sex industry is much like any other business. Pricing strategies are familiar from other settings. Despite evidence of a myopic attitude towards risk, there have been plenty of recent examples of that in the finance industry too. Illegality and lack of regulation are likely to heighten public-health risks. The Ecuador study concluded that rigorous policing of street prostitution might limit the spread of STIs by directing sex workers into the safer environs of licensed brothels. For an audience facing an evening away from home in the Big Easy, there was much to ponder.

---

\* [“An Empirical Analysis of Street-Level Prostitution”](#)

\*\* “Sex Work and Infection: What's Law Enforcement Got to Do with it?” by Paul Gertler (University of California, Berkley) and Manisha Shah (University of Melbourne)

† [“In Da Club: An Econometric Analysis of Strip Club Patrons”](#)



## Pricing and the brain

### Hitting the spot

Jan 17th 2008

From The Economist print edition

**People do not just say they enjoy expensive things more than cheap ones. They actually do enjoy them more**



EVERYONE loves a bargain. But retailers know that people will sometimes turn their noses up at a cheap version of a more expensive item, even if the two are essentially the same. That suggests something is at work in the mind of the consumer beyond simple appreciation of a product's intrinsic qualities.

The something in question is expectation, according to research published this week in the *Proceedings of the National Academy of Sciences* by Antonio Rangel of the California Institute of Technology. Dr Rangel and his colleagues found that if people are told a wine is expensive while they are drinking it, they really do think it tastes nicer than a cheap one, rather than merely saying that they do.

Dr Rangel came to this conclusion by scanning the brains of 20 volunteers while giving them sips of wine. He used a trick called functional magnetic-resonance imaging, which can detect changes in the blood flow in parts of the brain that correspond to increased mental activity. He looked in particular at the activity of the medial orbitofrontal cortex. This is an area of the brain that previous experiments have shown is responsible for registering pleasant experiences.

Dr Rangel gave his volunteers sips of what he said were five different wines made from cabernet sauvignon grapes, priced at between \$5 and \$90 a bottle. He told each of them the price of the wine in question as he did so. Except, of course, that he was fibbing. He actually used only three wines. He served up two of them twice at different prices.

### What is truth?

The scanner showed that the activity of the medial orbitofrontal cortices of the volunteers increased in line with the stated price of the wine. For example, when one of the wines was said to cost \$10 a bottle it was rated less than half as good as when people were told it cost \$90 a bottle, its true retail price. Moreover, when the team carried out a follow-up blind tasting without price information they got different results. The volunteers reported differences between the three "real" wines but not between the same wines when served twice.

Nor was the effect confined to everyday drinkers. When Dr Rangel repeated the experiment on members

of the Stanford University wine club he got similar results. All of which raises the question of what is going on.

There are at least two possibilities. The point of learning is to improve an individual's chances of surviving and reproducing: if the experience and opinions of others can be harnessed to that end, so much the better. Dr Rangel suspects that what he has found is a mechanism for learning quickly what has helped others in the past, and thus for allowing choices about what is nice and what is nasty to be made speedily and efficiently. In modern society, price is probably a good proxy for such collective wisdom.

However, goods can be desirable for a reason other than survival value. Many of the things for which high price is an enhancement are purchased in order to show off, as any male confronted with the wine list in a fancy restaurant knows. Indeed, conspicuous consumption and waste are an important part of social display. Deployed properly, they bring the rewards of status and better mating opportunities. For this to work, though, it helps if the displaying individual really believes that what he is buying is not only more expensive than the alternative, but better, too. Truly enjoying something simply because it is exclusive thus makes evolutionary sense.

Besides its role in giving cachet to wine, this may be the explanation for the sort of modern art that leaves the man in the street cold. Art collecting is a high-status activity *par excellence*. Many lowlier mortals regard it as pretentious. If Dr Rangel is right, though, pretence may not be the true explanation. The collector who has paid millions for a plain-coloured canvas or a pickled sheep probably really does think it is beautiful.

Whichever explanation is correct (and both might be), Dr Rangel's research also has implications for retailers, marketing firms and luxury-goods producers. It suggests that a successful marketing campaign can not only make people more interested in a product, but also, truly, make them enjoy it more.

## Acoustic shielding

## Sound reflections

Jan 17th 2008

From The Economist print edition

## How to stop echoes giving you away

IN GREEK mythology, Echo was a mountain nymph who lost her voice and was condemned to repeat only the words of others. Now science is poised to silence the sprite completely. A group of physicists, led by Steven Cummer of Duke University in North Carolina, has devised plans for a cloak that would shield objects from sound, preventing its reflection. Such a device could be used to hide submarines.

Sonar, the technique employed to detect subs, uses a transmitter to emit a pulse of sound—usually a distinctive “ping”—and a receiver to listen for its reflection. That reflection indicates the presence of an object and the time that elapses between the sound's being emitted and its being detected indicates how far away it is. A second ping allows the object's direction, speed and location to be calculated.

Dr Cummer, however, has devised a plan to surround a submarine with a shell that directs sound waves to flow around it as though the vessel were not there. The proposal relies on two properties of the material used to make the shield—its density and its “bulk modulus”, a measure of its springiness. It should be possible to tailor these so that sound waves are bent such that no echo results. The design would also avoid absorbing sound, ensuring no acoustic “shadows” were cast.

Dr Cummer's method, reported in the current issue of *Physical Review Letters*, is akin to an existing design for an invisibility cloak that would work for light waves, proposed by Sir John Pendry of Imperial College, London. (Sir John is also one of the authors of the new paper.) Yet the acoustic version has a distinct advantage over its optical counterpart. Making an invisibility cloak would be tricky because the device would work only at certain wavelengths. An aeroplane shrouded in such kit might be invisible to the human eye, for example, but would be picked up readily by radar, which works at radio wavelengths.

An acoustic cloak, however, would work for a wider range of wavelengths, making it far harder to spot. That is possible because light and sound are rather different sorts of waves. As Einstein observed, light in a vacuum travels at the greatest speed possible, around 300m metres a second. Even when it is slowed by air and water, its progress usually remains close to this limit. That means light must obey the rules of Einstein's special theory of relativity. When light is bent by an invisibility cloak, certain components of the wave are allowed to stretch the laws of physics and travel faster than the nominal speed of light, but only under strict conditions. The energy and the information that the wave carries, for example, cannot exceed the speed of light. The effect is to narrow the range of wavelengths that can be bent by an optical shroud.

Sound, meanwhile, travels at a sedate 300 metres a second. Because this is a million times shy of the relativistic limit, the behaviour of sound waves is not restricted in the same way. Under non-relativistic conditions, many different wavelengths can be bent simultaneously by the same acoustic shield, making it far more effective at concealing an object.

It was unrequited love that made the Echo of Greek mythology fade away until only her voice remained. Although Dr Cummer and his colleagues are still some way from transforming their design into a working device, they reckon precisely engineered materials may soon erase her final utterances.

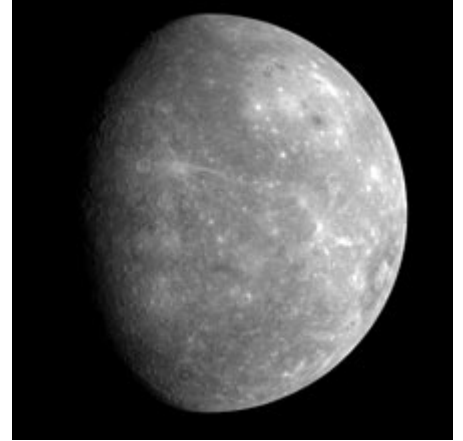
## A messenger from Mercury

Jan 17th 2008

From The Economist print edition

This is one of the first close-up photographs of Mercury taken for almost 33 years. It was snapped by a spacecraft called *MESSENGER* that was launched by NASA, America's space agency, in 2004. The craft's name, an allusion to Mercury's role as the messenger of the gods of ancient Rome, is one of the most contrived examples of reverse acronyms ever to come out of an agency famous for the art. It supposedly stands for MErcury Surface, Space ENvironment, GEochemistry and Ranging. The picture is mostly of parts of the planet unmapped during the previous mission to Mercury, by *Mariner 10*.

Reuters



## Syphilis

## Montezuma's revenge

Jan 17th 2008

From The Economist print edition

## Uncovering the origin of syphilis

IT WAS called the “French disease” by the Italians and the “Italian disease” by the French. In the Netherlands it was assumed to be Spanish; in Russia, Polish. The Turks thought it was a Christian affliction. The Tahitians thought it came from Britain. According to Kristin Harper of Emory University in Georgia, they were all wrong. Syphilis, the illness with so many suspected origins, actually came from the New World. In other words, Columbus brought back much more than knowledge of an unsuspected continent from his travels.

For hundreds of years, people have debated whether syphilis came from the Americas or whether it, along with a number of closely related diseases, had a much longer history in Europe. Because the first undisputed outbreak was recorded in 1495, shortly after Columbus's return, circumstantial evidence suggests an origin on the western shores of the Atlantic. But now science has turned to genetics in search of a definitive answer.

Dr Harper and her colleagues wanted to find out how syphilis was related to the bacterial pathogens responsible for other so-called treponemal diseases: yaws, endemic syphilis and pinta. These three infections are not transmitted sexually, as syphilis is, but by skin-to-skin or oral contact. However, her team faced a problem: collecting samples was difficult. During the 1950s and 1960s, the World Health Organisation undertook a huge eradication campaign in which more than 300m people in Africa, South America, South East Asia, the South Pacific islands and the Middle East were examined—and tens of millions were treated with penicillin.

Reducing the burden of disease by 95% was good for patients, but not so good for paleopathologists. Instead, the team had to gather together the world's entire laboratory collection of treponematoses, and collect strains of the disease in wild baboons and rabbits. In addition, they were able to locate two specimens of yaws from the only known site of active infection in the Americas: Amerindians living far inside Guyana. In all, they managed to find 26 genetic sequences from different types of treponemal bacteria.

Comparing such data allows educated guesses to be made about which species are most closely related and what evolved when. The first thing Dr Harper found, as she reports in the *Public Library of Science*, was that of all the treponematoses, yaws was most likely to resemble the ancestral pathogen. This supports a theory that yaws is an “heirloom disease”: one caused by a bacterium that infected humanity's ancestors and that has evolved with the species as people have spread around the world. Syphilis, though, emerged relatively recently in evolutionary terms.

The two Guyanese samples of yaws were a crucial component of this study, because they appeared to be the closest relatives of venereal syphilis and were genetically different from Old World species of yaws. Indeed, critics of the study reckon Dr Harper is relying too much on them, since the differences in question may be the result of local natural selection rather than the type of random mutation that this sort of analysis depends on. She, though, thinks the evidence suggests that an ancestral disease resembling yaws first arose in the Old World as a non-venereal infection. It spread to the Middle East and eastern Europe, and then on to the Americas in the form of New World yaws when humans crossed the Bering strait some 13,000 years ago. Finally, syphilis was introduced back into the Old World as a result of European exploration.

It is possible that when a bug that came from the moist, tropical New World arrived in the cooler climes of Europe it survived by adapting to the nearest thing European man (and woman) has to a tropical environment: the genitals. Thus freed from external constraint, it used the French, the Italians, the Dutch, the Spaniards, the Russians, the Poles, the Turks, the Tahitians and even the British to become the global success that it is today.



## Antarctic science

## Snow place like home

Jan 17th 2008 | THE SOUTH POLE  
From The Economist print edition

## America's new research station at the South Pole is officially opened



MOVING house is always traumatic, and the odd tear would have been forgivable as the flag came down over America's old base at the South Pole. It was handed from person to person along a line of scientists and support staff like an egg being passed between penguins. Slowly, it made its way past the marker that represents the exact point of the Pole, and then on to its new staff outside the third incarnation of the Amundsen-Scott station that is the home of America's scientific effort at the Pole. This new station, which formally opened for business on January 12th, took almost 20 years to design and build, and cost \$174m. It will house researchers from fields as diverse as neutrino astronomy, cosmology, seismology and atmospheric physics.

The first polar base was established in 1957, during the International Geophysical Year. Eventually, it succumbed to the elements and was buried under years of snowdrift. It was followed by a geodesic dome, an unheated structure filled with small shipping containers that served as buildings. That, too, is now partially buried and is scheduled for demolition over the next few years.

The latest station, though, is designed to stave off the fate of its predecessors by using the very elements against themselves. The building rests on 36 steel columns, elevating it four metres above the surface of the ice. Using detailed computer simulations, its designers have arranged its orientation and aerodynamic exterior to accelerate the gale-force winds that blow over the pole and channel them underneath the station. The resulting gusts scour the ice surface, depositing snow on the other side instead of letting it build up against the station itself.

However, in Antarctica, the elements are relentless. Eventually, over a period of about 15 years, snowdrifts will build up. When they do, the designers have another trick up their sleeves. Using hydraulic jacks, the entire building can be raised. Extensions another four metres long can be added to the steel columns, and the scouring can begin anew. Two such extensions will add 30 years to the base's life.

Once inside, not all is so strictly utilitarian. The station has many of the comforts of home—a full-sized gym for volleyball and basketball, an exercise room, a music room, an arts-and-crafts room and a library. For those needing an escape from the 24-hour sunlight (or 24-hour darkness), there are lounges with televisions, a pool table and a good supply of beer and Scotch whisky. And for those who prefer a healthier diet there is also a hydroponic greenhouse where fresh vegetables will grow all year round.

Each of the 750 people who will pass through the base in a typical summer season will have the luxury of a private room with a phone and an internet connection. In fact, it sounds just the place for an exotic holiday. So, to remind the inhabitants that this is, indeed, Antarctica, they will be allowed to shower only twice a week.





## The secret of happiness

### It's in Iceland

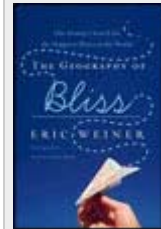
Jan 17th 2008

From The Economist print edition

**The search for happiness is becoming more scientific. But does that make it any more accurate than it used to be? Two books explore a growth industry**

The Geography of Bliss: One Grump's Search for the Happiest Places in the World

By Eric Weiner



*Twelve Books; 352 pages; \$25.99*

Buy it at

[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

Against Happiness: In Praise of Melancholy

By Eric G. Wilson



*Farrar, Straus & Giroux; 176 pages; \$20*

Buy it at

[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)



THE World Database of Happiness, in Rotterdam, collects all the available information about what makes people happy and why. According to the research, married, extroverted optimists are happier than single, pessimistic introverts, and Republicans are happier than Democrats. Nurses enjoy life more than bankers, and it helps to be religious, sexually active and a college graduate with a short commute to work. The wealthy experience more mirth than the poor, but not much. Most people say they are happy, but perhaps that is because they are expected to be.

Having long ignored the subject, psychologists, economists and social scientists are now tackling happiness with zeal, particularly in America. Mostly this involves examining why people are not as happy as they should be, given the unprecedented access to freedom, opportunities and riches. Because happiness is now considered more an entitlement than a pursuit among citizens of prosperous countries, unhappiness has become a sign of failure, of weakness, and a prime source of dread. "Happy, you might say, is the new sad," writes Eric Weiner in "The Geography of Bliss", the latest contribution to the expanding field of positive psychology.

A reporter for National Public Radio and a self-proclaimed unhappy person, Mr Weiner used the Rotterdam database to find out where the happiest people live. He then travelled to these places in search of the secrets of contentment. "Are you happy?" he asks the locals of Iceland, Thailand, India and the Netherlands. "Have you seen our public toilets?" replies a man in Switzerland, one of the happiest countries. "They are very clean." (Also the landscape is gorgeous, the trains prompt, the government attentive and the unemployment rate low.) In Qatar, a land of cartoonish opulence where happiness is seen as God's will, Mr Weiner's question is met with cringes; one of those asked suggests he "should become a Muslim" in order to know happiness. In mellow Thailand everyone is "too busy being happy to think about happiness."

Mr Weiner offers colourful observations, even when he samples *hakarl*, or rotten shark, an Icelandic speciality. Yet he chronicles his travels with a wearying feather-light jocularly, prizing one-liners over lucid analysis. And he fails to provide footnotes to his sources, despite relying simply on his "journalist's instincts".

Still, there is insight amid the anecdotes. Mr Weiner learns that the world's happiest places (such as Iceland and Switzerland) are often ethnically homogeneous even if they have high suicide rates. The least happy places (such as Moldova) are often former Soviet republics, where new political freedoms are undercut by general mistrust, nepotism, corruption and envy. For the British, happiness is a suspicious transatlantic import ("We don't do happiness," quips one chap). While Americans, who "work longer hours and commute greater distances than virtually any other people in the world", struggle hardest to be happy, and are often blind to their own failure; perhaps because the pursuit of happiness is an "inalienable right" in America.

In any event, it is this "American obsession with happiness" that Eric Wilson lambasts in his slim polemic, "Against Happiness". An English professor at Wake Forest University in North Carolina, Mr Wilson has crafted a tirade against the country's "wanton" embrace of "manic bliss". He sounds a shrill alarm: "We are right at this moment annihilating melancholia," he declares, which will deprive us of the creativity, genius and intellectual brilliance that come from this gloom. To experience beauty and lightness, we must also have death and darkness. But with anti-depressants, high-tech gadgets and botox, America is desperately trying to create "a brave new world of persistent good fortune, joy without pain, felicity with no penalty."

Given America's shift into positive-psychology overdrive, a thoughtful critique of this solipsistic grasping is welcome. Alas, Mr Wilson's is not that critique. Instead, it is an angry, emotional and often repetitive attack on a host of targets, including consumer culture ("happiness through acquisition"), the church ("happiness companies"), politics ("we blithely cheer its increasing demise") and, most of all, those bland, robotic happy types, with their "paper-thin minds". But who are these heartland Americans who are unable to feel pain and sadness? How did he find them? The author's self-serving indictment seethes with malevolence.

Mr Wilson seems to be overlooking the fact that America's growing self-help industrial complex does not indicate "flaccid contentment" but its absence. As Mr Weiner writes, since 1960 America's "divorce rate has doubled, the teen-suicide rate tripled, the violent-crime rate quadrupled, and the prison population quintupled." Also depression, anxiety and other mental-health problems are on the rise, ensuring there will be plenty of melancholic types to write poetry and compose music for some time. There is certainly little risk of eradicating the blues. As Eric Hoffer, an American social philosopher, once observed: "The search for happiness is one of the chief sources of unhappiness."

The Geography of Bliss: One Grump's Search for the Happiest Places in the World.

By Eric Weiner.

*Twelve Books; 352 pages; \$25.99*

Against Happiness: In Praise of Melancholy.

By Eric G. Wilson.

*Farrar, Straus & Giroux; 176 pages; \$20*

## America and the world

## Big think that gets you a headline

Jan 17th 2008

From The Economist print edition

AS A successful American journalist, diplomat and now president of the Brookings Institution in Washington, Strobe Talbott has been all over the place. Some people may think this book is all over the place too.

Its first half is a brisk history of civilisation: a mad gallop through the birth of Judaism, the coming of Christianity and Islam, the ups and downs of Greece and Rome, the imperial dynasties of China, the triumphs and depredations of Genghis Khan, the founding of America, the French revolution, Napoleon, the Ottomans and so forth. This part of the book also provides a speed-dating history of political ideas: for a fleeting couple of pages each, the reader meets thinkers from Dante to Darwin and Machiavelli to Marx, with no previous acquaintanceship assumed.

Mercifully, the gallop slows to a canter as modern times approach. Mr Talbott proceeds at a statelier pace through the two world wars, the cold war and the establishment of the League of Nations and then the United Nations. Eventually (at the point at which the author strides onto history's stage as Bill Clinton's deputy secretary of state), the canter becomes a walk. The story from the Clinton administration to the present fills almost half the pages.



Now, look here

A book that ranges so wide can be hard to digest, but there is method in Mr Talbott's meandering. He is fascinated by what he believes to be a continuous tension between the world's need and appetite for collective governance on the one hand and, on the other, the desire of tribes and nations to think of themselves as independent and sovereign. His dash through history ancient and modern is an attempt to show that the "great experiment" in global governance of his title has its origins in religion, philosophy and the strivings of leaders over thousands of years. Empires, he argues, have not all been about rape and pillage. Alexander and Napoleon had bigger ideas about the fellowship of man—or at least of those men who bowed to the imperial will.

Mr Talbott has also had the good luck to be able to track the same tension in the present day, as America after the cold war has oscillated between a multilateral and unilateral foreign policy under Presidents Clinton and Bush. This part of his story is the better read. He is frankly partisan, a multilateralist who sees the unilateralism of Mr Bush's presidency as a sorry interruption in history's inexorable progress towards a more consensual world in which going it alone can no longer answer pressing problems such as nuclear proliferation and climate change.

Fortunately, you do not have to buy the author's wider musings or share his admiration of Mr Clinton, Al Gore and Kofi Annan to enjoy this ambitious journey through history and politics. And it is not, in the end, so peculiar to dart back and forth between great ideas, the broad sweep of history and the day-to-day practicalities of politics. Wittingly or unwittingly, that is what political leaders do all the time.

In one amusing passage, for example, Mr Talbott describes a chat between President Clinton, Mr Gore and some of their speechwriters. Mr Gore is waxing eloquent about the differences between Alexander Hamilton and Thomas Jefferson on whether the principles of democracy were limited to America.

The Great Experiment: The Story of Ancient Empires, Modern States, and the Quest for a Global Nation

By Strobe Talbott



Simon & Schuster; 478 pages; \$30

Buy it at  
[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

Jefferson, says Mr Gore, was right: "Rousseau said the body politic is a moral being possessed of a will. He was thinking on the national level. We need to take it to the international one." There are a lot of contradictions in all this great stuff, grumble the speechwriters as the group breaks up. "You guys can do it," says the president with a grin: "We need some big think that gets us a headline."

The Great Experiment: The Story of Ancient Empires, Modern States, and the Quest for a Global Nation.  
By Strobe Talbott.

*Simon & Schuster; 478 pages; \$30*

## British post-war history

## At the centre

Jan 17th 2008

From The Economist print edition

EVEN in the childhood photographs, her glance is cool and appraising, the mouth firmly shut. Clarissa Eden, wife of Sir Anthony Eden, Britain's prime minister during the Suez crisis of 1956, was born a Churchill, in 1920. Her father was the brother of Winston Churchill, and her mother the daughter of the seventh Earl of Abingdon. Lady Eden's world was mapped out in country houses and aristocratic clans—Cecils, Stanleys and Angleseys. Her writing is understated, carrying the light, ironic inflections of her class and period. One doesn't unburden.

This book, like Lady Eden's life, falls into two parts: before and after her marriage. It was an extraordinary transition. Until then she had been a free spirit. Not quite as free as the girls of the preceding age, whom she envied, she says, with their cloche hats and Futurism, in comparison with her own "wan and bewildered" generation. But still, 1930s Paris, where she had been sent to be "finished", had opened her eyes to unconventional possibilities. When she returned for the London season, it was as a reluctant, though glamorous, debutante.

She decided to read philosophy—unofficially, owing to her lack of previous qualifications—at Oxford University. The dazzled dons were quick to oblige. But her real stimulation came from friends, the writers, artists and intellectuals she met, both then and later when she worked at *Vogue*, writing a cultural column, and after the second world war in the publicity department of Sir Alexander Korda's film company. Friendship was Lady Eden's gift, and her memoirs are full of vivid sketches of the men (usually men) she knew: Isaiah Berlin (a "torrent of words"), Lucian Freud ("exotic and sharp"), Cyril Connolly (a "civilised, indolent epicurean"), "steely" Cecil Beaton and many others. Evelyn Waugh fell in love with her, though she is characteristically discreet about that, just as she is about her other suitors.

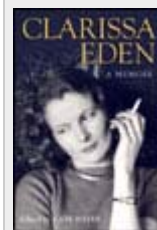
Then, suddenly, in 1952 she announced her engagement to the then foreign secretary, Anthony Eden, 23 years her senior. Her friends were horrified. Politics was a different world. True, she had often stayed with Uncle Winston and listened to political talk. But this was the thing itself. She was utterly unprepared for the sheer battering of it: the cameras and jostling journalists, the receptions and functions, the hats and tiaras, the political wives.

Nevertheless, her memoirs gain something from the experience. The stage is larger, the stakes higher. Lady Eden starts keeping a diary, which helps give dirt and detail. She delights in the bizarre—the gold-leaf-covered carrots at a Pakistani banquet, for example. And she can deliver a good putdown: at one function Nehru's speech "was excellent, about compassion and tolerance"; the New Zealand prime minister's was about "beef and cows". She sits next to the great and quietly skewers them: R.A. Butler, Eden's po-faced chancellor of the exchequer, self-important and "curiously unnatural", his wife "a school prefect, bullying the new girl"; Harold Macmillan, gracious and untrustworthy; John Foster Dulles, the American secretary of state, "slow, vain and jealous".

Eden confided in her. And it is salutary, on reading of the American-British summit on the Indochina crisis of 1954, to watch him in effect vetoing Dulles's military intentions in Vietnam. As for Suez itself (when Gamal Abdel Nasser nationalised the Suez canal, and a secretly planned British, French and Israeli invasion of Egypt collapsed for lack of American support), Lady Eden remains loyal. The reader may disagree, but her portrait of American hypocrisy hits home when she reports a senior American diplomat asking her later: "Why didn't you go on?"

Lady Eden's friends need not have worried. One of her attractions has always been her aesthetic sensibility. Eden shared it. Shakespeare and French art, the reader learns, ran in him as deeply as politics. And as for her, the hats and tiaras only lasted five years.

Clarissa Eden, *A Memoir: From Churchill to Eden*  
Edited by Cate Haste



Weidenfeld & Nicolson; 288 pages; £20

Buy it at  
[Amazon.co.uk](http://Amazon.co.uk)



Clarissa Eden, A Memoir: From Churchill to Eden.

Edited by Cate Haste.

*Weidenfeld & Nicolson; 288 pages; £20*

## Crime writing

## Death watch

Jan 17th 2008

From The Economist print edition

## In the new detective fiction at least, there is life after death

HOW to make an assassin sympathetic? This is a common dilemma for thriller writers, whose books demand plenty of action and often include several horrible deaths. Robert Ludlum, author of the Jason Bourne series, created a hero who was an amnesiac programmed to kill by evil American scientists, so making him morally ambiguous. Mark Burnell, who created the Petra Reuter series, gives Reuter multiple personalities, so one hand knows not what the others are doing.

Kevin Wignall takes a different approach, that is at once original and ambitious. His hero, Conrad Hirst, seeks redemption. Hirst is a former soldier traumatised during a stint working as a mercenary in Yugoslavia. After years spent toting a gun for what he believes is a German crime syndicate, he wants out. But things are not that simple, for Hirst has actually been carrying out hits for a different organisation altogether, one with a worldwide reach and all the manpower and technology it needs to track our hero down when he goes underground.

There are echoes of Bourne in Hirst's quest for his own truth, but, in his fourth book, Mr Wignall forgoes the Ludlumesque technology and fancy fireworks in favour of richer characterisation. Hirst's letters to a former girlfriend are mawkish in places, and he proves oddly unprofessional when faced with a pretty woman. But even hit-men have libidos. "Who is Conrad Hirst?" is a dark, clever book and its author a talent to watch.

"Dead Men" is the fifth outing for Spider Shepherd, a former SAS soldier turned undercover cop. Stephen Leather was once a journalist for the *Times* and the *Daily Mirror*. In brisk newsman's style he explores complex contemporary issues while keeping the action fast and bloody. Shepherd is dispatched to Northern Ireland after four former IRA gunmen are knee-capped and murdered there. This is exactly how they once killed a British policeman. But thanks to the peace agreement, the killers are now Britain's political allies and must be protected. Meanwhile, a Saudi official has sent an assassin to kill Shepherd and his female boss after his sons have died under torture in the basement of the American embassy in London, the plot of Mr Leather's previous Shepherd thriller, "Hot Blood". In "Dead Men", Mr Leather manages to avoid preaching while he poses tough questions about the morality of the fight against terrorism and whether the means justifies the end.

Like Shepherd, Chief Inspector Chen of the Shanghai police is also a cop. But the two men could not be more different. Chen is a poet and gourmet, hoping for some time out, after an investigation into party corruption has ruffled too many big-wigs. But in "Red Mandarin Dress" his plans to study his beloved Chinese literature soon collapse when a pretty young woman is found murdered at a busy Shanghai crossroads. Another victim soon follows and, in the new consumer-crazy Shanghai, the press is alerted before the police, triggering a media frenzy about the city's first serial killer.

Qiu Xiaolong, who has lived in America since 1989, vividly details the human cost of a city devouring itself. Corrupt and brutal property developers, who revel in nicknames such as "Number One Big Buck", are in cahoots with equally debased and unpleasant party officials to force residents out of their homes to make way for shiny new buildings. Beloved old cafés have now become branches of

## Who is Conrad Hirst?

By Kevin Wignall



Simon & Schuster; 240 pages; \$14

Buy it at

[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

## Dead Men

By Stephen Leather



Hodder & Stoughton; 320 pages; £11.99

Buy it at

[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

## Red Mandarin Dress

By Qiu Xiaolong



St Martin's Minotaur; 320 pages; \$24.95.  
 Sceptre; £17.99

Buy it at

[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

Starbucks. Yet even in these dangerous surroundings, culture and beauty endure and an honest man can still chart a path for good, no matter how perilous.

Like Shanghai, Istanbul is a cosmopolitan city on the sea. In "Pretty Dead Things" Emine Aksu, the wife of a Turkish publisher, is glamorous, and as crazy about sex as she is about toyboys and cocaine. Aksu goes missing. Soon after a woman's skeleton is found in Istanbul's banking district. Are the skeleton and the absent nymphomaniac connected? Is Aksu even dead? A Turkish Jew, Edmondo Loya, confesses to killing her, but Barbara Nadel's hero, Inspector Cetin Ikmen, remains highly suspicious.

Ikmen, like his Chinese counterpart, is a complex and very human hero. Ms Nadel won the Crime Writers' Association Silver Dagger award in 2005 for "Deadly Web", a previous outing for Inspector Ikmen. Her portrayal of an Istanbul where the old clashes with the new is more workaday than evocative. But Ikmen's journey into the city's dark side, and his discovery of its historic Jewish community, is well plotted. A killer, a policeman who kills and two policemen hunting killers. In thrillers and detective stories, at least, there is still plenty of life in death.

### Pretty Dead Things

By Barbara Nadel



Headline; 320 pages;  
£19.99

Buy it at  
[Amazon.com](http://Amazon.com)  
[Amazon.co.uk](http://Amazon.co.uk)

Who is Conrad Hirst?

By Kevin Wignall.

*Simon & Schuster; 240 pages; \$14*

Dead Men.

By Stephen Leather.

*Hodder & Stoughton; 320 pages; £11.99*

Red Mandarin Dress.

By Qiu Xiaolong.

*St Martin's Minotaur; 320 pages; \$24.95.*

*Sceptre; £17.99*

Pretty Dead Things.

Barbara Nadel.

*Headline; 320 pages; £19.99*

## The American Museum of Finance

### Curating capitalism

Jan 17th 2008 | NEW YORK  
From The Economist print edition

#### An enjoyable but incomplete look at Mammon's ups and downs

THE Wall Street banks may be battening down the hatches against the storms in the market, but one financial institution, at least, is expanding. America's only public museum dedicated to the financial markets, founded in 1988 and until recently housed in poky digs on Broadway, has reopened in surroundings more befitting its subject: a lavish, mural-lined former banking hall in what used to be the Bank of New York's headquarters at 48 Wall Street.

Museum of American Finance



In for a penny, in for a nickel

With large bank losses making almost daily headlines, the time is ripe for an expanded exhibition space that aims to serve as the "guardian of America's collective financial memory". The Museum of American Finance does its fair share of cheerleading—it is, after all, also the de facto visitor centre for the nearby New York Stock Exchange, which has been inaccessible to the public since the September 11th attacks. But it is not shy about hanging out some of capitalism's dirtiest laundry.

Much of the space is devoted to past crises and scandals, including the panic of 1907, numerous stockmarket crashes, the 1980s junk-bond debacle and the dotcom bust. These are brought to life through documents and objects, including ticker tape from the 1929 crash and a certificate for "lottery annuities" issued in 1720 by the South Sea Company to one Isaac Newton.

A pity then that, although the museum also bills itself as an interpreter of current financial issues, having dropped "History" from its name during the refit, the subprime mortgages and credit derivatives that have rocked the markets in recent months barely feature. Looking for something on the crisis of confidence in credit ratings? Nothing, except for a card explaining that a triple-A rating means "exceptionally stable and dependable". Try telling that to banks that have lost their shirts on top-notch mortgage-linked securities. A section about Citigroup is unbalanced, listing a welter of statistics designed to impress while giving no hint of its many self-inflicted wounds. Perhaps the curators will, in time, be persuaded to make space for a fuller exploration of the present crisis by ditching some of the less scintillating exhibits, such as the cabinets full of tradable commodities. Do we need to be reminded what a pork belly looks like?

Still, there is much to enjoy. Touch-screen displays let visitors explore the features of bank notes and electronic tickers. For those interested in America's early financial history, there is a room dedicated to Alexander Hamilton, the first treasury secretary. So rich in information are the displays that even veteran moneymen should find enough to keep them engaged. Who knew that Warren Buffett was the only student awarded an A+ by the great Benjamin Graham? Or that the rarely seen \$2 bill still accounts for 1% of all American notes printed? (Where do they all go?)

In this setting, moreover, finance takes on a surprisingly artistic quality—whether it be the colourful ornateness of 19th-century railway bonds or design classics such as the Quotron trading terminal or much older Brunsviga-Midget System Trinks counting machine. Art and capitalism also coexist in a sofa made entirely of nickels, placed symbolically between the museum's shop and the main exhibits (pictured below, and on sale for \$100,000). Fittingly, the museum is looking for other ways to make money: its display cases are designed to be mobile so that the hall can be rearranged and rented out for evening events at up to \$30,000 a time.

## John Harvey-Jones

Jan 17th 2008

From The Economist print edition

**Sir John Harvey-Jones, manager extraordinaire, died on January 9th, aged 83**

UPPA



IN THE winter of 1946-47, when ice and snow lay thick across Europe, John Harvey-Jones found himself in charge of bands of Germans and Russians dismantling Wilhelmshaven docks. The docks were to be shipped to Russia as war reparations. Naturally, the two squads of workers hated each other. Every advance was followed by slippage and obstruction before, at long last, the job was done. Mr Harvey-Jones, then a young naval lieutenant, was there because he spoke both languages. It sowed the seeds of a career in man-management.

He was born two years before Imperial Chemical Industries (ICI) was formed in 1926, and died within days of the disappearance of ICI as an independent company after its takeover by a Dutch competitor last year. When he became chairman in 1982 the company was making a loss, bleeding heavily from the harsh effects of Margaret Thatcher's economic policies on British manufacturing. Industrial customers for its plastics, paints and pigments were shrinking or going bust. Sir John knew whom to blame, once describing the prime minister as British manufacturing's greatest handicap.

His hair was long and scruffy, his ties ludicrous and his manner jovial bordering on Falstaffian; a board meeting, for him, was a debate, punctuated by gales of his maniacal laughter. Few were better at the brisk summing-up and the clear, no-nonsense decision. He could not have been more unlike the dull, grey-suited types in most British boardrooms. The top job at ICI fell to him after a tussle as his predecessor sought a second term; roaring in, he trimmed the bloated bureaucracy and tried to make the company more go-ahead. By the time he stepped down in 1987, it was back in profit. The business cycle accounted for much of that, but Harvey-Jones magic had made the difference too.

That got him noticed. His biggest impact, however, came when he presented "Troubleshooter", a pioneering BBC TV series that aimed to interest the general public in the nitty-gritty of running a business. Before long he became the best known boss in the country. Cameras in tow, he would breeze into a company, dispensing blunt criticism, bonhomie and brisk advice in equal portions. The series attracted 3m viewers, outshining stodgier business programmes, though with none of the cruelty attending "Dragons' Den". Sir John was sharp in order to be kind.

He did not always get it right. Had Morgan, a specialist maker of old-fashioned, hand-built sports cars, taken his advice to modernise and expand, it would have gone bust in the recession of the early 1990s. Instead, it largely stuck to its niche market and thrives to this day. Sir John combined his TV career with dozens of non-executive roles, including—from 1989 to 1994—chairman of *The Economist*. When he took up that job, he invited the then CEO out to dinner, asked him what his vision was, and mauled him until, by coffee time, some sort of grand plan for the future had emerged. The Harvey-Jones mantra, both in management and in media, was the need to confront change as the only way to survive.

## The hunter, not the hunted

Sir John's climb up the ICI ladder began in the 1950s, as a time-and-motion man at the huge petrochemicals complex at Wilton on Teesside, in north-east England. This site, the very symbol of post-war British industry with its dramatic floodlit skyline by the Tees, was the beating heart of the company, taking in oil and gas, brewing up and piping out the potions that supplied other ICI factories around the country. Later, as deputy chairman for petrochemicals, he tackled sour industrial relations and disjointed management at the plant. If workers at Wilton downed tools (and Sir John was quick to spot the stirrings of industrial unrest that were to lead to the "winter of discontent" in 1978-79), the whole company would grind to a halt within days. His job was to keep the site humming.

He was never an obvious candidate to lead this champion of industrial technology. He was neither an accountant nor a chemist; the only time he donned a white coat was in his early years at Wilton. Before that, he might have been a sailor. He went straight from Dartmouth College in Devon into the Royal Navy during the war, was torpedoed twice, and then went into submarines, typically opting to become the hunter rather than the hunted. After the war, with his German and Russian, he spent some time in the intelligence service "driving small boats in the Baltic", as he put it. But management soon became his first love.

By the time he reached its boardroom, ICI was rapidly becoming less imperial, less chemical and less industrial. The days of sprawling chemical companies were over; investors wanted more focused, individual businesses. The firm started to unravel less than ten years after Sir John's departure, when a threatened bid from two corporate raiders exposed its weaknesses. An expensive foray into speciality chemicals loaded it with too much debt. Even Wilton had to be sold off to Americans. ICI dropped out of the FTSE 100 list of leading British companies, and may survive only as a brand. The bellwether of British industry, and the man who symbolised it, went out together.



## Overview

Jan 17th 2008

From The Economist print edition

Consumer prices in **America** rose by 0.3% in December, to be 4.1% higher than they had been a year earlier. The core measure of prices, which excludes food and energy costs, rose by 0.2% in the month and by 2.4% from December 2006.

There are worrying signs that the **American consumer** is in retreat. Retail sales fell by 0.4% in December, a weaker out-turn than analysts expected. America's trade deficit in goods and services widened from \$57.8 billion in October to \$63.1 billion in November.

**Britain's** jobmarket proved resilient to the early impact of the global credit crunch. Employment rose by 0.6% in the three months to November. The unemployment rate edged down to 5.3%. Consumer prices rose by 2.1% in the year to December, a rate slightly above the Bank of England's 2% target. Britons' average earnings were 4% higher in the three months to November than in the same period a year earlier.

Industrial production in the **euro area** fell by 0.5% in November, suggesting that the preliminary estimate for fourth-quarter GDP, released next month, may be weak.

**Germany's** economy grew by 2.6% in 2007, adjusting for changes in working days, according to the first official estimate. This implies that German GDP increased by around 0.3% in the fourth quarter.

**Sweden's** consumer prices rose by 3.5% in the year to December.

## **Output, prices and jobs**

Jan 17th 2008

From The Economist print edition

# Output, prices and jobs

% change on year ago

	Gross domestic product				Industrial production latest	Consumer prices			Unemployment rate†, %
	latest	qtr* qtr*	2008†	2009†		latest	year ago	2008†	
United States	+2.8 Q3	+4.9	+1.8	+2.6	+1.5 Dec	+4.1 Dec	+2.5	+2.8	5.0 Dec
Japan	+1.9 Q3	+1.5	+1.4	+1.9	+2.9 Nov	+0.6 Nov	+0.3	+0.3	3.8 Nov
China	+11.5 Q3	na	+10.1	+9.6	+17.3 Nov	+6.9 Nov	+1.9	+3.5	9.5 2007
Britain	+3.3 Q3	+2.7	+1.9	+2.2	+0.4 Nov	+2.1 Dec <sup>§</sup>	+3.0	+2.1	5.3 Nov <sup>††</sup>
Canada	+2.9 Q3	+2.9	+1.9	+2.5	+0.8 Oct	+2.5 Nov	+1.4	+1.9	5.9 Dec
Euro area	+2.7 Q3	+2.8	+1.8	+2.0	+2.7 Nov	+3.1 Dec	+1.9	+2.3	7.2 Nov
Austria	+3.3 Q3	+3.0	+2.6	+2.6	-0.8 Oct	+3.6 Dec	+1.5	+2.1	4.3 Nov
Belgium	+2.6 Q3	+2.2	+2.0	+2.0	+0.6 Oct	+3.1 Dec	+1.6	+2.0	10.7 Nov <sup>††</sup>
France	+2.2 Q3	+3.2	+1.8	+2.0	+2.5 Nov	+2.6 Dec	+1.5	+2.0	7.9 Q3 <sup>§§</sup>
Germany	+2.5 Q3	+2.8	+1.9	+2.1	+3.5 Nov	+2.8 Dec	+1.4	+2.1	8.4 Dec
Greece	+3.8 Q3	+3.6	+2.9	+2.5	+3.6 Nov	+3.9 Dec	+2.9	+3.0	7.9 Oct
Italy	+1.9 Q3	+1.7	+1.3	+1.5	-2.4 Nov	+2.6 Dec	+1.9	+2.3	5.9 Q3
Netherlands	+4.2 Q3	+7.5	+2.1	+2.2	+1.8 Nov	+1.9 Dec	+1.3	+2.0	4.1 Dec <sup>††</sup>
Spain	+3.8 Q3	+2.9	+2.4	+2.3	-0.6 Nov	+4.2 Dec	+2.7	+3.1	8.2 Nov
Czech Republic	+6.0 Q3	+5.8	+4.8	+5.3	+6.7 Nov	+5.4 Dec	+1.7	+5.4	6.0 Dec
Denmark	+1.7 Q3	+6.7	+1.6	+1.7	-1.9 Nov	+2.3 Dec	+1.8	+2.0	2.8 Nov
Hungary	+1.0 Q3	+1.2	+3.0	+3.7	+5.5 Nov	+7.4 Dec	+6.5	+4.5	7.5 Nov <sup>††</sup>
Norway	+3.1 Q3	+5.6	+2.9	+2.6	+2.0 Nov	+2.8 Dec	+2.2	+2.2	2.5 Oct
Poland	+6.4 Q3	na	+5.2	+4.4	+8.3 Nov	+4.0 Dec	+1.4	+3.3	11.2 Nov <sup>††</sup>
Russia	+7.6 Q3	na	+6.7	+5.7	+4.7 Nov	+11.9 Dec	+9.0	+11.5	5.8 Oct <sup>††</sup>
Sweden	+2.5 Q3	+2.4	+2.7	+2.6	+4.2 Nov	+3.5 Dec	+1.6	+2.6	5.2 Nov <sup>††</sup>
Switzerland	+2.9 Q3	+1.3	+2.0	+2.0	+10.7 Q3	+2.0 Dec	+0.6	+1.4	2.6 Dec
Turkey	+1.5 Q3	na	+3.8	+5.2	+7.7 Nov	+8.4 Dec	+9.7	+8.1	9.2 Q3 <sup>††</sup>
Australia	+4.3 Q3	+4.1	+3.6	+3.4	+4.6 Q2	+1.9 Q3	+3.9	+3.2	4.3 Dec
Hong Kong	+6.2 Q3	+7.0	+4.8	+5.7	-2.1 Q3	+3.4 Nov	+2.2	+3.6	3.4 Dec <sup>††</sup>
India	+8.9 Q3	na	+7.7	+7.2	+5.3 Nov	+5.5 Nov	+6.3	+6.1	7.2 2007
Indonesia	+6.5 Q3	na	+6.1	+5.7	+8.3 Oct	+6.6 Dec	+6.6	+6.2	9.8 Feb
Malaysia	+6.7 Q3	na	+5.7	+5.8	+2.7 Nov	+2.3 Nov	+3.0	+2.5	3.1 Q3
Pakistan	+7.0 2007**	na	+5.4	+5.5	+9.8 Oct	+8.8 Dec	+8.9	+7.9	6.2 2006 <sup>††</sup>
Singapore	+6.0 Q4	-3.2	+4.9	+4.7	-1.5 Nov	+4.2 Nov	+0.5	+3.0	1.7 Q3
South Korea	+5.2 Q3	+5.4	+4.7	+4.7	+10.8 Nov	+3.6 Dec	+2.1	+2.5	3.1 Dec
Taiwan	+6.9 Q3	na	+4.6	+3.9	+11.1 Nov	+3.3 Dec	+0.7	+2.0	3.9 Nov
Thailand	+4.9 Q3	+6.3	+4.8	+4.1	+10.8 Oct	+3.2 Dec	+3.5	+3.2	1.2 Sep
Argentina	+8.7 Q3	+11.7	+6.2	+4.7	+8.3 Nov	+8.5 Dec	+9.8	+11.4	8.1 Q3 <sup>††</sup>
Brazil	+5.7 Q3	+6.9	+4.5	+4.1	+6.7 Nov	+4.5 Dec	+3.1	+4.0	8.2 Nov <sup>††</sup>
Chile	+4.1 Q3	-2.5	+4.5	+5.0	+4.2 Nov	+7.8 Dec	+2.6	+5.4	7.3 Nov <sup>†††</sup>
Colombia	+6.6 Q3	+6.9	+5.5	+4.4	+8.3 Oct	+5.7 Dec	+4.5	+4.7	9.4 Nov <sup>††</sup>
Mexico	+3.7 Q3	+5.9	+2.8	+3.5	+0.8 Nov	+3.8 Dec	+4.1	+3.8	3.5 Nov <sup>††</sup>
Venezuela	+8.7 Q3	na	+5.1	+3.9	+2.7 Sep	+22.5 Dec	+17.0	+19.8	8.5 Q3 <sup>††</sup>
Egypt	+6.9 Q3	na	+7.3	+6.6	+7.5 2007**	+6.9 Dec	+12.4	+7.5	8.8 Q3 <sup>††</sup>
Israel	+4.8 Q3	+6.1	+4.3	+4.6	+6.9 Oct	+3.4 Dec	-0.1	+2.4	7.3 Q3
Saudi Arabia	+4.3 2006	na	+6.0	+5.6	na	+6.5 Dec	+2.9	+4.2	na
South Africa	+5.1 Q3	+4.7	+5.1	+5.4	+4.4 Nov	+8.4 Nov	+5.4	+6.6	25.5 Mar <sup>††</sup>
<b>MORE COUNTRIES</b> Data for the countries below are not provided in printed editions of <i>The Economist</i>									
Estonia	+6.4 Q3	+7.4	+4.3	+4.7	+4.4 Nov	+9.6 Dec	+5.1	+8.2	5.4 Oct
Finland	+4.1 Q3	+3.0	+3.2	+2.8	-1.4 Nov	+2.6 Dec	+2.2	+2.2	6.8 Nov
Iceland	+4.3 Q3	+9.9	+2.3	+3.0	+7.6 2006	+5.9 Jan	+6.9	+4.6	0.8 Nov <sup>††</sup>
Ireland	+4.1 Q3	+5.6	+3.5	+3.4	+16.3 Nov	+5.0 Nov	+4.4	+3.0	4.7 Dec
Latvia	+10.9 Q3	na	+7.5	+6.5	+1.1 Nov	+14.1 Dec	+6.8	+9.0	5.0 Oct
Lithuania	+10.8 Q3	+10.0	+7.4	+6.5	na	+8.1 Dec	+4.5	+6.4	4.3 Dec
Luxembourg	+5.3 Q2	+5.3	+4.3	+4.6	-1.3 Oct	+3.4 Dec	+2.3	+2.2	4.4 Nov <sup>††</sup>
New Zealand	+3.4 Q3	+1.1	+2.3	+2.7	+0.5 Q2	+1.8 Q3	+3.5	+2.6	3.5 Q3
Peru	+10.4 Oct	na	+6.5	+6.8	+14.2 Oct	+3.9 Dec	+1.1	+2.7	8.0 Nov <sup>††</sup>
Philippines	+6.6 Q3	+1.1	+5.3	+5.4	-1.7 Oct	+3.9 Dec	+4.3	+3.5	6.3 Q4 <sup>††</sup>
Portugal	+1.8 Q3	-0.1	+2.0	+2.2	-1.6 Nov	+2.7 Dec	+2.5	+2.0	7.9 Q3 <sup>††</sup>
Slovakia	+9.4 Q3	na	+7.0	+5.7	+13.2 Nov	+3.4 Dec	+4.2	+2.5	8.0 Dec <sup>††</sup>
Slovenia	+6.3 Q3	na	+4.8	+4.0	+2.4 Nov	+5.6 Dec	+2.8	+3.4	7.3 Nov <sup>††</sup>

\*% change on previous quarter, annual rate. †The Economist poll or Economist Intelligence Unit estimate/forecast. ‡National definitions. §RPI inflation rate 4.0% in Dec. \*\*Year ending June. ††Latest three months. †††Not seasonally adjusted. §§New series.

Sources: National statistics offices and central banks; Thomson Datastream; Reuters; Centre for Monitoring Indian Economy; OECD; ECB

## *The Economist* commodity-price index

Jan 17th 2008

From The Economist print edition

### *The Economist* commodity-price index

2000=100

	Jan 8th	Jan 15th*	% change on	
			one month	one year
<b>Dollar index</b>				
All items	227.2	231.6	+7.0	+26.0
Food	223.7	230.7	+6.3	+47.7
<b>Industrials</b>				
All	231.6	232.7	+7.8	+6.0
Nfa†	181.6	183.4	+3.3	+20.8
Metals	259.0	259.8	+9.6	+1.3
<b>Sterling index</b>				
All items	174.5	178.2	+9.5	+25.3
<b>Euro index</b>				
All items	142.8	144.2	+3.7	+9.7
<b>Gold</b>				
\$ per oz	874.55	909.75	+13.6	+45.7
<b>West Texas Intermediate</b>				
\$ per barrel	96.50	91.74	+1.8	+78.9

\*Provisional †Non-food agriculturals.

# The Economist commodity-price index

Jan 17th 2008  
From The Economist print edition



Our commodity-price index reached a new high this week, buoyed by soaring food prices. Grains and soyabean prices are at record levels thanks to strong demand for animal feed and biofuel, and to buying by commodity funds. America's Department of Agriculture reckons the country's wheat stocks will fall to a 60-year low this year and that world maize stocks will be the smallest since 1984. Palm-oil prices are at their highest ever and the price of Robusta coffee beans is a near 12-year high. By contrast, the price of industrial commodities has fallen by 12% since May last year, crimped by concerns about the global economy. American timber prices are at a five-year low.

## **Trade, exchange rates, budget balances and interest rates**

Jan 17th 2008

From The Economist print edition



# Trade, exchange rates, budget balances and interest rates

	Trade balance*	Current-account balance		Currency units, per \$		Budget balance	Interest rates, %	
	latest 12 months, \$bn	latest 12 months, \$bn	% of GDP 2008†	Jan 16th	year ago	% of GDP 2008†	3-month latest	10-year gov't bonds, latest
United States	-813.0 Nov	-752.4 Q3	-4.8	-	-	-1.7	3.74	3.71
Japan	+107.0 Nov	+212.9 Nov	+4.8	107	121	-2.5	0.74	1.39
China	+261.5 Dec	+249.9 2006	+10.9	7.23	7.77	0.1	4.48	4.62
Britain	-168.2 Nov	-129.4 Q3	-3.4	0.51	0.51	-3.0	5.58	4.37
Canada	+48.7 Nov	+16.3 Q3	+0.4	1.02	1.17	0.8	3.59	3.81
Euro area	+51.7 Oct	+38.2 Oct	+0.2	0.68	0.77	-0.9	4.51	3.97
Austria	+1.0 Oct	+11.3 Q3	+2.7	0.68	0.77	-0.6	4.51	4.07
Belgium	+19.2 Oct	+13.3 Sep	+2.3	0.68	0.77	-0.4	4.57	4.15
France	-51.7 Nov	-31.6 Nov	-1.3	0.68	0.77	-2.6	4.51	4.07
Germany	+268.1 Nov	+218.0 Nov	+5.6	0.68	0.77	0.8	4.51	3.96
Greece	-53.7 Oct	-43.2 Oct	-12.9	0.68	0.77	-2.5	4.51	4.33
Italy	-12.0 Oct	-42.3 Oct	-2.4	0.68	0.77	-2.7	4.51	4.33
Netherlands	+56.4 Nov	+57.2 Q3	+7.6	0.68	0.77	0.4	4.51	4.06
Spain	-128.7 Oct	-126.1 Aug	-8.9	0.68	0.77	0.1	4.51	4.15
Czech Republic	+4.1 Nov	-5.4 Oct	-3.6	17.8	21.5	-2.6	3.97	4.53
Denmark	+4.2 Nov	+4.0 Nov	+1.4	5.07	5.76	2.8	4.77	4.09
Hungary	-0.5 Nov	-6.8 Q3	-6.2	174	196	-4.4	7.50	6.90
Norway	+59.0 Dec	+59.9 Q3	+15.3	5.42	6.44	18.0	5.74	4.60
Poland	-11.7 Oct	-15.8 Nov	-4.2	2.45	3.01	-1.9	5.65	5.85
Russia	+128.2 Nov	+76.6 Q4	+4.0	24.5	26.5	1.0	10.00	6.19
Sweden	+18.7 Nov	+29.4 Q3	+6.4	6.42	7.02	2.3	4.02	4.02
Switzerland	+11.8 Nov	+69.6 Q3	+14.7	1.10	1.25	0.6	2.65	2.83
Turkey	-60.8 Nov	-35.7 Nov	-7.1	1.18	1.43	-2.9	16.67	6.12‡
Australia	-17.6 Nov	-49.9 Q3	-5.4	1.14	1.27	1.4	7.17	5.97
Hong Kong	-22.7 Nov	+26.9 Q3	+8.9	7.80	7.80	2.3	3.12	2.58
India	-67.9 Nov	-10.9 Q3	-2.0	39.3	44.2	-3.3	7.00	7.77
Indonesia	+40.3 Nov	+10.3 Q3	+1.9	9,445	9,108	-1.8	8.00	6.84‡
Malaysia	+29.9 Nov	+28.7 Q3	+11.3	3.27	3.50	-3.0	3.62	3.87‡
Pakistan	-15.2 Dec	-7.3 Q3	-6.4	62.5	60.9	-5.0	9.92	9.77‡
Singapore	+36.1 Dec	+46.3 Q3	+22.4	1.43	1.54	0.1	1.75	2.19
South Korea	+15.3 Dec	+7.2 Nov	+0.6	940	937	0.3	5.86	5.39
Taiwan	+16.7 Dec	+28.4 Q3	+5.9	32.3	32.8	-2.0	2.60	2.63
Thailand	+11.0 Nov	+14.4 Nov	+2.4	33.1	35.8	-2.1	3.55	4.22
Argentina	+10.8 Nov	+6.8 Q3	+1.7	3.14	3.08	1.2	12.94	na
Brazil	+40.0 Dec	+4.7 Nov	+0.1	1.77	2.14	-2.5	11.18	6.16‡
Chile	+24.5 Dec	+6.7 Q3	+4.0	478	543	5.4	6.36	4.19‡
Colombia	-1.8 Sep	-5.2 Q3	-3.8	1,965	2,225	-1.3	9.05	5.89‡
Mexico	-11.2 Nov	-7.5 Q3	-1.8	11.0	10.9	nil	7.41	8.03
Venezuela	+23.4 Q3	+20.2 Q3	+6.9	5.40	3,980§	-2.6	12.88	6.55‡
Egypt	-15.8 Q2	+2.7 Q2	+0.7	5.46	5.70	-6.9	6.78	5.23‡
Israel	-10.3 Dec	+5.9 Q3	+3.1	3.73	4.23	-1.4	4.33	5.47
Saudi Arabia	+146.6 2006	+98.9 2006	+23.9	3.75	3.75	22.4	4.03	na
South Africa	-10.0 Nov	-19.9 Q3	-7.5	6.95	7.17	0.6	11.30	8.31
<b>MORE COUNTRIES</b> Data for the countries below are not provided in printed editions of <i>The Economist</i>								
Estonia	-4.2 Oct	-3.2 Oct	-13.7	10.7	12.1	1.3	7.10	na
Finland	+13.1 Nov	+14.8 Nov	+4.7	0.68	0.77	3.0	4.38	4.06
Iceland	-1.6 Dec	-3.0 Q3	-11.0	65.4	70.2	3.9	13.85	na
Ireland	+37.2 Oct	-11.1 Q3	-3.0	0.68	0.77	0.5	4.51	4.16
Latvia	-7.2 Nov	-6.5 Oct	-19.4	0.48	0.54	1.0	8.27	na
Lithuania	-6.9 Nov	-4.6 Oct	-14.2	2.35	2.67	-0.6	5.83	na
Luxembourg	-5.9 Oct	+4.7 Q3	na	0.68	0.77	0.7	4.51	na
New Zealand	-4.2 Nov	-10.2 Q3	-7.9	0.77	1.45	3.8	7.30	6.29
Peru	+8.3 Nov	+2.2 Q3	+1.4	0.34	3.19	1.5	5.10	na
Philippines	-4.3 Oct	+5.8 Sep	+5.2	40.8	48.8	-0.4	6.25	na
Portugal	-24.7 Oct	-18.6 Oct	-8.2	0.68	0.77	-2.6	4.51	4.23
Slovakia	-0.9 Nov	-3.5 Sep	-3.1	22.8	27.0	-2.5	4.15	4.51
Slovenia	-2.8 Nov	-1.8 Oct	-2.5	0.68	0.77	-0.8	na	na

\*Merchandise trade only. †The Economist poll or Economist Intelligence Unit forecast. ‡Dollar-denominated bonds. §Unofficial exchange rate.  
Sources: National statistics offices and central banks; Thomson Datastream; Reuters; JPMorgan; Bank Leumi le-Israel; Centre for Monitoring Indian Economy; Danske Bank; Hong Kong Monetary Authority; Standard Bank Group; UBS; Westpac.



## Markets

Jan 17th 2008

From The Economist print edition

## Markets

	Index Jan 16th	% change on		
		one week	in local currency	in \$ terms
United States (DJIA)	12,466.2	-2.1	nil	nil
United States (S&P 500)	1,373.2	-2.5	-3.2	-3.2
United States (NAScomp)	2,394.6	-3.2	-0.9	-0.9
Japan (Nikkei 225)	13,504.5	-7.5	-21.6	-12.6
Japan (Topix)	1,302.4	-8.6	-22.5	-13.6
China (SSEA)	5,552.5	-2.7	+97.2	+112.9
China (SSEB, \$ terms)	361.5	-2.4	+157.4	+177.8
Britain (FTSE 100)	5,942.9	-5.3	-4.5	-4.1
Canada (S&P TSX)	13,074.9	-3.7	+1.3	+15.0
Euro area (FTSE Euro 100)	1,275.5	-3.8	-0.2	+11.1
Euro area (DJ STOXX 50)	4,108.3	-3.5	-0.3	+11.0
Austria (ATX)	3,907.8	-8.7	-12.4	-2.5
Belgium (Bel 20)	3,801.4	-6.5	-13.4	-3.5
France (CAC 40)	5,225.4	-3.9	-5.7	+5.0
Germany (DAX)*	7,471.6	-4.0	+13.3	+26.1
Greece (Athex Comp)	4,523.8	-10.8	+3.0	+14.6
Italy (S&P/MIB)	36,632.0	-1.8	-11.6	-1.6
Netherlands (AEX)	462.6	-5.9	-6.6	+4.0
Spain (Madrid SE)	1,487.5	-5.6	-4.3	+6.5
Czech Republic (PX)	1,570.1	-7.0	-1.2	+15.7
Denmark (OMXC20)	389.7	-7.8	-8.1	+2.4
Hungary (BUX)	23,764.1	-7.5	-4.3	+4.8
Norway (OSEAX)	482.0	-10.9	-4.1	+10.2
Poland (WIG)	46,205.0	-11.9	-8.3	+8.5
Russia (RTS, \$ terms)	2,225.5	-3.1	+7.6	+15.8
Sweden (Aff.Gen)	302.4	-4.2	-17.2	-11.8
Switzerland (SMI)	7,847.5	-5.9	-10.7	-0.6
Turkey (ISE)	49,093.8	-6.9	+25.5	+50.8
Australia (All Ord.)	5,870.8	-4.7	+4.0	+15.9
Hong Kong (Hang Seng)	24,450.9	-11.5	+22.5	+22.1
India (BSE)	19,868.1	-4.8	+44.1	+62.3
Indonesia (JSX)	2,592.3	-8.4	+43.6	+36.7
Malaysia (KLSE)	1,453.7	-2.5	+32.6	+43.1
Pakistan (KSE)	13,846.7	-2.9	+37.9	+34.2
Singapore (STI)	3,058.5	-8.6	+2.4	+9.8
South Korea (KOSPI)	1,705.0	-7.6	+18.9	+17.6
Taiwan (TWI)	8,179.5	+1.2	+4.5	+5.6
Thailand (SET)	773.8	-5.7	+13.8	+24.2
Argentina (MERV)	2,065.8	-1.1	-1.2	-3.6
Brazil (BVSP)	58,777.0	-6.2	+32.2	+59.0
Chile (IGPA)	12,661.1	-2.0	+2.3	+14.0
Colombia (IGBC)	9,586.5	-7.5	-14.1	-2.1
Mexico (IPC)	27,343.6	-3.7	+3.4	+2.2
Venezuela (IBC)	36,861.3	-3.3	-29.4	-56.3
Egypt (Hermes)	96,122.1	-0.8	+56.8	+64.0
Israel (TA-100)	1,072.3	-3.7	+16.3	+31.4
Saudi Arabia (Tadawul)	11,544.0	-0.9	+45.5	+45.5
South Africa (JSE AS)	26,911.5	-5.2	+8.0	+9.6
Europe (FTSEurofirst 300)	1,383.2	-4.5	-6.8	+3.8
World, dev'd (MSCI)	1,469.6	-3.9	-0.9	-0.9
Emerging markets (MSCI)	1,147.5	-6.5	+25.7	+25.7
World, all (MSCI)	372.8	-4.2	+1.4	+1.4
World bonds (Citigroup)	751.0	+1.3	+14.1	+14.1
EMBI+ (JPMorgan)	437.1	+0.4	+7.3	+7.3
Hedge funds (HFRX)	1,309.3	-0.7	+2.6	+2.6
Volatility, US (VIX)	24.4	24.1	11.6 (levels)	
CDSs, Eur (iTRAXX)†	61.9	nil	+165.4	+195.5
CDSs, N Am (CDX)†	110.7	+5.1	+231.0	+231.0
Carbon trading (EU ETS) €†	22.8	-2.9	+24.9	+39.1

\*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. ‡New series.



# Latin American growth forecasts

Jan 17th 2008  
From The Economist print edition



The economies of Latin America are set to cool a little this year, according to the World Bank's annual *Global Economic Prospects* report. The slightly weaker outlook largely reflects faltering spending in the United States and lower remittances (many Latin American migrants work in America's shrinking home-building industry). Last year's strong performers include Argentina, boosted by easy policy, and oil-fuelled Venezuela. These economies are forecast to slow more than most this year. Brazil, the region's largest economy, is set to grow by 4.5%, only slightly down on last year's 4.8%. Mexico's growth is expected to perk up in 2008, despite the general slowdown forecast for the region.