FINANCIAL TIMES

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Martin Wolf
Brexit is a perilous one-way bet for Britain — COMMENT, PAGE 11

China uncorked
How Chile is challenging France in the Chinese wine market — BIG READ, PAGE 9

Pay grades
Students need more data on college performance — SARAH O'CONNOR, PAGE 12

Saudi Arabia borrows $10bn as oil slump drains reserves

- First debt-raising since 1991
- Move paves way for historic bond

SIMEON KERR — DUBAI
ELAINE MOORE — LONDON

Saudi Arabia is raising $10bn from a consortium of global banks as the kingdom embarks on its first international borrowing in 25 years to counter dwindling oil revenues and reserves.

The landmark five-year loan, a sign of Riyadh's newfound dependence on foreign capital, opens the way for the country to launch its first international bond issue. It comes as the low price of crude encourages other Gulf governments, such as Abu Dhabi, Qatar and Oman, to tap bond markets.

The oil-rich kingdom, which last weekend blocked a deal among oil producers to freeze output and bolster prices, has burnt through about $120bn in reserves since late 2014. Its fiscal deficit is set to widen to 19 per cent of gross domestic product this year.

Strong interest in the loan, especially from Asia, came despite rating agencies' downgrades on Saudi creditworthiness since the oil price collapsed. The government raised the amount it wanted to borrow from $6bn-$8bn to $10bn after the deal was oversubscribed.

"The deal is very successful, with very competitive pricing," said Elyas Algaseer, deputy regional general manager at Bank of Tokyo-Mitsubishi. "There was immense market appetite."

Ewen Cameron Watt, chief investment strategist at BlackRock, the world's largest asset manager, said: "The loan is a way for Saudi Arabia to test the waters and set up an international borrowing profile.

"This is paving the way for the kingdom to transform from a creditor nation into a debtor nation. It's a significant moment of change in debt markets."

Saudi Arabia may now raise its first global bond in the wake of the loan deal, bankers said. Institutions that loaned the most would be set to benefit from a mandate to help Riyadh raise the bond.

The lead lenders, each pledging about $1.3bn, include Bank of Tokyo-Mitsubishi, HSBC and JPMorgan, bankers said. Banks were required to lend at least $500m to participate.

Mr Algaseer declined to comment on the pricing but other bankers close to the deal said it had priced at around 120 basis points over US dollar Libor.

The loan is Saudi Arabia's first international borrowing since 1991, when it raised about $1bn in the aftermath of the Iraqi invasion of Kuwait.

Bankers are now confident that Saudi state-related companies will also seek to raise funds, using the sovereign loan, and later bond, as a benchmark.

Prince Mohammed bin Salman, who oversees economic reform, is set to publish his "vision for Saudi Arabia", a template for shifting to a post-oil era, in Riyadh on April 25.

It is expected to give details about the privatisation of state oil company Saudi Aramco, the creation of a sovereign wealth fund and other reforms to boost jobs and investment. JPMorgan has been working with the state oil company since late last year on a plan for an initial public offering, people aware of the matter said.

No more tears Millennial mums going ga-ga for organics spark J&J rethink

A Johnson & Johnson US magazine advertisement from the 1950s — Image courtesy of the Advertising Archive

DAVID CROW — NEW YORK
LINDSAY WHIPP — CHICAGO

Johnson & Johnson is relaunching its baby care business because millennial mothers are ditching its talcum powders and shampoos in favour of more expensive organic alternatives.

Tumbling sales of its baby care products have forced the change, making J&J the latest power brand to fall prey to the changing tastes of younger consumers. US sales of J&J's baby care products, including its "no more tears" shampoo, fell 14 per cent year-on-year in the first quarter to $95m, their lowest level in a decade.

"It looks like millennial moms are buying new organic products," said Dominic Caruso, chief financial officer.

Brands from McDonald's, Heinz and Campbell's Soup to Avon and Gap have been forced to rethink their strategies as they struggle to cope with the shifting tastes of millennials.

Mr Caruso said J&J had "robust plans to relaunch baby" this year.

The company's infant brands have been a mainstay since the launch of Johnson's baby powder in 1893. But more recently the company has struggled to combat the perception that some of its products contain dangerous chemicals.

Briefing

▸ EDF board warned over Hinkley Point
Managers at the French utility have written to its board warning that the directors could be held responsible if the company pushes on with its £18bn nuclear project.— PAGE 15; ANALYSIS, PAGE 17

▸ Hammond rules out Libya combat role
The foreign secretary has told MPs that there are no plans for troops to be involved in fighting Isis in Libya, though the UK was willing to send thousands to help train "unity" government forces.— PAGE 4

▸ Extremist allegations threaten Khan bid

Former human rights lawyer and Labour candidate for London mayor Sadiq Khan leads the polls but questions, pushed by Tory rival Zac Goldsmith, on links to extremists may be hurting his campaign.— PAGE 4

▸ Labour shortage to drive US wages
A leading business group has predicted that the US faces significant labour shortages in a wide range of sectors as unemployment falls towards 4 per cent and the working-age population stagnates.— PAGE 5

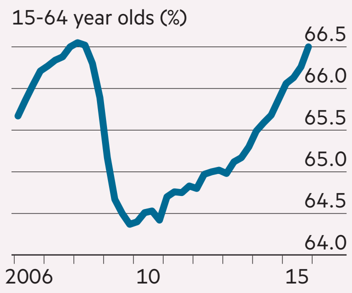
▸ Goldman profit plunge caps grim season
The US bank's profits have more than halved after across-the-board falls in revenues, bringing down the curtain on a sobering earnings season for the big US banks.— PAGE 15; LEX, PAGE 14; ANALYSIS, PAGE 16

▸ Saudis host Obama and look to successor
The US president arrives in Riyadh today, where he will be greeted by hosts looking past the US election in the hope his successor will restore ties that have frayed during his time in office.— PAGE 7

▸ Tesco Bank targets mortgage market
The Edinburgh-based lender has unveiled a push to take on the high-street banks by offering property loans through independent brokers, a sign that mortgage market competition is rising.— PAGE 20

Datawatch

Employment rates in the OECD
15-64 year olds (%)



Source: OECD

The last quarter of 2015 saw the proportion of people in jobs in the OECD area return to the peak level hit in the first quarter of 2008. However, employment rates are not back to pre-crisis levels in many countries, including the US

Mistrust of Spain keeps EU support solid in Gibraltar

Gibraltar, ceded to Britain in the 1713 Treaty of Utrecht but seen by Spain as a colonial relic that sooner or later will be returned, wants the UK to stay in the EU. A poll puts support at 88 per cent amid fears that should Britain leave, 'Spain might be tempted to be mischievous at best and downright vindictive at worst', especially with regard to its border crossing, used by 30,000 workers and visitors every day.
Analysis ▸ PAGE 2
Martin Wolf ▸ PAGE 11

Gove holds up Albanian model for post-Brexit future outside EU market

GEORGE PARKER — LONDON
ALEX BARKER — BRUSSELS

Britain will move outside the EU's single market and instead join "Bosnia, Serbia, Albania and Ukraine" in a European free trade zone if voters choose Brexit in June's referendum, according to a vision outlined by Michael Gove.

The pro-Brexit justice secretary for the first time confirmed yesterday that the Leave camp did not want Britain to remain part of the EU's tariff-free bloc in which British-based banks can trade under a "passport" scheme. He insisted the UK's financial services sector would "thrive" in this new environment.

He said Britain would forge its own deal with the EU but said that a continent-wide free trade area embracing a wide range of bilateral deals would "be the core of our new arrangement".

Critics seized on Mr Gove's "Albanian model", pointing out that the Balkan country has limited access to the single market, no financial services "passports" and its exports to the EU are subject to customs checks.

Brexit campaigners were challenged by George Osborne on Monday to set out exactly what "Out" would look like. Mr Gove set out to respond, saying: "There is a free-trade zone stretching from Iceland to Turkey that all European nations have access to . . .

"After we vote to leave we will remain in the zone. The suggestion that Bosnia, Serbia, Albania and Ukraine would remain part of this free-trade area — and Britain would be on the outside with just Belarus — is as credible as Jean-Claude Juncker joining Ukip."

Mr Gove's aides said Britain would not seek to remain part of the single market, saying the UK should not accept the principal conditions for entry. It would not pay into the EU budget, accept free movement of workers or the jurisdiction of the European Court of Justice.

The "free-trade area" described by Mr Gove takes several forms. Iceland, Liechtenstein, Norway and Switzerland are part of the European Free Trade Association, whose members have varying levels of single market access. Norway pays into the EU budget and accepts free movement. Switzerland does not have full access to the single market but does accept free movement.

Albania has an agreement covering trade in goods and potentially financial services. But it would only have full single-market access if it applies the existing and future EU rule book.

Britain in Europe pages 2 & 3
Martin Wolf page 11

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16
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World Markets

STOCK MARKETS

	Apr 15	prev	%chg
S&P 500	2080.73	2082.78	-0.10
Nasdaq Composite	4927.35	4960.02	-0.66
Dow Jones Ind	18022.17	18004.16	0.10
FTSEurofirst 300	1375.17	1355.26	1.47
Euro Stoxx 50	3110.95	3064.03	1.53
FTSE 100	6405.35	6353.52	0.82
FTSE All-Share	3502.70	3474.23	0.82
CAC 40	4566.48	4506.84	1.32
Xetra Dax	10349.59	10120.31	2.27
Nikkei	16874.44	16275.95	3.68
Hang Seng	21436.21	21161.50	1.30
FTSE All World $	269.47	267.12	0.88

CURRENCIES

	Apr 19	prev		Apr 19	prev
$ per €	1.138	1.133	€ per $	0.879	0.883
$ per £	1.440	1.428	£ per $	0.694	0.701
£ per €	0.790	0.794	€ per £	1.266	1.260
¥ per $	109.315	108.725	¥ per €	124.352	123.169
¥ per £	157.424	155.215	£ index	84.658	84.252
€ index	88.279	88.288	$ index	99.761	100.001
SFr per €	1.092	1.091	SFr per £	1.382	1.375

COMMODITIES

	Apr 19	prev	%chg
Oil WTI $	42.25	41.19	2.57
Oil Brent $	43.76	42.91	1.98
Gold $	1234.30	1227.10	0.59

INTEREST RATES

	price	yield	chg
US Gov 10 yr	98.56	1.79	0.00
UK Gov 10 yr	98.68	1.64	0.03
Ger Gov 10 yr	103.23	0.17	0.01
Jpn Gov 10 yr	102.35	-0.13	0.00
US Gov 30 yr	98.10	2.59	0.00
Ger Gov 2 yr	103.05	-0.51	0.00
	price	**prev**	**chg**
Fed Funds Eff	0.36	0.38	0.02
US 3m Bills	0.22	0.22	0.00
Euro Libor 3m	-0.27	-0.27	0.00
UK 3m	0.59	0.59	0.00

Prices are latest for edition. Data provided by Morningstar

A Nikkei Company

Legislation

Cameron compromises over new trade union laws

Ministers scrap plan to abolish payroll payments after referendum warning

JIM PICKARD AND SARAH O'CONNOR

Ministers have scrapped plans to abolish the automatic payment of union subscriptions through payrolls as part of a series of compromises over the trade union bill.

The concessions in the House of Lords came after unions warned David Cameron that they were unable to throw their full weight behind the campaign to remain in the EU because they were too busy fighting the "draconian" legislation.

The prime minister needs the support of millions of Labour voters if he is to win June's referendum on EU membership. Yet for months he has been embroiled in a parliamentary battle with the organisations that could help deliver that support: trade unions. Despite certain concessions, ministers are pressing ahead with laws that will make it harder to go on strike and will end the automatic "opt-in" system of funding of Labour by union members.

Nicola Smith, head of economic and social affairs for the Trades Union Congress, said last week that the unions' priority was preparing for the proposed new rules.

"There is a range of areas where, if the government was to recognise that as a minimum some parts of the bill need improvement, then they might have a better chance of convincing trade unions to focus more resources on the referendum," she said.

The Unite union also told the government that if it could adopt "a less adversarial approach" it might have a better chance of winning over union members in the EU referendum campaign.

The government had already endured three lost votes on the trade union bill after criticism from Labour, the Liberal Democrats and many crossbench peers.

> 'They might have a better chance of convincing unions to focus more on the referendum'

Yesterday, as the bill reached its report stage in the Lords, the government offered further concessions to prevent fresh defeats.

Ministers have given up attempts to end automatic "check-off": the system will remain, so long as the costs are covered by the union.

The government is pushing ahead with proposals to give greater powers to the certification officer, who monitors the sector: he will be able to access unions and their membership lists, even in the absence of a complaint — with the power to impose fines of up to £20,000.

But ministers gave ground by promising to amend the bill to ensure that the certification officer is free of ministerial interference.

Likewise, the bill will still compel all public sector employers to publish information on the cost of employees' "facility time" — time off for union-related activities. Yet ministers have given ground by promising not to cap facility time until there is at least two years of data from the relevant bodies.

Lord Mendelsohn, Labour's business spokesman in the Lords, described the concessions as a "major turning point" on the union bill.

But he urged the government to deliver more compromises, particularly over proposals that will force union members to actively "opt in" to their political funds.

Len McCluskey, head of Unite, welcomed the concessions, but warned that the bill — even in its current form — would set back industrial relations in Britain by decades.

"We still have a bill that will make it harder for UK workers to defend themselves, that undermines the right to strike and establishes an aggressive regulator," he said.

> 'We still have a bill that will make it harder for UK workers to defend themselves'

The government has been under pressure to water down some of the proposals in order to get its current legislative package through Parliament before the Queen's Speech in May.

Ministers are also mindful of unions' potential influence over the looming referendum: although they are a much diminished force, unions still have a direct link to about 6m members.

They are already involved in the EU campaign: last week Unison became the latest big union to back the Remain camp, joining the GMB and Unite on the same side as Jeremy Corbyn's Labour party and Mr Cameron's Conservative government. The GMB is training officials to talk to shop floor workers about why it benefits jobs and growth for the UK to remain in the EU.

Unite is encouraging members to talk to other members. An official said: "To be able to get an Airbus worker to talk to a Nissan worker about the benefits of staying in the EU will carry much more weight than George Osborne trying to scare people to death."

Overseas territory. Sovereignty

Gibraltar rock solid in its commitment to Brussels

Residents fear Madrid will advance its claim for control if the Leave campaign triumphs

TOBIAS BUCK — GIBRALTAR

Keeping up standards: flags of the EU, Gibraltar and the UK fly over the Rock's Main Street Oli Scarff/Getty Images

Nowhere in Gibraltar feels more British than Main Street, the commercial artery that runs the length of the old town.

Number 162 is home to the Gibraltar Arms Pub, offering a Sunday roast for just £8.95. The local Marks and Spencer department store is at Number 215, providing shoppers with a wide choice of navy blazers and English biscuits. In between the two is a striking reminder that the great political convulsions gripping Britain today are shaking its tiny overseas territory as well: the local headquarters of the Stronger in Europe campaign, which opened last week.

The office's staff of eight volunteers appear to have little to do. By all accounts, Gibraltar is united in its desire for the UK to remain a member of the EU. A poll published on Friday by the Gibraltar Chronicle, the local newspaper, found 88 per cent of the population would back EU membership in the referendum on June 23. Turnout is expected to be above 80 per cent.

"Gibraltar's best interests are served by remaining in the EU. That is undoubted in the view of the government, and there is widespread support for that in Gibraltar," says Fabian Picardo, the chief minister of Gibraltar.

The main reason for the territory's pro-EU stance is visible from the balcony of Mr Picardo's office, which offers a commanding view across the Bay of Gibraltar to Spain. Gibraltar was ceded to the British crown in the 1713 Treaty of Utrecht, but, at least as far as Madrid is concerned, the matter of sovereignty is far from settled. Officially,

Spain regards Gibraltar as a colonial relic that sooner or later has to fall back under Spanish control. The fear among Gibraltarians is that Madrid will be tempted to use Brexit as a lever to advance that claim.

The most immediate worry is the border crossing — Gibraltar's only land link with the outside world, and one that is used by 30,000 workers and visitors every day. "We have one constant issue and that is our border and the relationship with Spain," says Gemma Vasquez, campaign director of Gibraltar Stronger in Europe. "Should Britain leave the EU, Spain would have more of a free rein to do what it wants at the border."

Recent political tensions have often led to a near standstill in cross-border traffic — choking economic and social life both in the territory and adjacent Spanish communities. Since the summer of 2013, the European Commission has intervened repeatedly to unblock the border, just as the prospect of European Community membership helped open it more than three decades ago. From 1969 to 1982, Spain had kept the frontier sealed, a period remembered in Gibraltar with both anger and anguish.

"For us, the EU has proven itself as a guarantor of normality in our relationship with Spain," says Peter Montegriffo, a former Gibraltar trade minister and now a partner at Hassans, a local law firm. "People in Gibraltar fear that, if we leave the EU, Spain might be tempted to be mischievous at best and downright vindictive at worst."

> 'If the UK leaves the EU, and we were forced to leave as well, it would be very tough for Gibraltar economically'

How exactly Spain would respond to Brexit is hard to predict. The country has been without a proper government since the December general election and appears to be heading for a repeat ballot in June. In the meantime, all that London and Gibraltar have to go on are recent remarks by José Manuel García-Margallo, caretaker foreign minister.

He told Spanish television last month that the only way for Gibraltar to retain access to the EU single market if Brexit happened would be to accept "co-sovereignty", or joint control by Spain and the UK. That would mean, he added, "the Spanish flag on the Rock".

What is at stake for Gibraltar is not least the territory's booming economy. Over the past decade it has grown rich from its buoyant financial services and gambling industry. Part of the territory's attraction — and indeed its official pitch to international investors — is that Gibraltar offers a "gateway to Europe", and the ability to trade seamlessly with the rest of the EU.

Political and business leaders in the territory are quick to stress that Gibraltar trades more with the UK than with the rest of the EU. But losing unfettered access to the single European market would hit Gibraltar hard.

"This place is familiar with adversity. We have dealt with sudden change before," says Edward Macquisten, chief executive of the Gibraltar Chamber of Commerce. "But if the UK leaves the EU, and we were forced to leave as well, it would be very tough for Gibraltar economically."

With just over two months to go until the referendum, Mr Picardo makes no secret of his frustration with the debate in the UK.

Gibraltarians are "hearing some of the things being said by the Leave campaign with disbelief", he says. "It is very easy to make a pejorative argument about Brussels bureaucrats and the shape of bananas. But you are not going to make serious policy based on that sort of *Dad's Army* argument."

To Madrid, meanwhile, Mr Picardo offers a customary signal of defiance. Even if Britain and Gibraltar do leave the EU, the issue of Spanish control and influence in the territory will not be on the table. Gibraltar, he insists, will "not pay a sovereignty price for access to the single market".

FT **Video: Treasury analysis**
Lionel Barber and Janan Ganesh discuss the Treasury's estimates on the economic consequences of leaving the EU
www.ft.com/treasuryanalysis

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Business fears

Hundreds of entrepreneurs sign open letter against EU exit

KATE ALLEN
POLITICAL CORRESPONDENT

Some of Britain's best-known entrepreneurs have warned about the impact that a vote for Britain to leave the EU would have on their businesses and the prospects for future start-ups.

More than 200 businesspeople in sectors from technology to fashion have signed an open letter, published in the Financial Times, citing "the benefits of being able to do business within Europe's single market of 500 million consumers", the EU's cross-border regulatory regime and "the ability to recruit the brightest people" across the continent as key reasons to stay in the EU.

They include government technology adviser Baroness Lane-Fox, fashion designer Anya Hindmarch, Arnaud Massenet of fashion retailer Net-A-Porter, Alex Chesterman of property site Zoopla and Jacqueline Gold of underwear retailer Ann Summers.

Britain is the best place in the EU to launch a business and leaving would "undoubtedly undermine the ability of Britain's entrepreneurs to start-up, innovate and grow", they say.

Their warning comes as Anna Soubry, business minister, called on companies to speak out about the referendum. On Monday, George Osborne, the chancellor, set out the official Treasury projections of the damage a British exit from the EU could cause to the UK.

Downing Street regards economic arguments as its primary route to victory in June's referendum; polling has repeatedly shown it is the only aspect of the debate that consistently rivals immigration in its significance for the public.

Voters needed to hear from businesses before they made their minds up about how to vote, Ms Soubry said in a speech at the London Stock Exchange yesterday.

"It's right for us to belong to a group of countries with whom we have so much in common, whether it's the values of human rights, democracy or how we do business," she said.

"That's why it's imperative we hear loud and clear the voices of all businesses."

The Treasury's main scenario claimed that a British exit from the EU would cut trade and leave a £36bn a year gap in the public finances, equivalent to 8p on the basic rate of income tax.

Over 15 years the economy would be 6.2 per cent smaller, costing each household £4,300 a year.

The findings triggered a furious backlash from Leave campaigners, who said they were "highly tendentious".

In their letter, the entrepreneurs argued: "Of course the EU isn't perfect; but rather than cutting ourselves off from the opportunities it offers, it is better to be on the inside helping shape the rules of this market instead of just being subject to them."

Entrepreneur Baroness Lane-Fox is in favour of Europe's single market

Other signatories include Dinesh Dhamija of Ebookers, William Shu of Deliveroo, Simon Woodroffe of Yo! Sushi and Peter Williams of clothing brand Jack Wills.

Lloyd Dorfman, founder of Travelex, who signed the letter said leaving the EU would be "the biggest own-goal in our postwar history".

Another signatory, Doug Monro, founder of Adzuna, said the uncertainty and reduction in investment that would result from an exit would cause a jobs market slowdown.

The letter is the latest in a series of attempts by both sides of the campaign to demonstrate business support for their case.

Bosses of 36 FTSE 100 companies and 162 other businesses put their names to an anti-Brexit letter in February.

The campaign for Britain to leave the EU last month published a list of 250 business figures who support its case.

Letters page 10

Idea floated of Gove as deputy PM after vote

Promotion for Eurosceptic justice secretary a possibility to heal party wounds amid talk of ministerial job for Johnson

GEORGE PARKER — POLITICAL EDITOR

Michael Gove is seen by David Cameron as the key to restoring Conservative party unity after the EU referendum, but it did not sound that way yesterday as the justice secretary hit his Eurosceptic stride.

Mr Gove attacked the In campaign, led by Mr Cameron, for "treating people like children", for trying to persuade voters that "Britain is beaten and broken" and for being "overwhelmingly negative and pessimistic".

For good measure Mr Gove rubbished Mr Cameron's success in excluding Britain from "ever closer union", saying this supposed negotiating triumph offered "no protection" and had negligible legal meaning.

It is perhaps a sign of the Euro-trauma affecting the Conservative party that Mr Cameron is looking to Mr Gove to help bring the party together — if the prime minister succeeds in keeping Britain in the EU on June 23.

"Gove is the key," said one cabinet minister. Another said: "There's a lot of talk about Michael becoming deputy prime minister in a unity reshuffle. That might make a lot of sense."

Winning the referendum may be only the start of Mr Cameron's problems. If he loses, things could be more straightforward: many ministers expect the prime minister would quit immediately. "He wouldn't last 30 seconds," Ken Clarke, former chancellor, has said.

But Eurosceptic Tories say that if Mr Cameron wins the referendum he will have done so in such an unfair and disreputable way that some pro-Brexit MPs will demand his head. The £9m pro-EU leaflet and Chancellor George Osborne's 200-page Treasury analysis are held up as evidence.

Mr Cameron is therefore making plans for an immediate cabinet reshuffle to head off any Tory mutiny after the June 23 vote; if it is only a narrow margin of victory, the mood among Tory MPs will be febrile.

The prime minister's allies say that he will move quickly to bring key Eurosceptics into the fold, the most notable

Gove's view

'The In campaign want us to believe that Britain is beaten and broken . . . [It] imagines the people of this country are mere children, capable of being frightened into obedience by conjuring up new bogeymen every night'

Et tu? Michael Gove walks behind David Cameron during a visit to a school in Birmingham in 2013
Paul Rogers/Getty Images

'There's so much noise about how bad Brexit would be you wonder why we agreed to the referendum'

of whom is Mr Gove, a long-time friend of Mr Cameron and Mr Osborne.

Mr Gove's status as a genuinely committed Eurosceptic, willing to put his love of country ahead of his friendship with Mr Cameron, makes him a uniquely credible figure in this "unity reshuffle".

The idea of making him deputy prime minister would be the clearest demonstration of Mr Cameron's desire to bring the party back together, although what precise responsibilities he might hold in that role are unclear.

Intriguingly Mr Osborne, who was made Mr Cameron's "first secretary of state" and de facto deputy after the 2015 election, appears to be relaxed about the idea.

The chancellor's allies believe that Mr Gove, in spite of his standing in the party, genuinely has no ambitions to be prime minister and is therefore not a serious rival for the Number 10 job.

"I don't have what it takes," Mr Gove told the FT Weekend Magazine in 2014 about any prime ministerial aspirations. "The pressure of the job is phenomenal and it takes a toll on you and your family and I don't think I could do that."

The most recent parallel was John Major's decision to make Michael Heseltine his deputy prime minister in 1995 in the aftermath of another Tory Eurosceptic leadership challenge. Mr Heseltine, by that point, had abandoned his own prime ministerial ambitions.

While Mr Gove would be a key figure in any reconciliation reshuffle, Mr Cameron's allies say that the prime minister would also be obliged to offer a "proper job" to Boris Johnson through gritted teeth. The London mayor and MP for Uxbridge and South Ruislip infuriated Mr Cameron by deciding at the last minute to join the Brexit camp. Even though some on the Tory right do not trust Mr Johnson's motives, he remains too big a figure to sideline.

The question of "what job for Boris" is a common staple of ministerial gossip, much of which focuses around the possibility that Mr Cameron could create a vacancy at the Home Office by moving Theresa May to the Foreign Office.

Another key objective for Mr Cameron, according to supportive ministers, is to bring rising stars from the 2010 intake to the ministerial ranks. "He wants to make it a question of the future versus the past," said one.

The prime minister may not be able to escape or shake off the party's past obsessions with Europe that easily. It would take letters from only 50 Tory MPs to trigger a vote of no-confidence, and some MPs believe one is likely.

The level of acrimony among Tory Eurosceptics over Mr Cameron's running of the pro-EU referendum campaign is rising by the week, with more than two months still to go.

Philip Hollobone, a Eurosceptic Tory MP, said the "disgracefully dodgy document" from the Treasury on the cost of Brexit was worthy of the children's programme *Jackanory*.

One senior Tory backbencher said Mr Osborne and Mr Cameron were indulging in hyperbole which was harming their case for Britain to remain in the EU. "They're making so much noise about how bad Brexit would be that it makes you wonder why we agreed to have this referendum in the first place. If you really thought it was going to be that bad, why did you decide to have it?"

It is a rhetorical question. Mr Cameron agreed in 2013 to hold the referendum as a device to try to hold his party together. It might have seemed a good idea at the time.

Additional reporting by Kate Allen and Jim Pickard

FT **Reality check** The FT dissects pro- and anti-Brexit claims ft.com/brexit

Global Insight page 7
Martin Wolf page 11

Alternative trade model

Out camp smitten with attractions of Albania

Bosnia, Serbia, Albania and Ukraine are economically weak, desperate to integrate with the EU, and still carrying deep scars from war and revolution. So what makes their EU trade model so attractive for Brexit campaigners?

The praise for the Albania-Ukraine option voiced by Michael Gove, justice secretary, echoes the work of pro-Leave analysts, who see the countries charting "a way forward" combining free trade with tailored political co-operation. The hitch is that Brussels sees the pacts, known as "stabilisation and association agreements" in the western Balkans, as special support at the start of a long journey towards EU membership for relatively small, troubled economies, rather than a divorce settlement for a big, successful one.

Karel De Gucht, the EU's former trade commissioner, said any Brexit comparison was "ridiculous nonsense". "Albania is a poor country, a small economy, under-developed," he said. "It is like comparing a little nut with a big watermelon."

Olli Rehn, who negotiated such pacts as EU enlargement commissioner, said he was "surprised" the Leave side would want an agreement that would put the UK "permanently on the substitute bench".

The main attractions for Leave supporters are outlined in Business for Britain's 1,000-page research document called Change or Go.

This looked at Ukraine's "deep and comprehensive trade agreement" as an "alternative model" to joining the European Economic Area, which comprises EU and European Free Trade Association nations.

It allows for a close economic relationship with the EU, without the political and financial obligations of an EEA country such as Norway, which semi-automatically applies EU law, accepts free movement and pays into the EU budget.

The report argues the Ukraine trade deal, hatched under the shadow of the Russian annexation of Crimea and war in eastern Ukraine, was an "under-examined way forward" that covers "all the key aspects, as well as lightening the obstacles to trade, but without uniformly applying red tape across the home economy".

It goes on to say the format has similarities with the EU's approach to former communist countries in the western Balkans — first called the Central European Free Trade Agreement. These attempted to clear trade barriers without cumbersome requirements to pool sovereignty or accept rules wholesale.

For a country such as Albania, this has morphed into an association agreement that sets a framework for it to move closer to EU law and business standards, in part to give EU investors confidence to work in the country.

In theory, the pact is broad, covering trade in goods and — crucially for the UK — potentially financial services, but only amounts to full single market access if Albania adapts it to apply the existing and future EU rule book.

In financial services, it also relates to a tiny Albanian cottage industry, with barely any integration with the European market, whereas the City of London is the region's biggest financial hub, handling 40 per cent of wholesale euro-denominated trade.

Alex Barker, Brussels

Lords committee

Carney defends BoE public stance on Brexit

EMILY CADMAN

The Bank of England has a "duty" to speak out about the risks of the referendum on the UK's membership of the EU, governor Mark Carney said as he hit back at critics who have accused him of interfering in political matters.

Mr Carney told a House of Lords committee yesterday that it was a fundamental part of being an "open and transparent central bank" to report its judgments to parliament and the public.

"Assessing and reporting major risks does not mean becoming involved in politics; rather it would be political to suppress important judgments which relate directly to the bank's remits and which influence our policy actions," he said.

While the BoE has been careful to stress it will remain neutral in the campaign, it has repeatedly flagged that the EU vote is the biggest domestic risk to financial stability and has given considerable ammunition to the Remain camp. The tone and content of its statements have infuriated Leave campaigners.

After a recent hearing in the Commons, Eurosceptic MP Jacob Rees-Mogg accused Mr Carney of giving answers that are "speculative and beneath the dignity of the Bank of England", while former chancellor Lord Lawson said it was "quite wrong" for a BoE governor to enter the political fray in this way.

But Mr Carney said it was part of the BoE's core remit to assess the implications of the referendum for financial stability and monetary policy.

"The bank has a duty to report our evidence-based judgments to parliament and to the public," he said.

Whereas for the Scottish independence referendum the BoE publicised its contingency plans after the vote, the bank has already announced plans for a number of extra liquidity options around the June 23 vote to lower the risk of British banks running out of funds.

Mark Carney: governor says BoE has duty to report its judgments

Mr Carney said the BoE would continue to both develop and "if necessary" implement such plans, adding "we will communicate as much as is prudent about those plans in advance of any risk materialising and as comprehensively as possible once risks have dissipated".

The governor also told the economic affairs committee that some of the risks to the UK economy the BoE had flagged "may be beginning to manifest". He pointed towards the falling value of sterling, the rising cost of buying protection against further falls and a 40 per cent drop in commercial property transactions in the first quarter.

Mr Carney also offered backing for the Treasury's dossier earlier this week, on the costs of leaving the EU to the UK economy, saying the "broad approach" seemed sound. He added that the underlying economics were "consistent with the broad economic strategy the UK has pursued effectively since the repeal of the corn laws". Leave campaigners accused the Treasury of "scaremongering".

NATIONAL

New unity government

Hammond rules out Libya combat troops

Foreign secretary willing to send personnel to help train national forces

JIM PICKARD
CHIEF POLITICAL CORRESPONDENT

Philip Hammond, the foreign secretary, sought to reassure sceptical Conservative MPs as he insisted that there were no plans for British troops to be involved in frontline fighting against Isis in Libya.

Mr Hammond, who visited Tripoli this week, said there had been no request by the new UN-backed Government of National Accord for foreign combat troops on the ground.

However, the UK was willing to send troops — in the tens or hundreds — to help train forces under the command of the new "unity" government, he said.

Mr Hammond faced tough questions from his own backbenchers over Britain's involvement in the war-torn state, which has the largest oil reserves in Africa.

Libya has been a borderline failed state since western forces helped topple Muammer Gaddafi in 2011, prompting military conflict between various militias and factions — while Isis has secured a foothold of more than 3,000 militants in the coastal city of Sirte.

John Baron, a Tory MP, said the British-French action five years ago had been an "unmitigated disaster" and urged ministers to learn lessons from its previous mistakes.

Andrew Murrison, another Tory backbencher, said that a previous attempt to train Libyans in the UK had been a "disaster": that scheme was ended after claims of sexual assault and widespread indiscipline.

Mr Hammond visited Tripoli yesterday to show support for Fayez Sarraj, the new prime minister of the fledgling administration, based in a naval base in the harbour.

The new unity government was set up to end the instability of having two competing governments at either end of the country. Earlier this month the Islamist-allied administration in Tripoli announced it was stepping down. But Mr Sarraj still faces opposition in eastern Libya, where there remains a rival administration backed by remnants of the country's old army.

Sir Edward Leigh, a senior Tory MP, said the new administration was in reality "holed up in a naval base" and hardly controlled any of Libya, a country the size of western Europe.

The consequences of western intervention in 2011 had been "death and destruction" across the region, he said. "Can we learn the lessons?"

Updating the House of Commons about his trip, Mr Hammond acknowledged that Libya was suffering from a liquidity squeeze in its banking system, a shortfall of energy provision and a shortage of commodities.

But he said the country still had the potential to be a "rich" successful state. "There is the potential for this to be a real turning point in Libya's fortunes," he told MPs.

British special forces are already operating in the country, it has been reported, but Mr Hammond insisted there was no "appetite" for conventional troops on the ground. He quashed speculation that as many as 1,000 British troops could be asked to take part in an international force in the country.

"We do not anticipate any requests from the GNA for ground combat forces to take on Daesh (Isis) or any other armed groups and we have no plans to deploy troops in such a role," he said.

Yet the foreign secretary also suggested that now was the time for the new Libyan government to take action against Isis while it was still "relatively thin on the ground".

If that occurred, it was likely to seek naval and air support from international allies, he acknowledged. The training support being offered did not need the approval of parliament, he said, given the UK had no fewer than 16 such operations around the world.

Foreign dividends

Prudential closer to tax refund after marathon court battle

VANESSA HOULDER

Prudential came a step closer to securing a tax refund of more than £100m yesterday, in the latest round of the UK insurer's long-running battle for compensation over past breaches of European law.

Judges at the Court of Appeal rejected nearly all of HM Revenue & Customs' arguments against an earlier ruling they described as a "masterpiece of exposition and reasoning".

The decision also increases the likelihood of payouts running into hundreds of millions of pounds for 10 other insurers that were part of the case led by Prudential.

The case is one of a number of hugely complicated legal cases — involving multiple court hearings in the UK and Luxembourg — in which companies are trying to recover tax paid decades ago. At that time, many of the UK tax rules broke European law by treating cross-border transactions less favourably than domestic transactions.

The tax authority said: "HMRC is extremely disappointed with this judgment. Nothing is payable immediately as a consequence of these decisions and we plan to robustly defend our position through future appeals."

Prudential declined to comment, but Graham Aaronson of Joseph Hage Aaronson, the litigators acting for Prudential, said: "It is obviously an encouraging result."

The Treasury moved last year to impose a new 45p tax rate on refunds, in an attempt to ensure that claimants "do not enjoy an unfair tax advantage at the expense of the public purse". The move was a sign of fears over the impact of the claims on the exchequer, as well as the likely public anger over large payouts at a time of spending cuts.

£7.2bn	£100m
Total provisions made by HMRC likely to be paid over five years	Tax refund Prudential may receive in compensation

Breaches of European law are one of the legal risks that has led HMRC to make provisions of £7.2bn. The Office for Budget Responsibility expects the provisions to be paid out over five years, pencilling in payments of between £500m and £2bn in any single year.

Tax experts said it was not yet clear whether HMRC would get permission to appeal to the Supreme Court. The 13-year-old case has already involved several high court hearings and a referral to the European Court of Justice. Yesterday's judgment described the length of the litigation as "inordinate". The judges said: "Whether the final end is in sight after all this time remains to be seen."

The case pivots on the free movement of capital provisions originally enshrined in the Treaty of Rome, which means that member states are not allowed to treat foreign dividends less favourably than domestic ones. The latest phase of litigation will determine how much tax needs to be refunded to Prudential's policyholders and shareholders, after the courts previously established they had overpaid tax on foreign dividends.

Prudential's claims extend from 1990 to 2007, a period when it received several thousand dividends. The overpayment of tax on foreign dividends diminished the investment returns to with-profits policyholders, as well as shareholders. The company has not said how it would distribute the compensation.

The Court of Appeal's decision focused on highly technical issues around how much credit needed to be given for the foreign taxes it paid. The size of the refund from HMRC will also depend on whether the interest paid is compound or simple.

Culture and conquest British Museum to showcase Sicilian artefacts

Gilded bronze and gold falcon, circa 1200-1220

Ceramic bowl with triskelion, circa 650-600BC

The British Museum has gathered more than 200 objects for its new exhibition, which will retell the history of the Italian island of Sicily from about 735BC, when the Greeks made their first official colony at Naxos, through Carthaginian and Roman rule to its time under Norman conquerors and beyond. Sicily: Culture and Conquest will run from April 21 to August 14

Regione Siciliana; The Metropolitan Museum of Art

Marble statue of warrior, Akragas, Sicily, circa 470BC

Race for London. Central issue

Extremism looms large in mayoral election debate

The Labour candidate is ahead in the polls but fears that his campaign is being damaged

CONOR SULLIVAN

Sadiq Khan visited Battersea earlier this month, going door to door to canvass votes for his bid to be London's next mayor. One of his stops was with Silvestro de Besi, a 56-year-old insurance broker. His reaction to Mr Khan suggests that questions over the former human rights lawyer's links to extremists may be damaging his campaign. Mr de Besi said he could not make up his mind who to vote for because there had been "lots of information in the papers, rightly or wrongly, on terrorism".

Mr Khan's main rival in the London election on May 5, Zac Goldsmith, has repeatedly pushed allegations about the Labour candidate and extremism to centre stage. He has not accused Mr Khan of sympathy for extremists, but says there are concerns over his judgment.

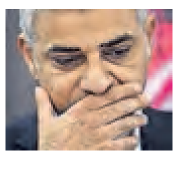
The accusations have diverted attention from Mr Khan's policies on two of London's most pressing problems: housing and public transport. Ahead by 10 points in the latest polls, he has tried to allay the damage by promising to be "the British Muslim mayor who will take the fight to extremists". He has also pledged to back police officers forced to shoot to kill in terrorist incidents and pointed out that he received death threats as an MP after voting for gay marriage.

Before becoming an MP in 2005, Mr Khan was a leading human rights lawyers and chairman of campaign group Liberty. He wrote a chapter called "Actions against the police" in a legal guide about fighting racism that advised readers to "think laterally in looking for human rights issues: many are not obviously a breach of human rights, but have a human rights angle".

The Goldsmith campaign has attacked his record, saying a person who helped those who "seek to do our police and capital harm" and "coached people in how to sue the police" should not be mayor.

Mr Khan accepts some former clients were "unsavoury" — they included the 9/11 plotter Zacharias Moussaoui. But he says that "even the worst people deserve a legal defence". Another client was Louis Farrakhan of the Nation of Islam. Mr Khan said "one of the great things about this country is due process, the presumption of innocence . . . Some of my clients were victims of police misconduct. Our police are not perfect. But I would rather live in a country where the police are accountable".

Mr Goldsmith said his rival has spoken at events where some of the other speakers had been extremists. In 2003, Mr Khan spoke at a conference about Guantánamo Bay prisoners organised by Yasser al-Siri, who once said Osama bin Laden "died an honourable death".



Sadiq Khan: the Labour candidate said he had made it clear he found extremist views 'abhorrent'

Mr Khan attended meetings of Stop Political Terror, the forerunner to Cage, a lobbying group that has spoken positively about "Jihadi John", the terrorist accused of murdering westerners in Syria. He accepts it is "possible" he has spoken alongside Suliman Gani, an imam in his Tooting constituency who has said women are "subservient".

Mr Goldsmith said in a BBC debate on Monday night that "we have a massive battle on our hands, an ideological battle, a battle that right now we are probably losing, and it doesn't help to give platforms or oxygen or cover to people who mean to do us harm".

Mr Khan replied: "I regret giving the impression I subscribed to their views and I've been quite clear I find their views abhorrent."

A spokesperson added: "Sadiq has spent his entire career fighting extremism — a fight which is made much harder by this kind of dog-whistling from the Tories — which just drives mainstream Muslims into the arms of the extremists and puts them off engaging with politics and public life."

Theresa May, home secretary, has criticised Mr Khan for being "in contortions over whether Babar Ahmad — a man subsequently [jailed for] conspiracy and providing material to support terrorism — was a friend of his or not".

Mr Khan said he supported Mr Ahmad, a constituent, in his unsuccessful battle against extradition to the US. But so did current mayor Boris Johnson. There was concern at the time about what Mr Goldsmith described as "lop-sided extradition arrangements to the US". Mr Ahmad's crime was committed in the UK, leading to accusations about justice being outsourced to the US. In 2012, Mr Goldsmith said that his was "a story which has caught people's imagination. I've been bombarded with letters from my local constituents".

A spokesman for Mr Goldsmith said: "There are a million miles between Zac's comments on extradition and cases involving his constituents, and Khan's repeated attempts to demonstrate that Ahmad, a man who pleaded guilty of terror offences, was innocent."

Mr Khan, with another two of the four Muslim MPs and organisations such as the Muslim Council of Britain, signed a letter to the Guardian in August 2006 saying Britain's foreign policy in the Middle East offered "ammunition to extremists" and put civilians at increased risk. He said at the time that "current policy on the Middle East is seen by almost everyone I speak to as unfair and unjust. Whether we like it or not, such a sense of injustice plays into the hands of extremists".

Mr Goldsmith said last week that this amounted to "blaming terrorism on British government policy".

Transport technology

Carmakers struggle to overtake motorists' lack of confidence in driverless vehicles

PETER CAMPBELL
MOTOR INDUSTRY CORRESPONDENT

The majority of drivers believe driverless cars are unsafe, according to a survey that shows the gulf in public confidence that carmakers have to bridge.

The motor industry has invested heavily in driverless technology to try to produce fully autonomous cars by the end of the decade, but a survey from What Car? said more than half of consumers feel either "unsafe" or "very unsafe" travelling in a fully autonomous vehicle.

Some 45 per cent of the 4,000 surveyed said they found "the idea of a car that is capable of taking over the entire driving process very unappealing".

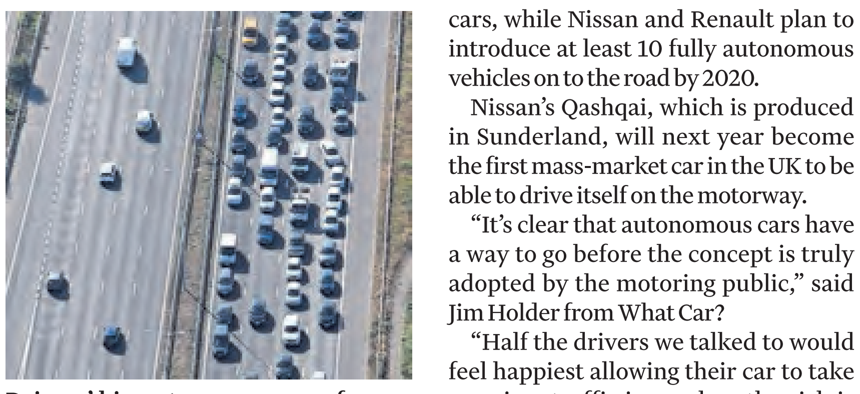
The report said: "The biggest concern among drivers was that an autonomous car would not be able to avoid an accident, with a third (34 per cent) citing that as their biggest reservation."

The results suggest that winning over public attitudes may be just as large a hurdle for the industry as designing the technology and winning regulatory approval to roll it out.

George Osborne, chancellor, has pledged to bring in regulations to allow driverless vehicles on UK roads by the end of the decade.

Carmakers say that vehicles with greater autonomy will be safer. Globally there are 1.2m deaths a year caused by motor accidents, and more than 90 per cent of crashes are caused by human error. By contrast, machines do not get distracted by mobile phones or fall asleep at the wheel.

Half of the cars sold in the UK have collision avoidance technology, including sensors that warn a driver if they are drifting out of a motorway lane. Several makers are working on fully driverless cars, while Nissan and Renault plan to introduce at least 10 fully autonomous vehicles on to the road by 2020.



Drivers' biggest concern was of cars being unable to avoid an accident

Nissan's Qashqai, which is produced in Sunderland, will next year become the first mass-market car in the UK to be able to drive itself on the motorway.

"It's clear that autonomous cars have a way to go before the concept is truly adopted by the motoring public," said Jim Holder from What Car?

"Half the drivers we talked to would feel happiest allowing their car to take over in a traffic jam, when the risk is minimal, while hardly any of them would feel safe letting their car guide them along urban and country roads."

A 2014 study by Sciencewise, a policy research group funded by the Department for Business, found that consumers were worried about the technology, given experience of phones and computers. "They feel machines aren't up to tasks where human lives are at stake," said the report. "If the car requires a human to take over the controls in an emergency, the driver may be too out of practice to safely do so." Nissan found many of the concerns were alleviated once people travelled in the cars.

INTERNATIONAL

Jobs market

US labour shortage set to drive up wages

Lack of skilled workers and ageing population likely to squeeze corporate profits

SAM FLEMING — WASHINGTON

The US faces significant labour shortages in a wide range of sectors as unemployment falls towards 4 per cent and the working-age population stagnates, a leading business group has predicted.

With the time needed to fill a job already near the highest in at least 16 years and the number of people voluntarily leaving jobs at its strongest since the recession, difficulties finding skilled labour will intensify, pushing up wages and squeezing corporate profits, the Conference Board said in a report.

Barring a recession, joblessness should fall another point compared with its 5 per cent rate now, and wage growth will be running at 3-3.5 per cent in 2017, a percentage point higher, said the board.

A lengthy list of lines of work that will show significant shortages includes occupational therapists, nurses, plant operators and machinists. The states with the tightest labour markets include Texas and Colorado.

"We are already very close to full employment, yet we have this trend of very slow growth of labour supply for the next 15 years, and there is very little that could be done about it barring major immigration reform," said Gad Levanon, the Conference Board's chief economist for North America.

"The implication of that is it is harder to find workers, and there is more acceleration in labour costs."

The jobs market has tightened steadily even as growth in gross domestic product remains lacklustre, presenting a conundrum to Federal Reserve policymakers as they consider the next move in interest rates. One question Janet Yellen, the Fed chair, and her colleagues are trying to answer is how much hidden slack there is in the workforce — for example, people working part-time because they cannot find a full-time job.

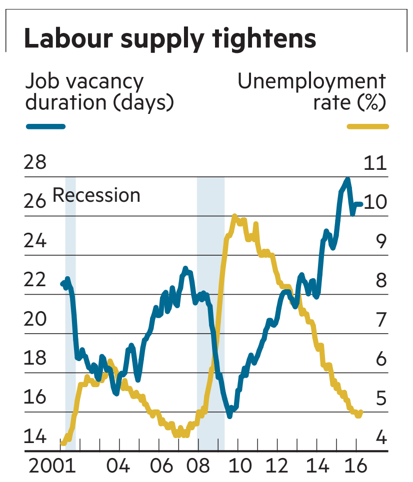
Slow wage growth suggests that considerable slack remains, but some measures of wage growth are starting to stir. The Fed's so-called Beige Book survey last week reported that the firming labour market was starting to deliver higher wages in nearly every region of the US.

Some employers are lifting entry level wages and states including California and New York are aggressively boosting minimum wages to well above the federal minimum of $7.25 an hour.

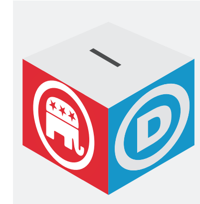
Analysis from Goldman Sachs estimated this week that labour costs as a share of S&P 500 companies' revenues rose to 9.8 per cent last year compared with 9.1 per cent in 2014, and were set to jump further.

While demand for workers has been sufficient to lure some Americans off the sidelines and into work, the steady exit of ageing baby boomers from the workforce is likely to weigh on the labour force participation rate in the longer term. That is good news for employees, Mr Levanon added, because it should mean pay increases faster.

Labour supply tightens



Sources: DHI Group; Bureau of Labor Statistics



Election updates
For latest news and results from the Democratic and Republican primaries in New York
ft.com/uselection

Android

Google and Brussels prepare for battle

CHRISTIAN OLIVER — BRUSSELS

The EU is poised to open a new front in its showdown with Google as early as today by announcing formal charges in relation to the company's mobile operating system, Android. The case would represent a new chapter in Brussels' efforts to combat the alleged abuses of US technology companies, and has already drawn comparisons to its clash with Microsoft a decade ago.

Hasn't the EU already charged Google with anti-competitive behaviour?

Yes, this would be a second charge sheet, known as a statement of objections. The first accused Google of abusing its dominance of online search to promote its own shopping services unfairly. Google denies the charge.

How dominant is Android as the operating system on smartphones?

Very. More than 80 per cent of smartphones globally use Android's open-source system, which can be used free of charge by anyone. By contrast, Apple's own iOS operating system represents only about 13 per cent of the market, according to data from Gartner.

Is being so dominant illegal?

No, but EU rules mean that Google faces special requirements not to crush new market entrants.

Why does the commission think Google could be harming other companies?

Margrethe Vestager, competition commissioner, says she is concerned that Google is forcing phonemakers and operators to enter into contracts that preload Google apps on to smartphones. This means that Google could be stifling smaller, innovative app makers and service providers.

Wasn't this problem of pre-installed software at the heart of EU's epic Microsoft case?

There are some similarities. Microsoft was bruised by its years of antitrust conflict in Brussels and was found to have abused its dominance of PC operating systems to force its media player on consumers. The case closed in 2007, with more than €2bn in combined fines. But the digital world has changed. Microsoft was making money by selling the software itself. Android is free of charge. Google is monetising the platform in a far more complex way, by harvesting data on users to target them more effectively with advertising and selling its services to them with different apps.

Do we expect any other charges?

The investigation has focused on two other areas. Brussels has said it is examining whether Google prevents smartphone makers from developing their own modified versions of Android, called "Android forks". Ms Vestager will also probably have to broach the difficult subject of "tying" — weighing up whether Google illegally hindered rival apps by establishing digital connections that automatically push Android users towards Google's own services.

What does Google say?

The company denies all wrongdoing. It says its app networks have given consumers more choice than ever before. It flatly rejects any suggestion by the commission that it is trapping customers into using its apps. The company says that its competitors' apps — from the likes of Facebook, Amazon, Microsoft and Expedia — are easily available with Android. Samsung's mobile phones are pre-installed with apps from Google's rivals. Companies including Nokia and Amazon have also used versions of Android without pre-installing Google apps.

Competition chief Margrethe Vestager, left, is concerned that Google is forcing phonemakers and operators to enter contracts that preload Google apps on to smartphones
Justin Sullivan/Getty Images
Emmanuel Dunand/AFP/Getty

Why isn't Apple's closed iOS operating system under the spotlight too?

That returns us to the issue of dominance. Google is feeling the heat because its market share is so much bigger than Apple's and it is therefore under greater pressure to change its behaviour.

What is the potential remedy if the commission does conclude there has been wrongdoing?

Some lawyers close to the case think the most likely course is that Brussels will seek to revise the contracts between Google and phone companies.

Will Google have to pay a fine?

If the commission finds wrongdoing, it can impose a fine of up to 10 per cent of the previous financial year's turnover, which was $74.5bn in Google's case. Most people involved rule out a fine anywhere near the maximum.

Editorial Comment page 10

Brazil

Rousseff pledges long fight against proposed impeachment

JOE LEAHY — BRASÍLIA
GEOFF DYER — WASHINGTON

Dilma Rousseff has promised to fight on against an attempt to impeach her, which she dismissed as part of Brazil's long tradition of coups.

In her first meeting with the foreign media after the lower house of congress voted to impeach her on Sunday, the president said her country had a tradition of not respecting elected authority that dated back 60 or 70 years.

"Brazil has a dormant coupist streak," Ms Rousseff said. "If we follow the trajectory of the presidents of our country . . . we will see that impeachment has systematically become an instrument for use against elected presidents."

The president, under pressure for a collapse in economic growth and a vast corruption scandal at Petrobras, the state-owned oil company, is locked in a bitter fight with her vice-president, Michel Temer, who will take her job if she is impeached.

The motion has now moved on to the senate. If more than half of the 81-seat upper house accepts the motion, which argues that Ms Rousseff violated the law by fudging the national budget to disguise a deficit, Ms Rousseff will be suspended and Mr Temer would take over as soon as early next month.

If after up to six months of deliberations the senate decides by a two-thirds majority to formally impeach Ms Rousseff, Mr Temer would assume power until the next elections in 2018.

The opposition has begun to fight back against Ms Rousseff's characterisation of the proposed impeachment as a coup, saying the country needs to get a new and stable government in place as fast as possible to rescue it from the worsening economic crisis.

"Congress and Brazilian society has realised we are rapidly arriving at the bottom of the well," said senator Aloysio Nunes of the opposition PSDB party. "We do not have hyperinflation, but we do have a social crisis. We have had two years of a recession which has no parallels, not even the crisis in 1929 and 1930. The social situation is one of emergency and congress is aware of this."

Backing congress's charges that Ms Rousseff manipulated the budget, allowing her to spend more ahead of the 2014 elections, he insisted the impeachment was legal. "We would be a banana republic if the president could do whatever he or she wanted, whatever enters his or her head, without anything ever happening to them," he said.

Mr Temer is the head of the PMDB, the biggest party in congress and until recently Ms Rousseff's main coalition partner. Yesterday, Ms Rousseff bitterly attacked him as the leader of the "coup".

"It is startling that a vice-president in the exercise of his mandate would conspire openly against the president," Ms Rousseff said. "In no democracy in the world would a person who did that be respected because every one of us knows the injustice and pain that you feel when are betrayed."

Asked if she would call early elections, Ms Rousseff did not dismiss the notion but said it was not being considered at present. "This is not the beginning of the end; we are at the beginning of the fight, and it will be a long one," she said.

Egypt tensions

Italy revokes cyber security company's export licence

JAMES POLITI — ROME
HANNAH KUCHLER — SAN FRANCISCO

The Italian government has stripped controversial cyber security company Hacking Team of its licence to export outside the EU amid growing scrutiny of its sales of surveillance software to repressive regimes such as Egypt.

The move coincides with a sharp rise in diplomatic tensions between Italy and Egypt over the brutal murder of Giulio Regeni, a 28-year-old Italian research student in Cairo.

Italy's ministry of economic development said the decision to revoke the licence was necessary due to "changed political circumstances" in a number of markets where Milan-based Hacking Team had been doing business. Although no specific country was mentioned, the company sold its products to Egypt, Brazil, Kazakhstan, Lebanon, Thailand and Vietnam in 2015, according to one Italian official.

Italian officials suspect Regeni's death was the work of Egypt's security services, despite Cairo's denials, and Rome's mistrust of official accounts of the student's death reached a tipping point last week when it recalled its ambassador to Cairo for consultations.

Although there is no evidence that Egypt used Hacking Team technology to keep track of Regeni, and Italian officials deny any explicit connection with the loss of the export licence, experts say the killing may have accelerated an effort already under way to keep closer tabs on the company's sales.

"Hacking Team was already in the spotlight but my sense is that the media and political pressure of the Regeni case might have accelerated the analysis and the decision-making around it," said Paolo Boccardelli, director of the business school at Luiss University in Rome. "It certainly didn't help the company to be providing this kind of technology to a government with which there is diplomatic tension."

Eric Rabe at Hacking Team acknowledged there had been a "certain political pressure to be more circumspect about licences" and said Egypt was "a good example of a country where the politics have changed and the relationship has changed". But he was cautious about drawing any conclusions, adding: "Whether that is the factor behind this decision I don't know — nobody has confirmed that."

Mr Rabe denied the loss of the licence, which emerged earlier this month, was a "game changer" for the company, since it was still free to export within the EU and could apply on a case-by-case basis for Italian government approval to sell its products outside the EU.

Hacking Team sells a remote-control system used by more than 50 government agencies worldwide to track criminals and terrorists online, and boasts on its website that it can bypass encryption. The company hunts for previously undisclosed vulnerabilities in software — known as zero-day exploits because the software maker has zero days to fix them before they become a problem — to exploit with its product.

A protest in Rome over the death of Giulio Regeni, which has soured relations between Italy and Egypt

Human rights groups have criticised Hacking Team for selling to regimes that may be using its tools to track dissidents and journalists. Privacy International named Hacking Team last month as one of the companies that sold "sophisticated surveillance technologies" to the technical arm of the Egyptian intelligence services worth about €1m, according to a client list leaked last year.

In a report, the NGO said the Egyptian intelligence agency wanted to target Apple's iPhones and Mac computers, as well as people using pirated copies of Microsoft's Windows operating system.

The revocation of Hacking Team's licence — first reported by Forbes — came as signatories of the Wassenaar Arrangement, which governs the sale of arms, met in Austria last week to discuss whether or not to change the rules on granting export licences for cyber arms or so-called "dual-use technologies", which can be used as weapons and defensively.

Hacking Team says on its website that it obeys the Wassenaar rules, to which Italy is one of 41 signatories. It said it only sells to governments, not companies or individuals, and will not sell its products to countries blacklisted by the US, EU or UN, among others.

INTERNATIONAL

Leaders at odds

Merkel stance on migrant plan angers Renzi

Berlin rejects Rome idea to fund refugee expenses by issuing EU bonds

JAMES POLITI — ROME
STEFAN WAGSTYL — BERLIN
DUNCAN ROBINSON — BRUSSELS

Italian frustration with Berlin boiled over again as Germany slapped down a proposal from Rome to fund refugee expenses by issuing common EU bonds.

The spat reignited tensions between Angela Merkel and Matteo Renzi that appeared to have eased in recent months.

Amid concern at a big rise in migrant flows across the central Mediterranean to Italy in the first months of 2016, Mr Renzi, the prime minister, on Saturday asked the EU to offer financial incentives to countries in sub-Saharan Africa for them to curb migrant flows and readmit them after deportation.

The Italian plan, dubbed the "migration compact", was well received in Brussels. Donald Tusk, EU council president, welcomed the idea and agreed to "work on an ambitious plan" to stem migration with "third countries".

But one crucial aspect of the plan — to fund "migration management" costs in member states and investments in Africa with common EU bonds — was rejected by Ms Merkel, the German chancellor, with unusual force and speed, despite her great need to maintain the EU's tattered unity in the migration crisis.

Steffen Seibert, her spokesman, said on Monday that while Mr Renzi's plans for "a comprehensive external migration strategy" would "naturally be deeply studied", the EU bond idea was a non-starter. He said: "The federal government sees no basis for a common debt financing of the migration expenditures of member states." Mr Seibert added that the EU already had appropriate instruments in the bloc's budget.

Mr Renzi could not conceal his irritation at the German reaction. "We have proposed eurobonds . . . if Merkel and the Germans have different solutions they should tell us," Mr Renzi said in an interview on Rai, Italy's public television. "We're not stuck to a solution, but it's clear that this is a problem that the EU has to resolve, all together."

Tensions between Matteo Renzi and Angela Merkel had appeared to have eased in recent months

Ms Merkel is, however, only restating her well-known opposition to plans for EU bonds, which have been proposed repeatedly — with consistent backing from Italy — for funding common challenges since the 2008 financial crisis.

Germany has blocked the proposals because of fears that bonds could ultimately result in Berlin having to shoulder the debts of economically weaker countries, notably southern EU states.

The latest dispute between Mr Renzi and Ms Merkel comes after a few months of fragile detente between the Italian and German leaders. In December and January, Mr Renzi had repeatedly attacked Ms Merkel for pursuing policies that fuelled populist forces across Europe, but had toned down the rhetoric after a January 29 summit in Berlin.

Some observers believe that the Italians are using the spat as leverage to pressure the EU to grant Italy's demand for leeway on its budget rules to deal with migration expenses. A decision on those budget rules is due in early May.

Italy and Germany have clashed before on aspects of the migration crisis — namely on the EU-Turkey deal, which controversially stemmed migrant flows from the Middle East along the Balkan route last month, and on the fingerprinting of migrants at Italian ports.

But generally, Berlin and Rome have been allies in the push for a revision of EU asylum rules, a sweeping relocation policy to spread migrants across EU member states, and resistance to border closures undermining the passport-free Schengen area.

In Brussels, some officials within the commission are thought to be open to the idea of refugee bonds. A spokesperson for the EU's executive arm said that countries should be "imaginative" in the way they handled the refugee crisis.

The bluntness of Ms Merkel's latest rejection reflects the concern in her conservative CDU/CSU bloc about the recent electoral success of the rightwing Alternative for Germany party.

Immigration. Fragmented landscape

Refugee influx rattles 'Russia-Germans'

Socially conservative group's allegiance sways to the AfD in a politically divided arena

STEFAN WAGSTYL — PFORZHEIM

On the march: the refugee crisis has shaken certainties around the 2.5m Russia-Germans
Hannibal Hanschke/Reuters

Andreas Fabrizius, a 29-year-old welder from Pforzheim, is helping to stir up one of Germany's most settled immigrant communities — his fellow ethnic Germans from the former Soviet Union.

For years, they mostly backed Angela Merkel's conservatives, often out of respect for former chancellor Helmut Kohl, who opened Germany's doors to ethnic Germans from eastern Europe following the cold war. They mostly worked hard, secured jobs and sought to integrate; some saw themselves as even more German than the Germans.

But the refugee crisis has shaken certainties around the 2.5m "Russia-Germans", descendants of farmers who moved east centuries ago but kept their culture. In last month's regional elections, many gravitated towards the immigration-sceptic Alternative for Germany party that scored big gains in polls opposing Ms Merkel's open-door policy.

Among its biggest victories was in Pforzheim, a historic goldsmithing centre in south-west Germany with a large immigrant population, where the AfD won nearly 25 per cent — double the local regional average. And its best result in the town was 43 per cent in the modern suburb of Haidach, where nearly half the 8,500 residents have a Soviet family background, including Mr Fabrizius.

"I'm not against immigration," says Mr Fabrizius, who arrived in Germany in 2002. "But immigrants must conform with our rules, not the other way round."

Although he declined to say which party he supported, he delivered AfD-like warnings at a recent rally of about 800 immigrants. Mr Fabrizius now arranges patrols to keep Haidach "safe for ordinary people", even though police say local crime rates are low.

Russia-Germans are descended from settlers recruited in the 18th century by Catherine the Great, who came to live along the Volga river, giving rise to their original name, Volga Germans. During the second world war, Stalin saw them as potential collaborators and sent them to Siberia and central Asia. Many retain their German language and culture.

The success of the AfD in Pforzheim raises the prospects of further electoral gains among Russia-Germans, adding to Germany's already fragmenting political landscape. Security experts also warn the radicalisation of some Russia-Germans increases the chances of Moscow using them as a political weapon to try to undermine German and EU stability.

Manfred Gullner, head of the Forsa polling agency, cautions against generalisations and says local influences played a role. Pforzheim, for example, has a long rightwing tradition: it voted strongly in the 1990s for the Republicans, an earlier anti-immigration party.

But the correlation between concentrations of Russia-Germans and AfD voters is strong. Sergey Lagodinsky, an analyst at the Heinrich-Böll Foundation research institute and himself a former Soviet immigrant, says: "The Russia-Germans voted CDU because of Kohl. Now their trust has declined because of Merkel and her refugee policy. More and more will vote for the AfD."

This shift has been driven by more recent ex-Soviet migrants, whose political outlook is shaped less by gratitude to Mr Kohl than by admiration for Russian president Vladimir Putin. Unlike their elders, they feel confident about their Soviet past and stay in touch with their homeland via television and internet.

The newcomers' lack of integration barely registered politically until the Ukraine crisis began. This divergence has been compounded by the refugee crisis. Many Germans have been unsettled by the arrival of more than 1m mostly Muslim refugees since 2015. But Mr Lagodinsky says Russia-Germans have felt it more keenly because they are social conservatives; less exposed to ethnic diversity than other Germans.

With Germans already outraged over mass sexual assaults in Cologne on New Year's Eve blamed on Arab-looking men, reports emerged in January of a 13 year-old Russia-German girl in Berlin who claimed she had been raped by men of foreign appearance. Although police ruled her story was fabricated, the case of "Lisa" resonated among former Soviet immigrants, not least because Russian media highlighted the allegations.

> 'I'm not against immigration but they must conform with our rules, not the other way round'

Stefan Meister, a Russia expert at the DGAP think-tank in Berlin, says the Lisa case shows there is "a policy from the Russian side to activate [Russia-Germans]." But Fyodor Lukyanov, editor of Russia in Global Affairs magazine, says: "It's a very Soviet way to find somebody outside to be responsible for dysfunctions in one's own system."

Mr Meister fears Kremlin-backed media could now seek to fuel discontent over other issues, not only among Russia-Germans, but among the country's 3m other Russian-speaking immigrants. This creates the prospect that more will switch to upstart parties such as the AfD. "I think the Russians were surprised by the Lisa case and have started to explore other possibilities."

Budget gap

Kremlin orders state companies to pay higher dividends

JACK FARCHY — MOSCOW

Russia has ordered its state-controlled companies, including gas giant Gazprom, to pay at least 50 per cent of their 2015 earnings in dividends, the latest of a string of measures designed to plug a gaping hole in the state budget.

The move would require eight state-owned entities to increase significantly the amount they pay the government and other shareholders in dividends — potentially forcing them to increase leverage or cut spending.

Dmitry Medvedev, prime minister, signed an order mandating the new dividend levels on Monday, according to a statement published yesterday. The move would bring an extra 100bn roubles ($1.5bn) to the 2016 state budget, he said. It comes as Russia is braced for a second consecutive year of recession amid lower oil prices, sending the government scrambling to amend its budget. It was planned on the assumption of a 3 per cent deficit based on crude prices averaging US$50 per barrel.

For Russia, which relied on oil and gas revenues for more than half of its budget until 2014, the slide in crude prices is painful. Last year, lower oil prices drove the share of oil and gas down to 43 per cent of budget revenues and in March that share fell to just 28.6 per cent.

Moscow has already made plans to cut spending by 10 per cent, and is planning to privatise government stakes in some of its most valuable companies, including oil companies Rosneft and Bashneft, diamond miner Alrosa and VTB, the country's second-largest bank.

However, it is still unclear how extensive the privatisation will be. Many influential figures in the Russian elite have argued against privatising state assets at current low valuations, while the corruption-tainted sales of state assets in the 1990s have tarnished the concept of privatisation for many Russians.

The move to mandate higher dividends also comes as Russia's plans to launch its first international bond since the imposition of sanctions over Ukraine look increasingly doubtful after western governments pressured banks not to participate in the deal.

"In the current situation, every rouble counts and the government is understandably trying to mobilise all resources to boost revenue so as to avoid deeper cuts to spending," said Vladimir Tikhomirov, chief economist of brokerage BCS, in a note to clients.

The higher dividend payments would apply to eight state-owned companies, according to a copy of the order published by the government yesterday: Gazprom, the state gas giant; Alrosa, the diamond miner; oil companies Bashneft and Zarubezhneft; RusHydro, the hydropower company; Sovcomflot, Russia's largest shipowner; Transneft, the state pipeline monopoly; and Rosneftegaz, a holding company for the state's stakes in the energy industry, including in Rosneft.

The order would require them to pay the higher of 50 per cent of net profit under international financial reporting standards (IFRS) or Russian accounting standards.

For some companies, that would require a significant lift in dividends — potentially benefiting minority shareholders. Gazprom's board has already recommended dividends of 7.4 roubles per share, which analysts estimate is roughly half what it would be forced to pay under the new rule. The company's shares jumped 6.6 per cent yesterday.

Nagorno-Karabakh

Moscow plays the peacemaker as decades-old conflict flares in the energy-rich Caucasus

JACK FARCHY

As one of Europe's most intractable conflicts teeters on the brink of war, Russia is in diplomatic overdrive.

Fighting between Azerbaijan and Armenia over the mountainous enclave of Nagorno-Karabakh left more than 100 dead this month and plunged a two-decade-old peace process into crisis.

In response, Vladimir Putin, the Russian president, brokered a ceasefire at talks in Moscow and sent some of his most senior lieutenants to the region. Analysts and diplomats say Moscow's move to act as peace broker could allow it to increase its already substantial influence in an energy-rich region that is a key focus of EU plans to diversify gas supplies from Russia.

"When the US has been so silent, Putin has filled a vacuum that leaves the impression in Baku and Yerevan that he's the only game in town," says Matthew Bryza, a former US ambassador to Azerbaijan.

Nagorno-Karabakh — a mountainous region roughly the size of Luxembourg — lies within the borders of Azerbaijan but is populated by ethnic Armenians. The conflict began in the dying days of the Soviet Union, and expanded into a bloody war that left more than 20,000 dead and a million displaced. The region has run its own affairs with support from Armenia since a ceasefire in 1994.

When the worst fighting since that ceasefire broke out on April 1, Russia's foreign and defence ministers were making calls to their Azerbaijani and Armenian counterparts within hours. A few days later in Moscow a truce was hammered out — at a trilateral meeting between the Russian, Armenian and Azerbaijani army chiefs. Days later, the Russian foreign minister and prime minister were in Baku and Yerevan.

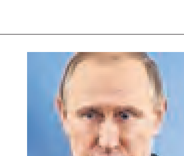
Moscow's energetic diplomacy overshadowed the work of the OSCE Minsk Group, a multilateral body co-chaired by the US, France and Russia, which since 1994 has been working to find a solution to the conflict. The group did not meet until April 5, by which time Moscow had brokered a ceasefire.

"It took me by great surprise that it took the OSCE Minsk Group co-chairs a considerable length of time to convene," said Tahir Taghizadeh, Azerbaijan's ambassador to London.

Armenia's foreign ministry said in a statement: "We are grateful for Russian efforts so far and we are hopeful that they will continue until a final resolution is reached."

Mr Taghizadeh criticised the west's lack of engagement: "The whole situation with the ceasefire regime not holding any more [. . .] is a direct consequence of the inability or unwillingness of the international community to act."

US diplomats privately concede there is little appetite to launch a new diplomatic push in the waning days of the Obama administration, according to people briefed on their thinking.



Vladimir Putin: Russian president sent ministers to the disputed region when fighting began

Still, Nagorno-Karabakh, located at the seam of Europe, Russia, Iran and Turkey, has the potential to destabilise the entire Caucasus region, say analysts.

The EU has tried to forge closer ties with former Soviet states in the region, which is strategically vital to the bloc as an energy supplier. The main oil pipeline from Azerbaijan to Turkey runs less than 30 miles from Nagorno-Karabakh.

Azerbaijan and Armenia accuse each other of starting the fighting. But as Thomas de Waal, an expert on the Caucasus at Carnegie Europe, says, exchanges of fire across the line of contact have become commonplace: "It's not really the question who fired the first shot, the question is who escalated and why."

The escalation appears to have been driven by Azerbaijan, which advanced beyond the line of contact to seize new land in the form of a few "strategic heights" — an escalation unprecedented since 1994. Mr Taghizadeh confirmed as much. Using a metaphor of a homeowner defending his house from squatters, he argued that "you will have to take up the shotgun at some point".

Russia has looked to strengthen ties with both countries following the flare-up. In Yerevan last week, Gazprom agreed to extend a gas supply contract with Armenia and cut already low prices. In Baku, Sergei Lavrov, Russian foreign minister, discussed a proposed railway line from Russia to Iran via Azerbaijan.

Nonetheless, Russia is not a wholly stabilising influence. It would continue to sell arms to both sides, Dmitry Rogozin, the deputy prime minister, said this week. And people who have worked on the settlement process say that neither side would have faith in a lasting peace brokered by Moscow alone.

As Mr Bryza says: "The key to resolving this is to get the two presidents to have sufficient trust in each other, and Russia is not going to be able to do that."

INTERNATIONAL

Obama faces testing talks in attempt to reshape Saudi ties

Riyadh looks to next president for closer relations while regional issues rile White House

GEOFF DYER — WASHINGTON
SIMEON KERR — DUBAI

Long before he became president, Barack Obama wanted to put some distance between the US and Saudi Arabia. During a 2002 speech against the Iraq war that eventually propelled his presidential bid, Mr Obama referred to the Saudis as "our so-called allies".

In the now famous Atlantic article last month on the "Obama Doctrine", Malcolm Turnbull, the Australian prime minister, was quoted as asking the president: "Aren't the Saudis your friends?" Mr Obama replied: "It is complicated."

With a hint of "be careful what you wish for" in the air, the consequences of Mr Obama's effort to reshape the relationship with the Saudis will be on display when he visits Riyadh today and tomorrow for a bilateral meeting and a regional summit.

He will be greeted by Saudi hosts quietly seething at their country being called a "free-rider" by the US president and looking past the election to see if the next occupant of the White House will try to restore the close relationship of the 1980s and 1990s.

But he will also meet a Saudi royal family that has in some ways taken the president at his word and taken more regional security matters into its own hands — in ways that have not always been to the liking of the White House.

"It is like this catch-22 where we want them to be more responsible for their own security, but when they do it, it can be ineffective and destabilising in the region," says Frederic Wehrey, of the Carnegie Endowment think-tank.

Tomorrow, Mr Obama will meet leaders of the Gulf Co-operation Council, the regional grouping that the administration has urged to work together more closely to deal with threats from Iran and other security issues.

Ashton Carter, US defence secretary, was due to meet his GCC counterparts yesterday to discuss missile defence and protecting against cyber attacks.

"From the start, there was a strategy of urging them to become more self-sufficient," says James Smith, US ambassador to Saudi Arabia during Mr Obama's first term.

While being urged to take more responsibility, the Saudis have found plenty of reason to question Mr Obama's commitment. Even before the negotiation of a nuclear deal with Iran, their great regional rival, Riyadh criticised the president for not backing Hosni Mubarak, the former Egyptian president, in 2011 and for not doing more to defeat the Assad regime in Syria.

The culmination of these frustrations has been the Saudi-led campaign in Yemen, which Riyadh says is aimed at restoring a government overthrown by an Iran-backed rebellion. While the US has provided some military support, it has privately criticised Riyadh for the humanitarian impact of the conflict.

Saudi irritation at the Obama administration has been matched in part by a revival of the sort of criticism of Saudi society that was common in the US after the 9/11 attacks. A bipartisan bill which would strip legal immunity for Saudi officials found to be involved in terrorist attacks in the US stands a good chance of passing the US Senate this year.

"I think their [the Saudis'] hope is that with a new presidency, things will revert to how they have been for decades, but there have been some deeper structural changes in the relationship," says Perry Cammack, a former state department official.

Yet for all the friction, the Obama administration has maintained — and in some ways enhanced — collaboration with Saudi Arabia. This will be Mr Obama's fourth visit, the most by any US president. The administration has also signed a record number of arms contracts with Riyadh, which surpassed Moscow to become the world's third-largest arms spender last year, and works closely with the Saudis on counter-terrorism. Saudi Arabia made corporate America its first port of call when trying to lure overseas investment to help transform the economy for a post-oil era. US exports to the kingdom continue to expand.

"This is an important partnership," says Derek Chollet, a former senior Pentagon and White House official in the Obama administration. "What Obama has been trying to do is have it evolve so that it can be sustained over time."

For its part, Riyadh wants more indication that the US will remain steady in its commitment to the region, and will prevent Iran taking advantage of the nuclear deal signed last year.

"Whenever we meet the Americans, it is clear that we have a special relationship, with overwhelming energy put into fostering that relationship," says a senior Saudi adviser.

"I think the Americans have already shown enough their confirmation of strength in our relations. We are just being more honest with each other."

The Saudi king, Salman bin Abdulaziz, far right, looks on as Barack Obama is welcomed to Riyadh in January last year. Below, smoke rises over Sana'a after a Saudi bombing raid on the Yemeni capital. The US has privately criticised Riyadh for the humanitarian impact of the conflict

Carolyn Kaster/AP; Mohammed Hamoud/Anadolu Agency/Getty

> 'Whenever we meet the Americans, it is clear that we have a special relationship. We are just being more honest with each other'

GLOBAL INSIGHT
WASHINGTON

Edward Luce

US leader's backing for Cameron over Brexit risks backfiring

George Canning, the 19th-century British statesman, famously called the New World into existence "to redress the balance of the old". David Cameron, UK prime minister, no doubt had similar hopes when he asked Barack Obama to visit the country this week barely two months before its Brexit referendum. Who better than a US president to refute the Brexiteer dream of replacing Britain's continental ties with an anglospheric world? Who better than Mr Obama to deflate the feverish ambitions of Boris Johnson, MP and mayor of London?

Alas, that is where the poetry ends. In the age of Donald Trump, Americans worry about the coarseness of their debate, but it is at least rivalled by Britain's tradition of character assassination. Mr Obama is taking quite a risk with his visit. US presidents make a point of avoiding other democracies ahead of general elections for fear of seeming to meddle. By putting the UK's economic and geopolitical future in question, the June 23 referendum is far more important than any ordinary election.

Instead of giving a helpful tilt to Mr Cameron's Remain campaign, Mr Obama's intervention could backfire. Even before Mr Obama opened his mouth, Mr Johnson last week accused him of "outrageous and exorbitant hypocrisy" for wanting Britain to persist with a sovereignty-pooling arrangement the US would never contemplate. Slightly more politely, a group of pro-Brexit members of parliament last month wrote to Mr Obama urging him not to interfere. "We would certainly never think of visiting the United States and telling the US public how to vote in an election or the amendment of their constitution," said Kate Hoey, a Labour party MP.

She had a point. Yet the intensity of the prebuttals before Mr Obama's visit betrays worries about his potential influence. Much of the Brexit case rests on the view that the UK could quickly negotiate a free trade agreement with the US. Having had to grapple with surging protectionist sentiment at home, Mr Obama is perhaps the world's leading expert on how difficult that would be to achieve. Last year Mike Froman, the understated US trade representative, said: "We are not particularly in the market for free trade agreements with individual countries," after he was asked about prospects for a US-UK deal. In plain English that meant there would be zero chance. Mr Obama will look for a tactful way to reinforce that point.

Furthermore, Mr Obama's popularity ratings in the UK are higher than for any local politician, including Mr Johnson. They are particularly high among Britain's millennial generation, whose high turnout would be key to defeating the pro-Brexit case in June. UK polls show younger voters are more comfortable with the EU than older ones. Mr Obama will hold a town hall event in London with young voters. He will have dinner with royals William and Kate and lunch with William's grandmother, the Queen.

The latter, who turns 90 tomorrow, might give Mr Obama a crash course on how to influence British voters without appearing to do so. Shortly before the referendum on Scotland's independence in 2014, the apolitical monarch urged Scots to "think hard" before they voted. It was clear in which direction she wished such thinking to go. The margin in favour of the status quo was wider than the polls anticipated. Mr Obama will be hoping for a similar outcome against Brexit on June 23.

In spite of Mr Obama's supposed coolness on the UK-US "special relationship", he readily agreed to this trip as a favour to Mr Cameron. "We want to do whatever Cameron thinks will help him to win this vote," says Lou Susman, Mr Obama's first ambassador to Britain, and an informal adviser. "Of course, it is entirely up to the British people which way they vote." Naturally, that goes without saying.

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South Africa. August poll

Corruption threatens Zuma's election hopes

Scandal over president means ruling ANC party faces uphill struggle to retain the big cities

ANDREW ENGLAND — PORT ELIZABETH

South Africa's ruling party boasted that more than 100,000 supporters would attend the launch of its manifesto ahead of crucial local elections.

The event, held at a stadium in Port Elizabeth, was meant to be a show of force after weeks of turmoil that had led to calls, even from within his African National Congress, for President Jacob Zuma to resign. But when he strode to the stage at the 46,000-seater stadium on Saturday, banks of seats were empty.

It illustrates the struggle the ANC faces ahead of the August poll. The former liberation movement may still draw thousands to its events but its support at the ballot box has waned at three consecutive votes since 2009. This year's municipal vote is expected to be the most fiercely contested since the ANC won the first democratic election in 1994.

The ANC's task has been exacerbated by the scandals engulfing Mr Zuma and threaten to cloud the party's election campaign. The most recent, which has triggered multiple calls for his removal, was a constitutional court ruling that he violated the constitution by failing to abide by the public protector's recommendations that he repay some of the millions of dollars of taxpayers' money spent upgrading his private residence.

At stake is the ANC's hold on big cities, including Johannesburg, the commercial hub, and Pretoria, the capital. The poll will gauge how much damage the controversies dogging Mr Zuma have wrought on his party and whether the opposition can capitalise on it.

The ANC's slim majority in Port Elizabeth in the Eastern Cape, a party stronghold, is considered the most vulnerable. Should it lose control of the city it would be a damaging blow to the ANC, heaping more pressure on Mr Zuma and presenting further evidence that voting patterns in Africa's most industrialised nation are gradually shifting.

"It would mean they can no longer talk of a sentimental hold that the ANC has over black voters; the emotional umbilical chord has been severed forever," says Mcebisi Ndletyana, an associate professor at Johannesburg university.

At present, only one big urban centre where black Africans are not in the majority — Cape Town — falls outside the ANC's control. But if the opposition is able to break the ANC's majorities in other cities, the former liberation movement will be increasingly reliant on poorer, rural areas.

"There's no doubt about the critical nature of this election," says Mmusi Maimane, leader of the Democratic Alliance, the main opposition. "You could end up with a scenario . . . where the liberation movement governs in rural areas through patronage; and in urban areas people making decisions on the basis of different choices."

In many ways, Nelson Mandela Bay Municipality, which includes Port Elizabeth, is a microcosm of the ANC's problems in cities where urban voters have grown frustrated with poor service delivery, mismanagement and corruption.

In an attempt to turnround its fortunes there, the ANC appointed Danny Jordaan — who led South Africa's successful 2010 football World Cup bid — as mayor 10 months ago. Since then he has battled to sort out its finances and dismissed 29 senior city officials.

Mr Jordaan acknowledges it would be "devastating" if the ANC lost control of the municipality. The party won 52 per cent of the vote there in 2011 local elections and less than 50 per cent in a national vote in 2014.

"If the ANC succeeds here and regains its strength, it would have been a benchmark . . . It would say: 'This is what we actually need to do. Roll up our sleeves and admit that yes there's corruption . . . and deal with it,'" he says. "It's very clear to me the people love the ANC but they hate corruption. Remove corruption and the people will love the ANC."

Yet Mr Zuma's battered credibility makes the task far harder. The president's charisma and common touch play well in rural areas, but analysts say urban voters are angered and disillusioned with their president.

Even at the manifesto launch, there were ANC supporters who felt he should resign. After initially saying he backed the president, Tapami, an unemployed man wearing a T-shirt handed out by the ANC with Mr Zuma's face on it, admitted "we want him to step down".

He added he would still vote for the ANC and in the eyes of many black voters, the ANC remains the only credible political option.

But the August vote will test the strength of that loyalty and others are already demanding change.

Linda Alindile, a university student planning to vote for the Economic Freedom Fighters, a radical breakaway of the ANC, said: "They are all corrupt, or most of them are. In the ANC, the more corrupt you are the higher you rise."

Waning support: President Jacob Zuma has faced calls for his removal

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Geneva negotiations

Syrian peace talks on verge of collapse as ceasefire fails

ERIKA SOLOMON — BEIRUT

Syrian peace talks appear close to collapse in Geneva after the opposition declared a "pause" in its participation and fighting intensified in the country.

Activist groups reported increased government shelling across northern and central Syria yesterday, a day after some rebel groups launched the "Battle to Redress Injustices" in response to regime air strikes.

The opposition and President Bashar al-Assad's forces accuse each other of violating a US and Russian-brokered ceasefire that looks increasingly irrelevant in many parts of the country.

The opposition's High Negotiations Council in Geneva, facing growing frustration from rebels on the ground, said on Monday it had requested a "brief hold" to its participation. It said the move was in protest at ceasefire violations by Assad forces and a lack of progress in improving conditions, such as increased access, to millions of people in areas besieged by pro-regime forces.

Staffan de Mistura, the UN special envoy for Syria, said he would continue with the effort, already run as indirect talks, by pursuing "technical discussions" with the HNC at its hotel in Geneva.

Both sides seem to be stepping up the rhetoric at a time when the future of the talks already looks bleak. One western diplomat likened efforts to keep the talks going to "watching a slow-motion car crash".

This round of peace talks is the third since the US and Russia, which back opposing sides in Syria's five-year civil war, began pushing for a revival of negotiations. This is Mr de Mistura's first attempt at raising political transition, the most contentious subject of all.

The opposition wants a transitional governing body that excludes Mr Assad and his inner circle. Mr Assad's delegation proposes expanding the government to include opposition figures.

At a news conference yesterday, Riyad Hijab, the HNC president, said the opposition would accept only "real political transition".

"We will not surrender, oh sons of our people, as long as we have a pulse," he was quoted as saying on HNC's Twitter page. "We did not come to Geneva to reproduce the Assad regime, we came to end this criminal regime."

Earlier yesterday, Bashar al-Jaafari, the head of Mr Assad's delegation and Syria's UN representative, said he had a mandate only to expand the government, not to discuss the president's fate.

Mr de Mistura tried to play down the entrenched positions and argued it was normal after five years of conflict, rather than a sign of failure.

Infrastructure

China-led bank approves funds for projects along new Silk Road

AIIB backs schemes in central Asia and Pakistan focused on transport links

TOM MITCHELL — BEIJING
JACK FARCHY — MOSCOW

China's flagship international development bank is hoping to pave a new Silk Road, with at least three of its initial projects focused on transport arteries in central Asia and Pakistan.

The Asian Infrastructure Investment Bank will help fund a highway in Pakistan, an expressway from Tajikistan's capital to the border with Uzbekistan, and a ring road in Almaty, Kazakhstan, according to people with knowledge of the projects and tender documents.

The AIIB was formally launched in January after attracting dozens of Asian and European member countries, many of them US allies that ignored Washington's concerns about the emergence of a Chinese rival to the World Bank and Asian Development Bank.

In an effort to counter the Obama administration's initial criticism, the AIIB has said it will enforce governance standards on a par with those at the World Bank and ADB. Last week Jin Liqun, AIIB president, and his World Bank counterpart signed a framework agreement to work together on co-finance projects. The AIIB expects to approve about $1.2bn in financing this year, including about a dozen projects with the World Bank that have not yet been announced.

The AIIB will also co-finance projects with the Washington and Tokyo-led ADB, the European Bank for Reconstruction and Development and the UK Department for International Development. Japan was the only major US ally to refuse Beijing's invitation to join the AIIB.

In Pakistan, the AIIB will join the ADB and Department for International Development to fund a 64km stretch of road connecting Shorkot to Khanewal, according to a tender document.

The ADB-led project's terms were recently revised to allow the AIIB to participate. Under its guidelines, the AIIB can only fund projects open to companies from all countries, while the ADB restricts participation to bidders from its member nations.

But the ADB will not cede its lead role. "ADB is the lead financing partner for the project and administers it on behalf of the other co-financiers," the tender document said. "Bidding shall be carried out in accordance with ADB's procurement guidelines and procedures."

> 'The benefit for AIIB is establishing a project portfolio that will help them get a better rating'

In Tajikistan, the AIIB will join the ADB and EBRD to help fund a road between the country's capital, Dushanbe, and Tursunzoda on the Uzbekistan border. The third transport link that the AIIB is expected to help fund is the Bakad Ring Road, a joint World Bank-EBRD project in Kazakhstan's commercial capital, Almaty.

All three projects will receive preliminary approval from the AIIB's investment committee before the end of this month, according to two people familiar with the process, followed by a formal go-ahead from the bank's board in June. The AIIB declined to comment.

By focusing on projects led by other international development banks, the AIIB can build up an investment portfolio more quickly than if it acted alone. Meanwhile, the World Bank, ADB and other development banks can tap into the AIIB's $100bn in capital, while saving their money for additional projects.

"The World Bank projects they are looking at are ones where AIIB can make a difference by helping with additional financing and increasing their scale," said a person familiar with the two banks' discussions. "The benefit for AIIB is having something to show and establishing a project portfolio that will help them get a better credit rating."

Editorial Comment page 10

Canberra conundrum

Mustering cattle at Anna Creek station, one of Kidman's holdings in the South Australian outback — Chris McLennan/Alamy

Chinese consortium strikes Australia land deal

JAMIE SMYTH — SYDNEY

A Chinese-led consortium has agreed to buy a historic Australian company that owns more than 1 per cent of the country's landmass just months after Canberra blocked a similar deal led by the same prospective purchaser.

Shanghai Pengxin Group has brought in Australian investors since the previous deal was blocked, but S Kidman & Co's decision to sell most of its holdings to the consortium creates a political problem for Scott Morrison, Australia's treasurer, who last week tried to delay approving Kidman's sale beyond a general election on July 2.

Under the proposed sale a company controlled by Shanghai Pengxin would acquire an 80 per cent stake in Kidman with 20 per cent purchased by Australian Rural Capital, a company listed on the Australian Stock Exchange.

"The consortium and Kidman have complied with all requests that have been made by the Foreign Investment Review Board and we believe the sale will secure the long-term future of the Kidman enterprise," said John Crosby, Kidman chairman.

A wave of Chinese investment into foreign housing, agriculture and public infrastructure assets is generating public concerns in many developed economies, including Australia. While Canberra states it continues to welcome foreign investment, it has progressively tightened the rules.

Family-owned Kidman, founded in 1899 by Sidney Kidman, controls pastoral leases of more than 100,000 sq km of outback and owns roughly 185,000 cattle. In November, its proposed sale to foreign investors, including a consortium controlled by Shanghai Pengxin, prompted Mr Morrison to intervene and declare he would block any deal.

Mr Morrison cited advice from FIRB, which raised concerns about the proximity of a missile-testing range to Anna Creek, one of Kidman's pastoral stations. To meet regulators' concerns, Kidman has agreed to a separate sale of Anna Creek station, which controls roughly 24,000 sq km of land, to Australian company Williams Cattle Co, as long as the Chinese consortium deal is approved.

80%	A$46.3m
Company run by Shanghai Pengxin would acquire this stake in Kidman	Amount the consortium is pledging to invest in Kidman

The Chinese consortium is led by Shanghai Pengxin, founded by Chinese billionaire Jiang Zhaobai, and owns real estate, agricultural and chemicals assets. Shanghai CRED Real Estate Stock Co, founded by property developer Gui Goujie, is the other major backer. The consortium is pledging to invest A$46.3m ($36m) in capital improvements and restocking in Kidman in the first year after a sale, and to create 50 jobs.

Over recent weeks shareholders in Kidman and the Chinese-led consortium have become frustrated at the long review into a sale process, which first began in April 2015. This prompted them to refuse a request from FIRB for a further delay in its decision-making.

But in an apparent effort to head off political sensitivities over foreign ownership of such a high-profile Australian company, Mr Morrison has signed an order extending the decision review period to mid-July.

This means a final decision on the proposed sale will come after a proposed general election on July 2.

"The government will not be making a hasty decision on this very significant matter," said the treasury yesterday.

Lex page 14

Japan

Abe poses threat to press freedom, says UN official

ROBIN HARDING — TOKYO

Press freedom in Japan is under serious threat from Prime Minister Shinzo Abe and his government, according to a scathing report by a UN official.

After a week-long fact-finding mission, David Kaye, special rapporteur on freedom of expression, pointed to "really worrying" trends on media independence in Japan and urged reform of the country's broadcasting law.

Mr Kaye's comments are the first official recognition of fears that Mr Abe is systematically weakening freedom of the press in Asia's richest democracy and seeking to silence critical voices.

"A significant number of journalists I met feel intense pressure from the government, abetted by management, to conform their reporting to official policy preferences," Mr Kaye told a press conference. "Many claimed to have been sidelined or silenced after indirect pressure from leading politicians."

Mr Kaye came to Japan after his original visit, scheduled for last December, was cancelled when the government said it could not arrange meetings.

While a UN special rapporteur has no formal powers, finding itself singled out for criticism is highly embarrassing for Japan's government. Mr Kaye, a law professor at the University of California, Irvine, will present a full report to the UN's Human Rights Council next year.

Concerns about press freedom in Japan have been growing after Mr Abe appointed Katsuto Momii, an ally, two years ago as chairman of public broadcaster NHK, communications minister Sanae Takaichi said she could shut down "politically biased" broadcasters, and journalists known for asking tough questions left their television jobs.

Mr Kaye took Ms Takaichi to task, saying her view was not dictated by the law itself, and that her comments had reasonably been perceived as a threat to restrict the media. He called for the government to "get itself out of the media-regulation business" by repealing the clause that allows it to determine what is fair and what is biased.

However, Mr Kaye also criticised the country's media, saying it would easily be able to resist government influence if it stuck together, preserved its independence and practised self-regulation.

Among Mr Kaye's other targets for criticism were Japan's kisha clubs — closed groups of reporters that sit inside every government ministry, gaining privileged access to officials and information but self-censoring their reporting in return. "I think the kisha club system should be abolished. They're a tool to restrict access — they foster a kind of access journalism and undermine investigative journalism. I think they're a hindrance to media freedom in Japan."

David Kaye, a UN special rapporteur, says many journalists claim to have been silenced by top politicians

Mr Kaye said he had heard first-hand reports of newspapers delaying or cancelling the publication of articles and demoting or transferring reporters who wrote articles critical of the government. He did not confirm allegations of government pressure forcing out some broadcasters but said the cluster of departures was "surprising in an industry in which employees stay with companies for decades".

Mr Kaye criticised Japan's new official secrets act as going "further than necessary in protecting information from disclosure", and said a body that approved school textbooks should be insulated from political interference.

Energy technology

'Clean coal' hailed as saviour for jobs in US and Beijing

LUCY HORNBY — BEIJING

Developing "clean coal" technology would help the coal sector in the US and China and prevent further job losses, according to US energy secretary Ernest Moniz.

Crashing prices for coal amid China's economic slowdown and US investors' preference for newer, less polluting energy technology has hit the industry hard in both countries.

Last week US coal group Peabody filed for bankruptcy under the weight of about $6bn in debt. Meanwhile, Beijing's bid to shut down capacity and cut jobs in the sector last month prompted mass protests in China by coal workers from at least two big state-owned mines.

Clean coal is the holy grail for those who accept the world's dependence on the energy source but want to curb emissions of carbon and other greenhouse gases that scientists say contribute to damaging global warming.

"The idea of having a continued opportunity for coal use in a highly carbon-constrained world is something that's attractive for carbon reasons. It's also attractive in addressing the coal country, the dislocations that otherwise would become even greater," Mr Moniz said in an interview in Beijing before the Peabody announcement.

China and the US, the world's two biggest polluters, have reached a series of deals to curb emissions and build domestic political support for lower-carbon industrial policies to help meet commitments made late last year in Paris. Mr Moniz said the two countries' reliance on coal required the development of coal technologies that emitted less carbon.

Clean coal is contentious among environmentalists. Some see it as the only way to reduce emissions while maintaining or increasing the energy supply available to the world's 7bn people. Others believe it diverts funds from more promising technologies while so far failing to deliver on emissions reductions.

The US is promoting pilot projects in China, including carbon capture and storage. Chinese construction companies have been involved in planning coal-based projects in the US, including the energy department-backed Texas Clean Energy plant, although many of those projects have stalled.

"For a carbon-constrained world, we feel we must develop the enabling technologies for all sources, including coal. The marketplace will then decide," Mr Moniz said.

China consumes about 4bn tonnes of coal a year for power generation and direct burning by industry, accounting for over 60 per cent of its energy mix. The US burns about 900m tonnes a year, more than 90 per cent of which is used for power generation.

Up to 5m of China's 12m jobs in the state-owned coal and steel sectors could be lost amid government-mandated restructuring, according to some estimates, although Beijing has officially given a lower figure of 1.8m.

In the US, coal mines directly employed about 75,000 people in 2014.

Afghanistan

Suicide bomber kills 28 in Kabul car blast at start of Taliban 'spring offensive'

AMY KAZMIN — NEW DELHI

A powerful car bomb in the centre of the Afghan capital, Kabul, killed 28 people and injured hundreds more yesterday, just days after Taliban rebels formally announced the start of a "spring offensive".

Officials said the bomb, detonated by a suicide bomber close to a government security agency charged with protecting the country's VIPs, exploded at the peak of the morning rush hour.

Afghanistan's presidential palace is just a few hundred metres away from the site of the explosion, which occurred in a crowded area where homes, mosques, schools and businesses are packed among government offices.

Gunmen were reported to have stormed into the area during the attack, with security forces battling them before clearing the area.

The Taliban, which last week warned it planned to bring more territory under its control and renew its offensive against the government of President Ashraf Ghani, has claimed responsibility for the attack.

"Clearly the networks the Taliban have established in Kabul have not been completely eliminated," said Ahmed Rashid, author of several books on Afghanistan, Pakistan and central Asia.

In a tweet, Mr Ghani said the attack "clearly shows the enemy's defeat in face-to-face battle" with the Afghan security forces. But the devastating explosion comes at a time of rising anxiety for Afghanistan, Mr Ghani's administration and the national security forces, as well as the international coalition forces now gradually reducing their presence in the country.

In September, Taliban fighters briefly captured the town of Kunduz and two months later almost conquered the strategically significant town of Sangin in Helmand province. While Afghan security forces — backed by Nato reinforcements and air support — managed to push the rebels back in both instances, the areas are again under threat.

A man in Kabul learns his relative has been killed in the bomb blast

"There has been heavy fighting in Kunduz in the last few days, there has been heavy fighting in Helmand province in the south and there is a danger that either one of these places could fall to the Taliban," said Mr Rashid.

Planned peace talks between Mr Ghani's government and the rebels have stalled, with Islamabad unable to persuade the Taliban's leaders, many of whom are believed to be in Pakistan, to come to the negotiating table. "Pakistan has promised that they would deliver the Taliban for talks but they have failed to do so," said Mr Rashid.

"The Taliban went on to announce the spring offensive in total defiance of what Pakistan had promised they would do."

In a statement announcing their spring offensive, the Taliban rebels vowed to "employ all means at our disposal to bog the enemy down in a war of attrition".

Meanwhile, Mr Ghani's fragile unity government is fighting dissent among coalition members and externally, with Hamid Karzai, the former president, behind growing calls for a traditional *loya jirga*, or tribal council, to choose a new leader.

Nato members are due to meet in July in Warsaw to discuss their future plans and presence in Afghanistan.

FT BIG READ. CHILE

Turning copper into wine

As Beijing's crackdown on lavish gift-giving hits expensive wines, Chilean exporters are taking aim at China's casual drinkers. Can the grape wean Santiago from its dependence on bulk commodities?

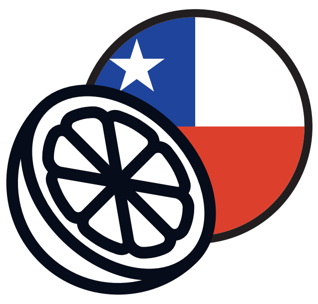
By Lucy Hornby

The bottles of Great Wall, Changyu and Dragon Seal wine line up like sentries on the shelf behind Cristián López as he sits in his office in Santiago's gleaming business district. For Mr López, in charge of Asian sales for Chilean group Viña Concha y Toro, these are a daily reminder of the fast-changing fashions of Chinese cities half a world away. "Chile and China both start with 'C- h-' but they could not be farther away," he says.

China is the world's largest market for red wine, which should be enough to put it on the radar of any winemaker. But as the business seeks to recover from the Chinese government's crackdown on corruption and lavish gift-giving, consumers are turning away from expensive French labels to "new world" exporters like Chile, the fifth-largest wine-producing nation and second-largest supplier to China.

For Chile, this is more than a sales opportunity: the hope is that the wine business can wean the country off its dependence on bulk exports like copper and agricultural commodities.

Wine appreciation is growing among prosperous Chinese. In Shanghai or Beijing, professionals meet at wine bars. Well-off couples give a bottle as a gift. At



$5bn
Value of Chile's annual fruit exports

holiday times, families propose toasts with red wine instead of the fiery, high-alcohol *baijiu* favoured by older men.

Ten years ago, Chinese who liked the cachet but not the taste of wine mixed it with Sprite to make it go down better. Supermarkets would plastic-wrap two bottles of wine to a can of Coca-Cola as a sales promotion. A Chinese dairy executive once proudly poured yoghurt into French wine, to demonstrate the versatility of his product.

All that is in the past. Ecommerce is the fastest-growing channel for wine sales in China and specialist clubs are springing up. In 2013, Mr López moved to Shanghai, intending to stay for six months. He ended up living for two years in a country he calls "crazy, like a movie on fast-forward".

Around the globe, wines from Chile, South Africa, Australia and the US have eroded the market for their French counterparts. Diners in London and New York now choose a bottle based on

> 'China bought huge volumes of bulk wine and expensive bottles. Most was for corruption. The industry has to start again'

the type of grape rather than their knowledge of French geography.

China was an exception to this until recently. Confused about which wine to buy, newly rich Chinese would simply buy the most expensive French labels. "People are becoming more sophisticated in terms of thinking which countries the wine is coming from rather than just choosing France," says James Roy, analyst at the China Market Research Group in Shanghai.

Mr López sees an opening for Chile. He wants to convince the 36m Chinese who purchase at least one bottle a month that wine need not be expensive to be good value.

He has an unlikely ally in the Chinese Communist party, which is in its third year of an unrelenting anti-corruption drive. Wine sales have suffered, particularly French wine, which government importers and state-owned firms bought in lavish, bribery-fuelled binges.

Wine consultant Guy Hooper recalls extravagant dinners even in provincial cities, far from Beijing. "Everyone was very glamorous and we were like the celebrities. There were models on catwalks, signed bottles as gifts, and then a businessman buys 60 or 80 cases."

Those in the marketing business who thought one such sale meant they had mastered China are having to think again. Many failed to check on basics, such as whether their Chinese agents owned refrigerated warehouses or genuine distribution networks. "Wine spoil destroys brand," Mr Hooper says.

So do the inflated prices that some in marketing thought would give their labels extra cachet. Ecommerce allows for instant price comparisons. "It has exposed brands that don't have a solid pricing strategy," says Mr López. "If pricing is all over the place it affects your brand in every way possible. If you aspire to build a brand, the challenge is different than if you just want to sell wine into China. A lot of discipline is involved."

Ready to go: wine casks at the Cono Sur vineyards 200km south of Santiago — Martin Bernetti/AFP/Getty

$2bn
Value of annual wine exports

Bulk commodity

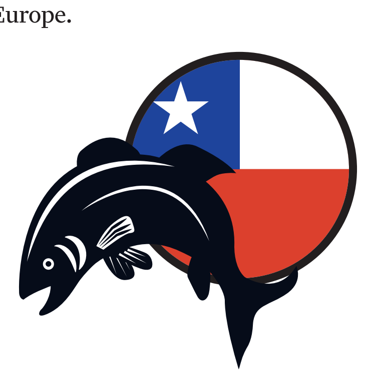
Leaving Santiago on the motorway, dusty residential neighbourhoods quickly give way to flat green vineyards and billboards advertising fungicides. This is the Maipo valley, the heart of Chile's wine country.

In the town of Isla de Maipo, a road crew with a single backhoe has created a traffic jam. Just past the construction lies the De Martino vineyard, where export manager Francisco Venegas displays a framed photograph of a ceremony, 10 years ago, to mark the day a free-trade agreement between China and Chile came into effect.

Following that deal, copper exports quickly turned China into Chile's largest trading partner. Wine exports also surged, doubling within eight years. But most Chinese who drank Chilean wine were no more aware of where it came from than they were of the origin of the copper in their mobile phones.

That is because most of the Chilean product sold to China is "bulk wine", a commodity, like copper.

Chile's sunny, dry days and cool evenings create far more grape juice than the market for Chilean bottled wine can support. The excess is pumped into plastic bladders big enough to fit inside a shipping container and sent to China or Europe.



$3.5bn
Diversification has sparked growth in sales of salmon

Winemakers with bulk sales keep them separate from their bottled brands, with good reason. A customer selecting a single bottle from the wooden shelves of a wine shop does not want to think about 24,000 litres of the stuff sloshing across the oceans.

A lot of bulk wine goes to pad out production for other countries' labels. In China, no laws require the disclosure of the origin of wine inside a bottle. Mixing in better quality Chilean bulk wine has salvaged many a Chinese brand, but marketers are discreet about such details.

Mr Venegas is unusual because he is willing to discuss De Martino's three product lines: bottled wines, bulk sales and grape juice sales. He is equally proud that Marcelo Retamal, De Martino's winemaker, was recently named the 13th most influential in the world.

While Viña Concha y Toro is mapping the precise habits of China's cosmopolitan drinkers, Mr Venegas sees Chinese wine sales from the point of view of his customers, the owners of Chinese labels like the ones whose bottles lined Mr López's shelf. The picture is not pretty.

"The main concern for some years has been corruption. The industry suffered a lot. China bought huge volumes of bulk wine and very expensive bottled wines — most of that consumption was for corruption, for people related to the government. Big parties, very expensive gifts," he says. "The whole industry has had to adjust and start again."

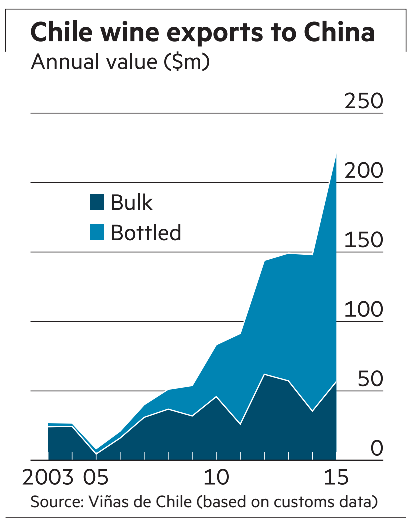
As China's purge took effect, one niche market that suffered was counterfeit wines. At the peak of the country's boom, Chinese consumption of French wine outpaced the production of top French châteaux. A clue to that arithmetical impossibility lies in the $500 paid for empty bottles of Château Lafite in Beijing. Chilean bulk wine may have filled them but no one is willing to say.

Bottled wines account for three-quarters of Chile's wine sales to China by value, but only one-third by volume. The bulk trade could suffer if Beijing ever adopts labelling rules to make clear where wine comes from.

"In my latest trip I found customers becoming aware there were other importers and their wineries are really cheating," Mr Venegas says. "They are losing confidence in their own imports. They are noticing that when the Chinese label says it is a French wine, or a local brand, most of it is just blends of the cheap stuff.

"Now they are in a different stage of development. They see themselves as a strong country and empowered. They have the money and they want to buy the good stuff."

Chinese wine producers led by Cofco, the state-owned food and beverage conglomerate, and privately held Changyu, are responding to Chinese consumers' desire for authenticity by investing in Chile directly, Mr Venegas says. "The most important thing is that the label says 'Chile'."



Building Brand Chile

Bottled wine is Chile's answer to its century-old dilemma — what to do with too much of a good thing? In the 19th century it was nitrate, used in fertiliser and explosives. Chileans feel the boom created little lasting wealth. In the 20th century mining put the country on the map as the world's largest copper producer.

"In Latin America there's an embedded idea of the curse of natural resources," says economist Patricio Meller, head of the state-backed think-tank Fundación Chile.

Santiago's solution has been to diversify exports. Fundación Chile incubated a salmon industry, then fruit, and is working on shellfish. The development of bulk wine exports means Chile produces twice as much as it did in the 1980s, even though local wine consumption is only one-third what it was then.

China's boom presented a mixed blessing for the copper producer. The economy grew at the fastest pace in

$40bn
Annual copper exports dwarf all others

Latin America but tilted dangerously towards a single product. Chilean wine and seafood sales to China quadrupled after the trade deal but were dwarfed by copper. Chile's wine exports are worth $2bn per year, fruit $5bn and salmon $3.5bn. Copper takes the main share, at $40bn.

Taxi drivers in Santiago rattle off copper prices the way Shanghai cabbies point out the price per square metre of each housing block. Copper accounts for 55 per cent of Chile's exports and almost 15 per cent of government revenues.

Jorge Heine, Chile's ambassador in Beijing, was bemused when journalists in Santiago started calling him ahead of China's quarterly announcement on gross domestic product last week. "This is not the stuff that normally makes headlines in Chile!" he noted. It is now. China's slowdown has ended the commodities supercycle. The value of the peso has plummeted and an increasingly unpopular government is trimming budgets.

Amid the mining downturn, those involved in wine marketing do not pretend that it can replace copper. They do, however, see their efforts to build a name for Chilean wine as a way to create a brand for the country itself. This could translate into more tourism, the seeds of a service industry and the beginning of a path away from being an exporter of bulk commodities.

"Wines are Chile's product. It's the flag. All those other products, copper, whatever, there's no designation of origin. Wine is the product that gets in front of the consumer," says Mr Hooper.

"Wine is our ambassador."

A tale of two critics

How wine consuming became a business

If wine sales are still a developing business in China, the practice of wine criticism is in its infancy.

"Normal people listen to their friends. They don't really understand the vocabulary of wine criticism," says Li Demei, wine consultant and a professor at Beijing Agriculture University.

That has been a challenge for Hans Qu, China's first sommelier. A chance promotion from hotel bartender to wine steward 12 years ago "changed my life", he says. "I liked everything . . . I felt really excited [that] I was going to do this for the rest of my life."

But the people taking Mr Qu's courses on wine appreciation are more likely to be sales representatives trying to get their tongues around strange foreign terms than wine consumers. "I don't feel consumers like advice from sommeliers or experts. My feeling is still that they look at the budget. Advice plays only a small part in their consideration."

Several years ago Mr Qu (right) felt angered at wine importers who made astronomical margins on Chinese buyers' eagerness to spend. Now, he is more worried about imported wines being sold cheaply.

"Imagine a Spanish wine for Rmb9.90 ($1.50) a bottle, or Rmb19.90 or Rmb29.90. I wouldn't drink that," he says, "I don't know what's inside."

A similar sense of indignation inspired Jim Boyce, Chinese wine's greatest cheerleader. His Grape Wall of China blog promotes the best of the country's wines.

Foreign journalists arriving in China before the 2008 Olympics provoked his ire. "A lot of people started talking about fake wine, or mixing Coke with Lafitte, and I thought, that's not what I am seeing. There was all this negative press.

"Now it's almost gone the other way. There are too many overly optimistic expectations."

Speed read

Chinese demand Chile hopes it can use wine sales to help wean the country off its dependence on commodity exports

Bribery-fuelled binges Wine sales in China have suffered as a result of Beijing's anti-corruption crackdown

Production up Chile produces twice as much wine as it did in the 1980s even as local consumption has fallen

FINANCIAL TIMES
'Without fear and without favour'

WEDNESDAY 20 APRIL 2016

Google and the art of monopoly maintenance

Brussels is right to draw parallels with the celebrated Microsoft case

European antitrust cases against Google seem to be like London buses. You wait ages for one to arrive and then they all come along at once.

When Margrethe Vestager took over as antitrust chief at the European Commission at the end of 2014, Brussels had spent the previous five years locked in unavailing negotiations with the US search group over a series of competition disputes. It took her just a few months to open the first formal case: into whether Google abuses its 90 per cent share of search traffic to squeeze out rivals unfairly.

Now Ms Vestager is poised to widen the attack. She is expected to launch a second case, possibly as early as today, this time looking at Google's mobile platform, Android. It will examine whether Google leverages its high market share in mobile operating software to push its apps on to customers whether they want them or not.

Ms Vestager's concerns are understandable. Google has come under fire from rivals for taking advantage of customers' desire for pre-installed apps ready for use as soon as the smartphone is taken out of the box. Its tactics include ensuring a suite of its own apps installed on each phone, and excluding those it does not wish to distribute.

In a speech this week, Ms Vestager drew an explicit parallel between Android and the commission's marathon case against Microsoft. It is an apt comparison. Just as the software group threw in free internet browsers and media players with its PC operating software, Google freely distributes Android software to phonemakers and mobile operators. This is then exchanged for the contractual right to install its apps on their phones.

Google can argue that it gives space on its system for rival products such as Amazon and Facebook, and that it provides a valuable free service to millions of users around the world. There is however another parallel with Microsoft, namely the dominant position Google enjoys in mobile operating systems, which makes its self-promoting tactics questionable. Apple might have a stronghold at the top end of the market but Android supplies its software platform to more than 80 per cent of smartphones.

This latest shot in the battle between Google and the commission is likely to stoke suspicions in the US that Europe and its institutions are anti-American and anti-Silicon Valley. While Americans may have legitimate complaints about issues such as "safe harbour", the questions raised over Google are much more valid.

A great deal rests on the commission's investigation. The internet group is promoting its products to consumers in order to deepen its already dominant control of online search: a process known in the US as "monopoly maintenance".

Given the digital world's propensity to create winner-takes-all positions, and the feedback loop that "big data" provides in sharpening search results, this could leave Google with a vice-like grip on digital services. It is better for Google that these questions are decided in the open. Before Ms Vestager's arrival, the commission's probe into the company was plagued by suggestions of political interference and lobbying by French and German media companies. Due process will allow the US tech group to make its case.

Ms Vestager is right to pick this second fight with Google. Ducking another bruising battle with the internet giant might seem the less stressful course but anything short of a robust approach would only weaken innovation. In the long run, that could leave consumers with a worse service than would otherwise be the case.

Mission creep must stop at the World Bank

Crisis lending should be the job of the International Monetary Fund

Another emerging market commodity exporter deep in fiscal trouble; another chance for the World Bank to try to prove its relevance.

Papua New Guinea is the latest exporter of oil and gas which, hit by the falling global price of hydrocarbons in recent years, has found itself short of foreign exchange and obliged to turn to international official lenders. As was the case with Nigeria, it is currently trying for a loan from the World Bank rather than accepting the advice of the acknowledged crisis lender, the International Monetary Fund.

It is easy to see why this benefits both Papua New Guinea and the bank. The Oceanian nation gets dollars without the stigma of borrowing from the IMF, and the bank occupies itself at a time that its core mission of development finance has been substantially eroded.

Nonetheless, it is not a sensible move. Pretending that what is at heart a macroeconomic foreign exchange problem can be resolved through microeconomic intervention will not help Papua New Guinea make the adjustment that it needs. It will merely draw the World Bank further into problems it is not designed to resolve.

The justification for calling in the bank to help is that the country's commercial banks are short of dollars to help their clients clear foreign exchange transactions and thus conduct international trade. But the root of the dollar shortage is not the kind of microeconomic structural issue in the banking sector in which the World Bank has undoubted expertise.

Far more important is an exchange rate overvalued after sustained intervention by the central bank, together with a collapse in dollar earnings because of sliding global oil and gas prices, which have driven official foreign exchange reserves to dangerously low levels. As the IMF has been urging for years, Papua New Guinea needs to move towards a flexible currency and shore up its long-term fiscal position.

This is unlikely to be a short-term problem. There is a fundamental need to adjust public finances and restore external competitiveness. Papua New Guinea should not simply take loans from the World Bank to bail out its banks from the short-term consequences of the authorities' own actions.

This is not the first time that the bank has wandered towards or over the edge of its remit. Nigeria, which faces similar problems with collapsing oil earnings and downward pressure on the currency, has also asked the World Bank for a loan that is fairly clearly meant to bail it out of a straight-up fiscal balance problem, not to improve its productive capacity.

It is understandable that the bank is seeking new ways to push money out of the door to clients. Its role in providing development finance country-by-country has increasingly been usurped by China's bilateral lending and by regional development banks, including the new Asian Infrastructure Investment Bank.

But rather than contorting its lending to keep its existing model alive, the bank should switch much more of its energy towards plugging the real holes in development, the provision of "global public goods" — technology and know-how in areas such as health, energy and the environment.

The trend of countries with macroeconomic adjustment problems making a path to the World Bank's door needs to be halted. The proper agency for crisis lending is across the road at the IMF. Papua New Guinea needs to admit it has a bigger issue than temporary difficulties in commercial banks, and the World Bank needs to find more fruitful things to do now that its traditional role is in long-term decline.

Letters

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Corrections: corrections@ft.com

Public sector must be clear on cost of capital

Sir, "The public sector needs to be better at accounting for its assets," Martin Wolf argues persuasively (April 15). The public sector also needs to be clear about its cost of capital. The public sector can borrow at lower rates than the private sector. Hence Mr Wolf states that it makes little sense to advocate private infrastructure finance. As John Kay put it in 1993, this view is "naive". Default risk for government paper is low because taxpayers come to the rescue when projects fail. Taxpayers de facto provide unremunerated credit insurance. They bear a risk and that is a cost to them and thus society at large.

When governments care about overall benefits and costs to society they need to assess the cost of risk-bearing of taxpayers. There is a school in economics going back to an article by Arrow and Lind in 1970, which argues that governments can perfectly diversify risk by spreading it over many taxpayers and thus reduce the cost of risk-bearing to zero.

A closer look suggests that this is misguided. For example, Arrow and Lind assume that project outcomes are uncorrelated with economic development overall. Yet, the outcome of the average project must be correlated with economic development. After all the economy is the sum of all projects.

Christian Gollier, head of the Toulouse School of Economics, makes the arguments clearly. He chaired a commission advising the government of France on how to treat risk in public projects in *"Le calcul du risque dans les investissements publics"* (2011). There is no reason to believe that the cost of capital of the public sector is systematically lower than that of the private sector. The ostensibly low cost of capital may tempt governments to disguise risks even more subtly than off-balance sheet borrowing under the private finance initiative. Just think how nuclear plant investment would fare when evaluated using a cost of capital similar to that of the private sector.

Michael Klein
Washington, DC, US

Leaving the EU is simply not worth the risk

Sir, We are the founders and CEOs of some of the UK's most entrepreneurial businesses — from early stage start-ups to household names.

Every day, as we build our companies, we see the benefits of being able to do business within Europe's single market of 500m consumers, with one set of regulations across 28 countries, and the ability to recruit the brightest people here and across Europe.

Once the latest round of British-backed EU reforms have been completed, the European market for services, as well as digital products, will create even greater business opportunities for our companies.

Of course the EU isn't perfect; but rather than cutting ourselves off from the opportunities it offers, it is better to be on the inside helping shape the rules of this market instead of just being subject to them.

The economic shock of a vote to leave the EU would also be hugely damaging to our businesses. Leaving could lead to lost investment, missed opportunities and lost jobs.

The UK is currently the best place in Europe to launch and grow a business; leaving the EU will undoubtedly undermine the ability of Britain's entrepreneurs to start-up, innovate, and grow. It is simply not worth the risk.

Alex Asseily
Founder, Jawbone, State and Chiaro
Alex Chesterman
Founder and CEO, Zoopla Property Group
William Shu
Founder and CEO, Deliveroo
Lloyd Dorfman
Founder, Travelex; Chairman, The Office Group and Doddle
Martha Lane Fox
Founder, doteveryone; Co-Founder, Lucky Voice and lastminute.com
Niklas Zennström
CEO and Founding Partner, Atomico; founder, Skype
Peter Williams
Founder and CEO, Jack Wills
Rumi Verjee
Founder, Domino's Pizza UK
Saul Klein
Co-Founder, LoveFilm
Simon Woodroffe
Founder, YO! Sushi and YOTEL
Arnaud Massenet
Founder and Director, Net-a-Porter Group; CEO and Director, de-pury Group
Dinesh Dhamija
President, TIE; Founder, ebookers.com
For the complete list of 211 signatories go to www.ft.com/letters

Press freedom is not a vehicle to insult people

Sir, I wonder if Gideon Rachman has indeed any idea about the words of the poem attacking Turkish president Recep Tayyip Erdogan ("Merkel must guard freedom of the press", April 19). Press freedom has nothing to do with a pure insult to a country's elected president. The democratic west is not built on insulting people and nations. Contrary to Mr Rachman's argument, the pursuing of the case by prosecutors will strengthen western democracy, not tarnish it. The democratic west should learn to find other, more respectful and constructive ways of satire and criticism. Insulting people and nations is not the right way.

Dr Saruhan Ozel
Istanbul, Turkey

Egypt accepted Saudi sovereignty of islands

Sir, Your report "Sisi blames social media users . . ." (FT.com, April 13) states that the "Egyptians had long considered" the islands of Tiran and Sanafir "part of their territory". No one disputes that the islands have been under the Egyptian government's management since 1950 at the invitation of the Saudi government. But this did not involve a transfer of sovereignty, which the Egyptian government has always accepted.

In a UN Security Council meeting in 1967, the Egyptian ambassador made a statement declaring that "Egypt has never asserted sovereignty over the Islands, and its presence was merely to administer them". Further, the Egyptian government has declassified a 1990 document of advice from the Egyptian Ministry of Foreign Affairs to the then Egyptian Prime Minister Dr Atif Sidki which concludes that Egyptian management of the Islands "does not affect the continuation of Saudi sovereignty over them". This is why, as you quote, Mr Sisi said: "I did not give up any of our rights."

Dr Saud Al-Ammari
Blakes Law Firm,
Al-Khobar, Saudi Arabia

Greeks can only dream of such a parallel universe

Sir, By mistake, on Friday April 15 I must have received the FT's copy from a parallel universe, where there is another Greece with, by coincidence, a prime minister also called Alexis Tsipras, laying the foundations of a sustainable and inclusive recovery ("Greece has defied the doom-mongers — now the IMF must do its bit"). Unfortunately, here in our version of Greece, we can only dream of such an outcome.

Despite six years of crisis, there are still no structural reforms of any sort that would free Greek entrepreneurial spirit from the clutch of the all-consuming state, or encourage foreign investment. Closed professions remain hermetically so, time-wasting, senseless bureaucracy holds firm, the justice system doesn't work, and any form of meritocratic evaluation of staff in the large and inefficient public sector is resisted tooth-and-nail. Instead, the current government is extending the well-rehearsed practice of inundating key public sector posts with cronies and is seeking to meddle more than ever in culture, private education (what there is of it, since private universities are banned) and the media.

In our country, the progressive new tax system has an effective top tax rate of 75-80 per cent (including social security contributions), which means that there will be no new wealth created to redistribute. The brave pension reforms involve tinkering at the edges of a system in which 1.7 workers pay-as-they-go for one pensioner, which is structurally unsustainable. The three-times recapitalised banking system cannot begin to provide liquidity until the huge overhang of nonperforming loans is commercially addressed. And meanwhile social fairness is achieved by the excellent being forced to emigrate.

Markos Komondouros
Athens, Greece

'I've never seen anything like it — but then my eyes aren't what they used to be'

The very companies that should be staying

Sir, As a gay man, I read with dismay that companies are boycotting North Carolina.

A gay person in North Carolina, which has just passed a law permitting companies to discriminate against them, wants a job with an organisation that won't discriminate; but these are the very organisations pulling out.

Those organisations are inconsistent: some still have operations in countries with more repressive anti-gay laws: for example Singapore, or worse, Saudi Arabia.

James Thomas
London SW12, UK

Strong measures to offset the rich parent effect

Sir, You report (April 13) a striking finding that earnings 10 years after graduation for students with rich parents are about 10 per cent higher than those with poor parents, even after taking account of the university attended and subject studied. This gap rises to 15-20 per cent for the highest 10 per cent of all earners and the highest earners are medics and economists. The authors of the study are aware that these higher earnings could be due to several unobserved causes such as higher ability of "rich graduates", more use by them of the "parental bank" (for private school fees and other handouts during and after university) and greater networking capabilities.

Undoubtedly, I personally benefited from networking in my (unplanned) economist job at the Treasury in the early 1970s, thanks to a kindly and sociable high ranking official who invited everyone (from chief economic adviser to secretaries) who had been involved in each Treasury macro-forecasting exercise to his house for a celebratory dinner party. It was here that I first observed the Oxbridge networking club and also discovered the correct order in which to use an array of dinner party silverware. These two simultaneous events probably resulted in an uplift to my future salary of around 20 per cent.

Now about 50 per cent of pupils go on to higher education rather than 6 per cent back in the 1960s, so strong measures may be needed to offset the rich parent effect on children's future earnings. I doubt that the government's advice on internships or relying on kindly employers will address this imbalance. With inheritance tax largely ineffective, then providing genuine equality of opportunity may require a progressive tax on lifetime gifts.

Prof Keith Cuthbertson
Cass Business School,
London EC1, UK

Correction

● The Brexit scenario shown in a front-page illustration yesterday indicating a 9.5 per cent reduction in GDP by 2030 if the UK opted for WTO membership only was the high end of the Treasury estimate. To be consistent with the other scenarios cited, it should have shown a 7.5 per cent reduction, the mid-range estimate.

Feminists in a tangle over Islamic fashion

Paris Notebook

by Anne-Sylvaine Chassany

When Laurence Rossignol, France's minister for women's rights, likened women willingly wearing the burka to African Americans backing slavery, she caused international controversy.

The row was amplified by her use of the word "*Nègres*" or "Negroes". She later apologised for the "language mistake" but she stands by her point, criticising brands such as Marks and Spencer and H&M that are designing Islamic fashion.

"These clothes highlight the imprisonment of women's bodies," the minister said last week. She described as "irresponsible" the labels offering burkinis — cover-all swimsuits — or hijabs. "Today there are some women promoting political Islam and there are some women who are suffering in the suburbs from the pressure [exerted by the former]."

French feminist groups have largely come out in defence of Ms Rossignol. "The image that came to your mind is slavery because that is what the veil symbolises through the invisibility of women's bodies in the public space," a dozen organisations wrote in an open letter. "Alas, the downtrodden are often accomplices." Among the signatories was Femmes sans Voile d'Aubervilliers, formed by women of north African descent in a poor suburb of northern Paris.

French historian Elisabeth Badinter, an influential feminist, has called for a boycott of the brands in question and says more coercive means should be considered. "Only the law can protect those who wear the veil under pressure," she told Le Monde newspaper. "But when we support those women, we are considered 'Islamophobic.'"

The western backlash against the veil in the past two decades has been fiercest in France. In 2004 it was banned in schools. Manuel Valls, the Socialist prime minister, and Nicolas Sarkozy, the centre-right former president, have recently suggested extending the ban to universities.

Feminism in France, shaped by Simone de Beauvoir's notion that tradition oppresses women, has been impregnated with republican secularity, or *laïcité*, explains Florence Rochefort of the Centre for National Scientific Research. As the notion of *laïcité* has taken on a more uncompromising and anticlerical hue, moving away from the spirit of the 1905 law that regulates the relationship between the state and religious institutions, so has French feminism. Because it is a religious symbol, she says, the veil is regarded by definition as suspicious.

"The veil is a challenge to a hard-fought French feminist norm, which can be summarised as 'I am a feminist and I am sexy','" Ms Rochefort explains. Today's feminists "are not interested in nuances. Is the veil experienced as a religious alienation? Not for all who wear it," Ms Rochefort says. "Studies show it's also a tool used by a minority that faces discrimination to create a sense of dignity or opposition. The best response may not be a ban."

Like many nonreligious French women my age, I knew where Ms Rossignol's reaction came from. I have the example of my mother in mind: she insisted on receiving a higher education and having a career when all her Corsican Catholic family required of her was to get married and raise children. The fact that she did not go to school before the age of eight and, unlike her older brother, was not allowed to learn a musical instrument still blows my mind.

But I recently had an experience that made me see how disconnected this legacy has become from the daily lives of a lot of Muslims whose parents or grandparents came to France after the feminist revolution of the 1960s.

I was talking to an unemployed 23-year-old from Bobigny, a Parisian suburb similar to Aubervilliers, about his experience, as the son of Haitian immigrants, of discrimination in the workplace. He praised the UK, where "policewomen can wear a veil if they want to". One woman, he said, had recently dared to wear one to work in the mall where she worked. Shoppers were so astonished that her employer allowed her to keep it on that they took selfies with her "because it was such progress".

I was taken aback. The veil has never looked like progress to me. But if it is perceived as such by some, then there may be something wrong with the approach being taken by France — and its feminists.

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Comment

Sophisticated states are failing, so politicians need to take risks

OPINION
Jan Techau

An illness is afflicting societies in both Europe and North America: sophisticated state failure. It fuels the Donald Trump and Marine Le Pen insurgencies and endangers the ability of advanced societies to secure a bright future for their citizens. Sophisticated state failure is a cancer eating away at societies in the west and undermining the liberal world order that, up to now, they have upheld.

Yet by and large, everything works as it should in the mature democracies of the developed world. Elections are fair and free. The courts work, and so do the tax authorities. The police can mostly be trusted, corruption is comparatively low and, overall, the institutions of public administration function as they should. In other words, none of the classic elements of state failure are present. Yet nothing gets done.

For roughly 30 years, since Margaret Thatcher performed drastic surgery on an ailing British economy, the western world has done piecemeal reform at best. Politicians have promised change, of course — reform of pensions, labour markets, the tax system and education. They have promised smaller states and less bureaucracy.

But with a few notable exceptions, little of this has ever materialised in any meaningful way. Much of it died before it could reach the statute books. That is the definition of sophisticated state failure: to have a functioning state in which nothing gets done. There are countless examples of this: the inability of successive French governments to reform their labour market; the wasted majorities of Silvio Berlusconi and Tony Blair, or the eurozone's inability to put the common currency on a solid footing.

There are many reasons for sophisticated state failure. The sheer difficulty of governing complex, highly diverse societies should not be underestimated,

> Political elites are disposed to protect the status quo, so opportunities for painless change are missed

but since lawmakers often do not (and cannot) know what they are doing, they decide instead to do very little.

The benefits of globalisation and the entry of China into the world economy, along with low interest rates, led to an unnaturally long period of growth during which politicians grew complacent and voters developed a strong sense of entitlement.

Voters are now more fickle, and so majorities are less stable, which leads politicians to avoid controversial issues and shun big risks. As Jean-Claude Juncker, the president of the European Commission, put it, politicians "know exactly what they need to do, but they don't know how to get re-elected".

As long as this dilemma remains unresolved, the result is paralysis. Over time, as disappointments have accumulated, growing numbers of voters have begun to voice their frustrations. Political elites, however, are disposed to protect the status quo, so opportunities for painless change are routinely missed. The result is the slow migration of discontent from the fringes to the centre.

Populism, whether of right or left, is not the answer to sophisticated state failure. While populists such as Mr Trump or Ms Le Pen are often good at pointing out when things are broken, they are almost invariably wrong on how to fix them.

The only lasting way out of sophisticated state failure is for responsible politicians to worry less about getting re-elected and to start risking their political careers for things that need to be done — just as Thatcher did in the 1980s and as Gerhard Schröder did with labour market reform in Germany in the mid-2000s.

If mainstream politicians do not start taking these risks, less savoury figures will take their place. Institutions will suffer lasting damage and the worst political instincts, ones that have previously lurked beneath the surface, will be unleashed. And with that, sophisticated state failure will eventually turn into real state failure.

The writer is director of Carnegie Europe

Britain's friends are right to fear Brexit

ECONOMICS
Martin Wolf

How might future historians judge a British to decision to leave the EU in the referendum on June 23? It might well be seen as the moment when the west started to unravel. That is why Barack Obama, US president, is not merely entitled to present his views on "Brexit". As leader of the west, he must do so.

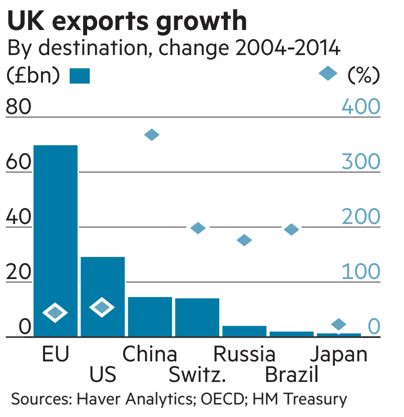
The choice the UK faces in June is whether to exercise its option to leave the EU now. So long as it is a member, it will always have this option. But it will not be granted the choice to rejoin after it has left. The moment to exercise a perpetual option is when its value is not just high, but unlikely to become much higher. The UK should vote to leave if, and only if, it is sure it will be better off than if it postponed the choice. That is not the case now. It might never be.

Indeed, those in favour of remaining, like me, would argue that, far from bringing gains, exercising the option to depart would deliver immediate losses. This, proponents of Brexit complain, is "project fear". That objection is absurd. Avoiding needless and costly risks is how adults differ from children.

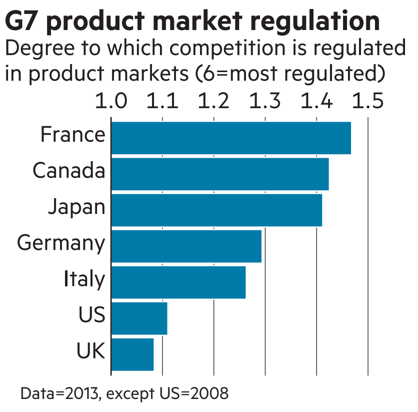
Possible economic costs of leaving are laid out in the Treasury's excellent analysis, published this week. It argues that the UK would be significantly worse off under any of the three most plausible alternatives to membership: membership of the European Economic Area (like Norway), a bilateral trade agreement (like Canada) or shared membership of the World Trade Organisation (like Japan). Under the first, the loss, relative to a baseline of continued membership, would be between 3.4 and 4.3 per cent of gross domestic product by 2030; under the second, it would be between 4.6 and 7.8 per cent; under the third, it would be between 5.4 per cent and 9.5 per cent. Should we believe these numbers? No. But the direction is right and the magnitudes probably too small. In sum, the UK economy would be less open to trade and foreign direct investment than otherwise, if it left the EU. This would then damage its level of productivity and so its output.

Some proponents of Brexit argue that this is incorrect, because the UK economy would become more deregulated and dynamic outside the EU. Yet the UK is already one of the least regulated large high-income economies. Furthermore, the worst UK regulations — those on land use — are homegrown. Again, the biggest intervention in the labour market in recent years has been the government's decision to impose a big jump in the minimum wage. (See charts.)

Proponents of Brexit will also argue that the UK economy need not become less open. But this argument has a catch. The more the UK wished to preserve its privileged access to the EU market (by becoming a member of the EEA) the less sovereignty it would regain. It would not gain control over immigration and would have to accept single market regulations without any influence on them. If, to take an opposite extreme, the UK chose the WTO option in its trade with the EU, but decided unilaterally to keep its tariffs against the EU at zero, it would be obliged to offer the same deal to all other WTO members. Such unilateral free trade is an option. But it would also remove virtually all the bargaining chips needed to negotiate preferential access to non-EU markets. This is quite apart from the fact that the UK would have far more clout in such negotiations if operating via the EU than if acting all on its own.



Sources: Haver Analytics; OECD; HM Treasury



Data=2013, except US=2008

* Protection for permanent workers against individual and collective dismissal

Another objection is that the EU is becoming a less important market for the UK. Yet the absolute increase in UK exports to the EU over the 10 years to 2014 was still far larger than to any other market even though the growth rate was far slower. This is because the base is so huge. The UK is also the largest recipient of inward foreign direct investment within the EU. It is inconceivable that the attractions of the UK to investors would not be diminished if it did not have access to the EU market on a par with that of members. (See chart.)

These arguments, however, relate only to the long term. Despite absurd attempts to deny this fact, it is also true

> Despite absurd attempts to deny this, nobody knows what would follow a vote to leave the EU

that nobody knows what would follow a vote for Brexit. First, proponents of Brexit do not agree on which alternative to pursue. Second, we do not know what the UK's partners might want. Some foolishly assume that latter will be generous. But a partner who has been repudiated is unlikely to be generous in a divorce. Moreover, the overwhelming aim of the rest of the EU will be to keep it together. They will want to make any exit painful. Finally, Brexit will mean a long period of turmoil and uncertainty. The financial crisis has shown how costly such uncertainty can be, not just for a few years, but far into the future.

For all such reasons, foreign friends are appalled by the potential damage done by Brexit — and not just to the UK, but more widely. Foremost among these is the US. It behoves those who prate of violated UK sovereignty to remember that, had the US not become engaged, the UK would now be a Nazi or Soviet satellite. US resources and will sustained the west during the second world war and the cold war. Pressed itself, the US desires a prosperous and outward-looking Europe, capable of sharing burdens in the decades ahead. The US has long regarded the UK's active participation in the continent, of which the latter will always be a part, as a vital interest. The UK is not the great power of the past. But its actions still have consequences. It is not — and must not wish to be — a European Singapore. Only the west's enemies would welcome such a folly.

How do most informed Americans, Australians or, for that matter, other Europeans, react when they see the UK considering the end of a relationship that gives it a voice in the direction of the continent, while being free from so many of the burdens and mistakes of our partners? They think it mad. Nicely, but firmly, Mr Obama should say so.

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The secret of a world-class biotech sector

OPINION
Geoffrey Owen

Britain, it is often said, has world-class science but too few world-class science-based companies. Nowhere is this more true than in biotechnology. Although Nobel Prizes have been awarded to British scientists in molecular biology, genetics and immunology, no UK biotech company comes close to matching US leaders such as Amgen, Biogen and Gilead in scale, profitability or number of marketed drugs.

Several well-financed companies were founded in the 1980s and 1990s, but there were few successes and too many disappointments, as potentially big-selling drugs failed in clinical trials. After initial enthusiasm, investors lost confidence. The only big winner, in terms of market capitalisation, has been Shire, whose growth has been based largely on drugs acquired through takeovers, principally in North America; it has few links with the UK science base.

The blame is sometimes put on short-termism, investors' reluctance to back companies whose research will take 10 years or more to pay off. But this is hard to square with the fact that the countries known for their patient approach to finance, Germany and Japan, have performed worse than the UK in creating and sustaining biotech businesses; yet the US, where investors are criticised for their fixation on the next quarterly results, has done outstandingly well.

The UK's poor performance compared with the US has less to do with distinctively British weaknesses than with American strengths. When the first biotech companies were formed the US had advantages no European country could match: many high-quality universities whose biomedical research was funded on a massive scale by the federal government; an efficient system for transferring technology from academic laboratories into business; a developed venture capital industry that had made

> The UK's poor performance has less to do with uniquely British weaknesses than with American strengths

money in electronics and could apply its company-building skills to biotech; Nasdaq, a stock market that offered a congenial home for young, high-growth companies; and a big domestic market that, because of the absence of price controls, offered exceptional rewards for innovative drug producers.

On top of this, pioneers such as Genentech, with its genetically engineered insulin, were quick to bring drugs to the market, giving a boost to investor confidence that other countries lacked. As the sector grew, so did the number of specialist investors and the pool of experienced managers.

Although many of its biotechs are ultimately taken over, often by Big Pharma, the US has been able to support emerging companies long enough to create a number of giants. It took Gilead 15 years to go from start-up to profitability, and another 10 to achieve Big Biotech status; the rise in its market value to more than $100bn is the result partly of its successful hepatitis C drug, Sovaldi. In the UK there is a dearth not only of big biotechs but also of independent, medium-sized companies that would make the life sciences sector less reliant on the Big Pharma companies: GlaxoSmithKline and AstraZeneca.

The prospects of filling that gap have improved in the past two years, thanks in part to the spillover into Europe of the prolonged (but now fading) biotech boom in the US. More British companies have gone public. New sources of funding have been established by City of London institutions and the Wellcome Trust, a biomedical charity. Several early-stage companies — for example, those in the hot area of cancer immunotherapies — have recently raised large amounts of fresh capital.

If UK biotech is to grow further, it needs to come up with a big-selling drug using novel technology to treat a serious disease. One or two such successes could transform the sector's image, and the willingness of investors to support it.

The writer, a former editor of the FT, is the co-author with Michael Hopkins of 'Science, the State and the City'

Transparency over tax is not the answer to all our prayers

BUSINESS
John Kay

The Panama Papers have provoked yet more soul searching about tax avoidance. So over the weekend I read the guidance on Gaar recently issued by HM Revenue & Customs. For the benefit of readers outside the UK, and those within Britain who have a life, HMRC is Britain's tax collecting agency and Gaar is the General Anti-Abuse Regulation, which has been part of Britain's tax code since 2013.

Gaar nullifies any tax advantage gained from arrangements found to be abusive. It transforms, and perhaps eliminates, the traditional distinction between avoidance and evasion. It destroys the traditional argument that there is no morality in taxation, only the obligation to comply with the letter of the law and tax code. Regulations such as Gaar in effect say that if you ought to be paying tax, you are legally liable for the tax. Australia pioneered the idea of a general anti-avoidance statute approach a century ago, and France, Germany, Ireland and Canada (but not the US) have followed.

The declaration made in 1929 by Lord Clyde — "No man . . . is under the smallest obligation, moral or other, so to arrange his legal relations as to enable the Inland Revenue to put the largest possible shovel in his stores . . . [and] the taxpayer is entitled to be astute to prevent, so far as he honestly can, the depletion of his means by the Inland Revenue" — has been overruled by statute. But it is easier to proclaim the goal than to make it operational. The guidelines subject a potentially abusive commercial arrangement to a "double reasonableness" test. The arrangement is not abusive if reasonable people would think it reasonable.

The primacy of reasonableness makes the outcry over the Panama

> The primacy of reasonableness makes the outcry over the Panama Papers troubling

Papers troubling. Reasonable is a matter of perception. While it seems reasonable to say that what is reasonable is what reasonable people would think reasonable, this circular definition breaks down if reasonable people have little knowledge of the complexities of modern finance and taxation.

I confess that I recently opened a brokerage account in Luxembourg, with a subsidiary of a Canadian bank. I have never been to Luxembourg except to visit Eurostat, the pan-European statistical agency (yes, I do get out sometimes, but not far). The purpose of the account is not to avoid tax, and the arrangement does not avoid tax. I opened the account to avoid excessive currency charges when buying foreign securities.

But I realise today that this arrangement might sound dodgy if it was described on the front page of a tabloid newspaper, and reasonable people might reasonably ask me to explain why it was reasonable; although no one in the City of London would raise an eyebrow, and many reasonable citizens with reasonably sophisticated investment portfolios would have similar arrangements (sometimes without knowing it).

There was nothing on David Cameron's tax return that told us more than that the prime minister is a reasonably well-off bloke, which most of us know already. The obvious problem of transparency is that journalists, the general public and opposition politicians, who do not really understand what is going on and may not want to, are suspicious of complex-sounding transactions in which they do not themselves engage (or may not know that they themselves engage in).

Such scrutiny has two dangers. One is that having to explain your possibly complex financial affairs to unsympathetic journalists adds to the already too long list of reasons why able people might not want to go into politics. And the other is that such concerns draw attention away from genuinely serious and widespread tax evasion, corruption and money laundering, practices of which the Panama Papers provide yet further evidence.

johnkay@johnkay.com

Shine a light on the disparity of graduate pay by university

Sarah O’Connor

On employment

Imagine that you are facing the biggest investment decision of your life. You are familiar with the small print on investment adverts that says, “Past performance is no guarantee of future results”, but in this case you don’t even have reliable data on that past performance. No idea of whether this particular investment has been delivering higher or lower returns than any of the similar-looking ones on offer. Oh, and you are 17 years old.

For many young people, this is what it is like to choose a university. Not that it is putting anyone off. Degrees have never been more popular: the number of 25 to 34-year-olds with degree-level qualifications in OECD and G20 industrialised nations swelled nearly 45 per cent between 2005 and 2013. In general terms, they are indeed a good investment. Most studies show that graduates earn substantially more over their lifetimes than non-graduates.

But that does not mean every degree from every institution is of equal value. Little wonder that some graduates — in countries like the US and UK, where students generally pay for higher education — have been left feeling short-changed because they can find only non-graduate jobs.

Now there are moves afoot to equip young people with better data. President Barack Obama has passed new “gainful employment” regulations that force for-profit career colleges to disclose the proportion of students that graduate, how much they earn and how much debt they accumulate.

The UK has taken a small step towards transparency, too. Last week, a UK study exploited a vast trove of tax and loan repayment data to examine graduates’ earnings 10 years into their careers. This is a big improvement. Previous, less robust, data looked only at earnings between six months and three years after graduation.

The study confirmed there were big disparities between the earnings of graduates from different universities.

The median male graduate from the London School of Economics was earning about £45,000 a year, for example, while the median university graduate was on about £26,300. Most strikingly, there was a substantial minority of institutions (23 for men and nine for women) where the median graduate was earning less than the median non-graduate.

But the academics did not name those institutions at the bottom. For 17-year-olds, this seems worse than useless. Now they know for a fact some universities will be a waste of money — but they do not know which ones.

To be fair to the researchers, there are reasons to be cautious about publishing data like this. It can be misleading to compare raw numbers without context. David Willetts, the UK’s former universities minister, offers the example of a university in a deprived area that takes local students with relatively poor A-levels. Those graduates might go on to earn more than they would if they had they not attended, but they still might earn less than the UK median salary, since average pay is lower in some regions.

> Young people deserve as much data as possible so they can decide where to study

At the other end of the spectrum, some experts fear the data could pave the way for the universities with the highest-earning graduates to charge higher fees (UK fees are currently capped at £9,000 a year). Critics say the success of those institutions might not reflect the value of the education they provide, but simply that they recruit people with better A-level results or richer parents, or because they offer lots of courses that lead to investment banker jobs.

Yet these are reasons to publish *intelligent* data, rather than none at all. We need a measure of “value added” for each university: a sense of what graduates earn relative to non-graduates with the same backgrounds, locations and A-level results. It sounds tricky, but the authors of last week’s study are halfway there. They did not have all the data they required, but they did adjust for background and A-level results. This narrowed the differences between universities but did not eliminate them.

Of course, the value of university cannot be measured just by the boost to your earnings. But young people deserve as much information as possible so they can decide. I struggle to sympathise with the purists who say this would “financialise” higher education. When I left university in 2006, the average graduate left with £9,670 in debt. Last year, it was more than £20,000. If we did not want young people to see university as a financial decision, we should not have made them pay for it.

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Entrepreneurship. Nerio Alessandri, Technogym

Fit for purpose

The founder of the fitness equipment maker brought Italian design acumen to working up a sweat, writes Rachel Sanderson

Health is wealth: working out at Technogym’s headquarters. Employers encouraging staff to keep fit is the next area of growth, says founder Nerio Alessandri, below

Alessia Pierdomenico

You first see Technogym’s motorway-side headquarters speeding along the road towards the Italian beach resort of Rimini. Undulating curves on the roof look like a sinuous running track racing toward the sea.

Inside the Antonio Citterio-designed building, home to one of the world’s largest sellers of high-end gym equipment by sales, there is no let-up in the sense of motion. Wall-to-wall gym machines — bikes, ellipticals, treadmills — whirr, as they are tested by staff on the factory floor, or used by employees during their breaks in the vast on-site gym.

Even in the offices people do not sit still. There are no chairs. Large black balls take their place. Written on the doors of a single lift: “Take the stairs. Burn calories.” Someone admits that in this workplace it is not worth your career to be seen not taking the stairs. Everyone is trim and smiling.

This is the vision of Nerio Alessandri, who founded Technogym here in his home town of Cesena in the Italian province of Romagna in 1983. Humans are “born to move”, he argues. An autobiography-cum-self-help guide published two years ago opens with the mantra on which Mr Alessandri has built a global fitness business that had revenues of just over €500m last year. Its machines are in top-flight hotels, gyms and homes: “Our ancestors walked 30k a day, nowadays we walk less than 1k daily on average.”

Mr Alessandri is lean, looks younger than his 55 years and moves nonstop. Seated, he rocks forward; standing, he paces about. Showing off an exercise bike, he decides it looks better in another position so, wearing blazer and formal trousers, he picks it up and lifts it. “Physical exercise is incredibly powerful. It is too late looking for a cure in the 20 days before you die, you need to have started preventing [the illness] 20 years before,” he says.

Technogym has been the exclusive supplier to the past four summer Olympics and will be again for Rio this summer.

Still, the Technogym vision is “fitness as pleasure”. In founding the company, Mr Alessandri took the 1980s US fitness craze and added Italian design, with a dash of dolce vita. This is fitness equipment that doubles up as haute interior decor. Mr Alessandri also invokes a newly fashionable term for working up a sweat, Technogym-style: “wellness”.

“Fitness is only hedonistic while wellness is an emotional approach. It is design, glamour, allure, coolness. It becomes fashion and aspirational,” he says.

Indeed, Mr Alessandri considers he is competing with makers of luxury goods. Technogym’s MyRun home treadmill, which retails at well over £2,000 in the UK, for example, is “aspirational like a Chanel handbag”, he says. “But it is aspirational for your health and wellbeing. That is why it needs to be trendy, cool and not punishment.”

Fitness as fashion is having a moment. Hashtags #fitspo — fitness inspiration — and #eatclean — eating healthily — have spread across Instagram, with people taking selfies while working out and photographing their food.

Initially, Mr Alessandri wanted to be a fashion designer and wrote to Giorgio Armani, Italy’s king of pret-a-porter, in the early 1980s seeking a job. Mr Armani never wrote back. It was Mr Alessandri’s “sliding doors moment”; he found fitness equipment instead.

In 1983 he built his first machine — the Hack Squat — in a small garage. Today, alongside Mr Alessandri’s sleek Citterio-designed machines, it looks like torture equipment. But he sold it to a local gym near Rimini, then at the frontline of Italy’s body-beautiful beach scene, and never looked back. For the first publicity photos, his wife Stefania Migani dressed up like Jane Fonda in the 1980s *The Workout* era.

And like Mr Armani, who helped revolutionise women’s wardrobes and working lives by creating the soft-shouldered suit, Mr Alessandri’s Technogym is not just about design: there is technical innovation too. This makes him an outlier in Italy, where laggardly productivity is often blamed on companies skimping on R&D investment.

Technogym launched the industry’s first software system to help people training in the gym in 1996 and the first gym machine with a built-in TV screen in 2002. This year it will launch Running Music, an interactive treadmill that detects the runner’s tread to create a personalised music soundtrack. Overall, it has 240 international patents plus more than 100 design patents.

Still, Mr Alessandri’s longer-term vision appears more intrusive, arguably closer to Big Brother: an Orwellian ecosystem where logging into the Technogym app will feed all the data on your fitness and training regime to your health club, personal trainer, insurer, doctor, hospital and even employer. Isn’t that terrifying? No, he says. “The vital point is that to obtain a result you need to have programmed physical exercise. If you want to tone up, or to treat diabetes, depression or obesity you can’t just go for a walk, you need exercise as medicine. You need personalised training.”

Mr Alessandri says the biggest growth opportunity for Technogym is corporate customers tapping into a trend among businesses to encourage employees to keep fit — both to limit the cost of sick leave and because of growing evidence that it helps productivity.

He cites the ancient Roman mantra “mens sana in corpore sano” or “healthy mind, healthy body”. “We need to return to a human-centric approach,” he says, after too much focus for too long on technology.

How much momentum his idea has will be tested in the coming weeks, when Mr Alessandri plans to list up to 30 per cent of the business on the stock market in Milan.

The reasons are threefold. Its private equity backer Arle Capital Partners, which owns 40 per cent, wants an exit. Mr Alessandri, who with his brother owns 60 per cent of the company, wants to improve governance, and he argues that getting fit for the rigour of the stock market will help do that. Funds raised will be used for expansion.

Technogym is shortly to open its first standalone flagship store in a three-storey palazzo in central Milan, just around the corner from the fashion capital’s grid of luxury shopping streets.

Its revenues in 2015 were €512m, with €87m of earnings before interest tax, depreciation and amortisation. That is up from revenues of €412m in 2013 and €37m of ebitda.

“Health is wealth,” he observes, as a parting shot. In Mr Alessandri’s case, it rings particularly true.

In his own words

Regrets, deals and the best mentor

First breakthrough: “We were the first to create exercise equipment with a built-in TV. We were then the first to add internet connectivity, which enabled us to provide digital content on our products.”

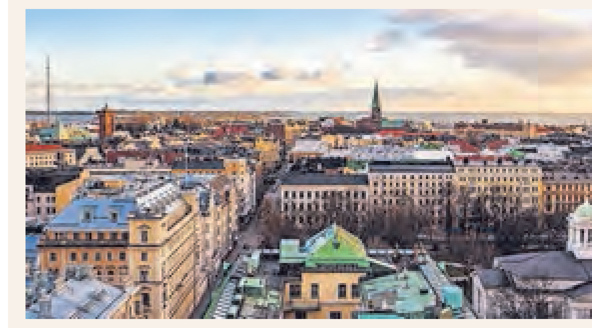
Best deal: “Becoming a supplier of the British Army. Today, the UK is our number-one market in the world.”

Biggest regret: “Choosing the wrong person in a key position. The biggest mistake for a CEO is not finding the right person for the right place.”

Best mentor: “Vittorio Giaroli, founder of consultancy Value Partners in Milan, who helped me transform my entrepreneurial vision into a strategic plan.”

Lets launch in . . .

Helsinki, Finland



Dreamstime

Population **600,000 (wider region 1.4m)**
Invested in start-ups in 2015 **$198m**
Days to set up a company **14**

Few European countries need a start-up launch pad quite like Finland does. Mired in recession for the past four years, the Nordic country has suffered the decline of its two biggest industries: forestry and Nokia. So hopes are high that a cohort of former mobile phone workers can turn promising start-ups into the next big thing.

The case for: The demise of Nokia’s mobile phone business has one benefit for start-ups in Helsinki: a flood of qualified engineers and others with tech skills. Few businesses begin without several ex-Nokians, often at the top.

Finland benefits from good fundamentals: its education system has long been judged one of the best in the world and it has regularly topped the charts. Foreigners often marvel at the quality of skills, and it has established several world-beating companies, especially in gaming.

Helsinki has one of the pre-eminent tech gatherings in Europe. Slush is held in November and December, highlighting the dark winter days as a reason for Finnish success because they inspire people to work. “Welcome the dark. Embrace the cold,” is the festival’s slogan.

The case against: Despite some big successes, late-stage funding remains a problem. Many medium-sized start-ups go abroad for financing and growth.

Finland’s isolated location forces companies to look outwards but limits the size of the local market. Nokia might have been a good training ground but its sheer size was not conducive to entrepreneurialism.

The dark nights and difficult language, despite decent English among locals, can make Helsinki a tough sell for some.

Show me the money: Start-ups can draw on multiple sources for financing, from government innovation agency Tekes, which awards more than €100m a year, to angel investors: the chief executive of Supercell, founder of Skype, and chairman of Nokia are all active; together they recently invested in Wolt, a food delivery start-up.

Local heroes: Supercell has become one of the most successful European tech companies by daring to be different. It has focused on developing a few games for mobile technology. To date it has four: *Clash of Clans*, *Hay Day*, *Boom Beach*, and *Clash Royale*, developed by small teams of no more than 10 people. In 2015, with 180 workers, it made €2.1bn in sales and operating profits of €850m.

Several other gaming start-ups have gained global attention including Seriously, split between Helsinki and Los Angeles, which has tried to bring some of the lessons of the US entertainment industry to its *Best Fiends* title.

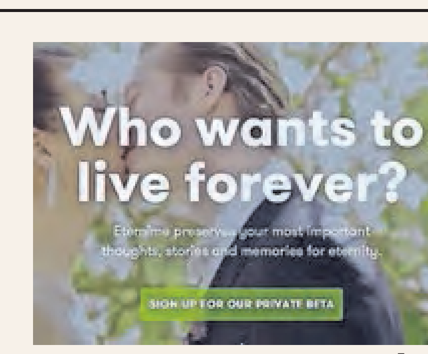
What the locals say: Juho Makkonen, chief executive and co-founder of Sharetribe, says: “There are starting to be enough people with knowledge of networks, accelerators and the support ecosystem, and the quality of engineering, especially, is very good.” However, he says: “At the point you want to get really serious — when you want to raise €10m or more — the funding isn’t really available.”

Richard Milne

Innovation to watch

Chatbot life beyond the grave

HANNAH KUCHLER



Eternime

If Silicon Valley talks about death, it usually plans to stop it.

When Alphabet, the company formerly known as Google, launched its biotech company Calico in 2013, Time magazine ran a cover asking: “Can Google solve death?”, while computer scientist Ray Kurzweil takes a cocktail of pills he believes will help him stay one step ahead of the grim reaper.

But one Bay Area start-up is taking a more modest approach to life beyond the grave by promising to use chatbots to achieve immortality.

Chatbots are taking off. They are being used to order drinks, find information or, less happily, in the case of the recent scandal with Microsoft’s Tay, exchange racist comments. Eternime is betting that people will get so comfortable with these robotic representations that they will want to talk to artificially intelligent versions of their ancestors.

Eternime says it “preserves your most important thoughts, stories and memories for eternity”. Which sounds sweet, until you read the vaguely threatening website: “We all pass away sooner or later. We only leave behind a few photos, maybe some home videos, or in rare situations, a diary or autobiography,” adding: “But eventually, we are all forgotten.”

The product, currently in a private beta test, creates an “intelligent avatar” that looks like you (largely because it is a picture of your face) and is trained to know and understand your life so that people in the future can converse with it.

Some 30,000 people have signed up for early access to the service, which Eternime wants to become a database of the dead: “Think of it like a library that has people instead of books, or an interactive history of the current and future generations. An invaluable treasure for humanity.”

Lex.

Twitter: @FTLex **Email:** lex@ft.com

Ashmore: pride of place

The Argentines themselves joke about their country's pridefulness: how does an Argentine end it all? By climbing his own ego and jumping off.

The sense of self-worth will be bolstered by Argentina's first successful sovereign bond launch this decade. The new president is market friendly and has settled inherited grievances with hedge funds. With longer maturities yielding more than 7 per cent, the oversubscribed deal, worth up to $15bn, went well. After this year's strong run, emerging market bond managers have sturdy egos, too.

One of those, the UK-listed emerging-market debt specialist Ashmore, reported yesterday. There was some good news: assets under management rose almost 4 per cent on the quarter to $51bn, better than analysts' forecasts. Chief executive Mark Coombs, a proud cheerleader for emerging markets, thinks there is still plenty of "absolute and relative value". Someone is listening. Ashmore's shares are up by half from their January lows.

Emerging-market yield spreads have fallen below the average US corporate high-yield spread, Credit Suisse says. A year ago, markets favoured US high yield over EM (the shift is as much about the dire state of US energy bonds as sentiment towards EM). EM debt issuance has not diminished, either. It is up more than 12 per cent year to date, according to Dealogic.

Mr Coombs will need to keep on persuading. Ashmore's shares have priced in a very healthy recovery. Last quarter may have been good but AUM a year ago were almost a fifth higher at $61bn. It is a stretch to believe that earnings will jump enough during the next two years to justify that sharp share price recovery.

Consider what would happen if AUM did recover to the previous peak. On its average fees of 60 basis points and a better than expected profit margin, the added revenues — about £42m — would lift earnings to a level a fifth higher than current consensus estimates for 2016. Yet the shares are up 50 per cent this year. Only if earnings rise as much as the shares have will Ashmore look historically cheap relative to earnings.

Ashmore can brag that its funds have performed well versus peers in recent quarters. May it continue.

But unless the growth in inflows is surprisingly sharp over the coming year, Ashmore shares have seen their best.

Australian beef: well done

Whenever China comes out of the present period of political and economic uncertainty, it is sure to have worked up a heck of an appetite. Best be ready.

Yesterday, China's Hunan Dakang, a pig breeder, said that its Australian subsidiary would buy a majority stake in Australian cattle-rancher S Kidman.

It will pay $230m for 80 per cent of the target, which owns about 100,000 sq km of Australian farmland — 1.3 per cent of the country — rearing nearly 170k head of cattle. The price equates to 15 times S Kidman's 2015 net earnings, according to Hunan Dakang's disclosures. The remaining fifth will be bought by Australian Rural Capital, an Australia-listed company that invests in agriculture.

The purchase looks well timed. Australia's beef exports to China amounted to A$750m (US$585m) in the year to June 2015, on official data. Last year the two countries signed a trade agreement to eliminate tariffs of between 12 per cent and 25 per cent on Australian beef exports to China over the next decade. Meanwhile, other factors that have suppressed supply, such as drought and destocking, will encourage a recovery in prices, Deloitte expects.

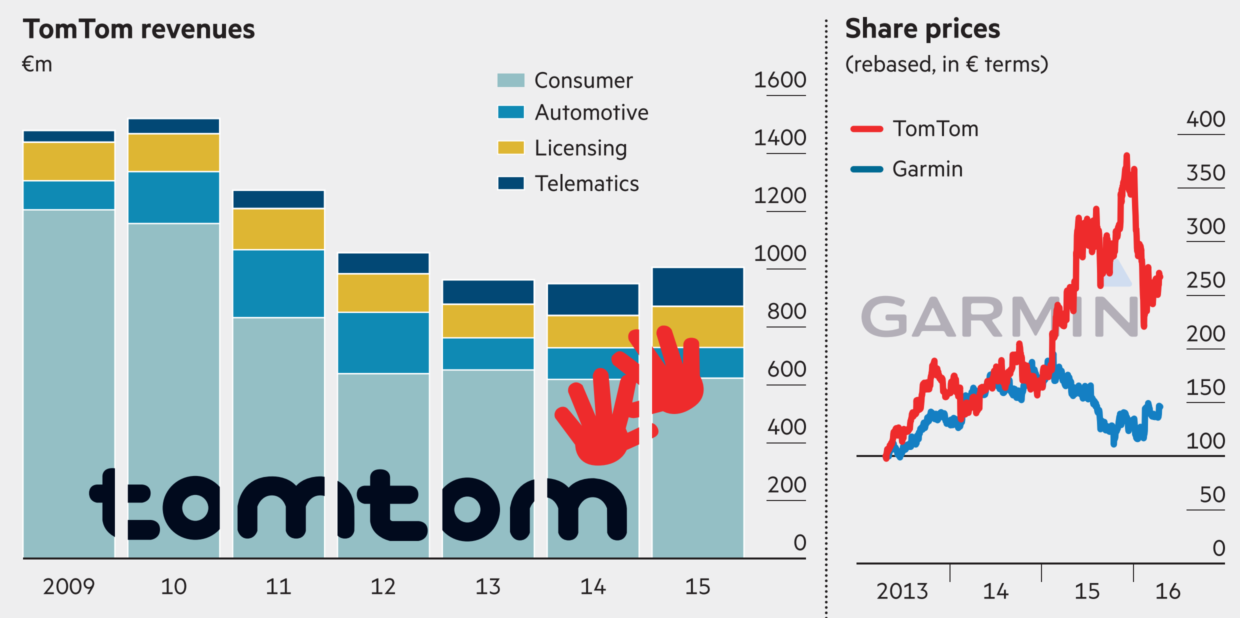
Shenzhen-listed Hunan Dakang, with a market capitalisation of nearly $3bn, seems a sensible enough suitor.

ARC, with a listed value of $4m, looks more odd. With $350,000 cash on hand, ARC will need to convince investors to stump up $60m for the deal even as its primary asset — one-tenth of the listed cotton co-operative Nomai — is faring badly. Adding a local partner, however, may give the deal a better chance of success after it was rejected last year on national security grounds.

The Foreign Investment Review Board will rule on the deal in July. If successful, ARC will offer a new way to access Australia's promising cattle market. Hunan Dakang will tap into diversified routes to China's growing demand for animal protein. Yum, yum.

Lost and found

Smartphones have curtailed sales of satnavs, and crushed their margins, but TomTom has found other ways to monetise its intellectual property – one reason its shares have outperformed Garmin's recently



FT graphic Source: S&P Capital IQ; Thomson Reuters Datastream

When satellite navigation was the new thing, tales abounded of drivers stranded miles from their destination by the still-buggy tool. TomTom, a satnav trailblazer, must also avoid getting stuck in a cul-de-sac.

Smartphones have squeezed the Dutch company's device sales. Despite a foray into watches, first-quarter sales of consumer products fell 4 per cent, it said yesterday. But TomTom is no BlackBerry. It still has two very credible assets: its mapping database and, closely related, its independence. The world's other two map databases are owned by Google and Here, which was sold to a consortium of German carmakers last year. The theory is that most carmakers will be reluctant to allow a rival or software titan under the dashboard and will instead flock to the uncompromised TomTom.

Sales in the automotive division were up 30 per cent in the first quarter. Licensing revenue rose strongly too. And the stock market is increasingly appreciative of the value of TomTom's intellectual property. Over three years, its shares have outperformed those of Garmin — a US company with similar roots but without a mapping database.

The question is how to monetise that knowledge. Digital cartography is expensive, especially when it comes to adding the kind of detail that will be needed for driverless cars. TomTom warned that investment levels would increase this year; it is questionable how long it can rely on device sales to help fund such commitments. Before interest, tax, depreciation and amortisation, profits in the consumer division were €14m in 2015 — down from €55m in 2014. Consumer margins are barely a quarter of their 2013 levels.

It could sell the maps database; the €2.5bn fetched by Here is more than TomTom's market value.

A better option, given its waning profitability, might be to ditch the consumer devices and focus on selling to carmakers and on mapping, with the fleet tracking and licensing businesses (Uber is a customer of the latter) driving profits. The company says there is still mileage in the devices that made its name. But it risks running out of road.

Netflix: red peril

Netflix is "breaking through the cultural zeitgeist", proclaimed the video-on-demand company in quarterly results on Monday. Its stock then broke below the more tangible $100 level, falling sharply after hours.

Grand ambitions helped Netflix become the best-performing S&P 500 stock of 2015. In January, it produced a map of the world coloured almost entirely in its corporate red to publicise its expansion to 130 more countries. But while first-quarter results contained a 4.5m bump in non-US customers, to 34.5m, Netflix forecast just 2m more in the current quarter — more than 50 per cent below analysts' forecasts. In percentage terms, the increase would be the smallest ever.

After Monday night's 8 per cent drop, the company still has an enterprise value of more than four times its 2016 revenues. This is puzzling. Other high-priced internet stocks can boast bigger barriers to entry — think of Amazon's physical infrastructure. Netflix, like the TV networks it seeks to displace, is on a hamster wheel of buying or producing ever more content. The next Adam Sandler film or new Gérard Depardieu series — both launching soon on Netflix — may lure more subscribers, but more will always be needed.

Amazon announced a video-on-demand offer on Monday, separating it from its Prime shopping membership programme. It offers some advantages over Netflix, including the ability to download content to watch offline. At home and on its travels, Netflix will encounter similarly stubborn competitors, unwilling to roll over.

The battle is expensive. Netflix has raised prices in the US to help fund an additional $1bn spending on content, but is burning cash at $1bn a year and needs to tap debt markets. The company notes that its bonds trade better than their single B rating implies and suggests that "over time" the rating agencies "may catch up". Then again, shareholders might catch up with the risk of the proposition. Zeitgeists are fickle things.

Goldman Sachs: primary challenge

It is fitting that Goldman Sachs reported first-quarter earnings on the day of New York's presidential primary. Wall Street's most fabled franchise is polarising, too, and Goldman has been slammed repeatedly by Bernie Sanders, the firebrand challenging Hillary Clinton for the Democratic nomination. Mr Sanders will surely be heartened by the bank's poor showing. Revenue and earnings per share fell 40 per cent and 55 per cent, respectively, from the year before.

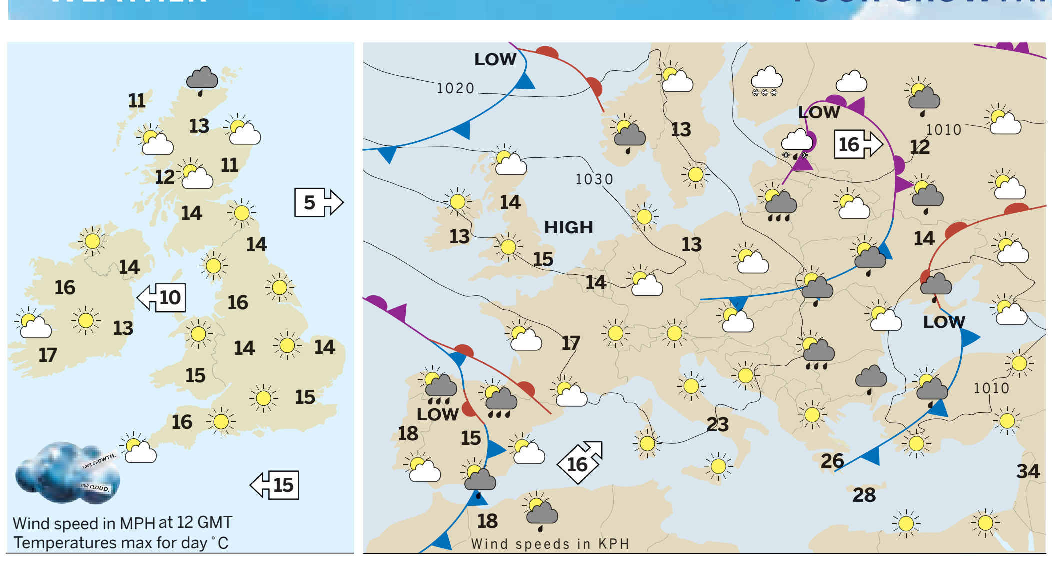
This revenue shortfall was not the result of the regulatory clampdown Mr Sanders craves. Rather, fees from IPOs and dealmaking fell, as volatility in equity markets spooked investors around the world. Trading in fixed income, currency and commodities, a strength at Goldman, was down sharply as well. But the weaker profits would have looked better if regulators had not insisted on less leveraged balance sheets (Goldman's return on equity was a thin 6.4 per cent; it usually leads peers at about 10 per cent).

Goldman claims its results were down to a low point in the cycle. It offset the weakness by holding non-payroll operating costs to the lowest level since 2009 (it helped that the quarter did not contain a $225,000 speech from Mrs Clinton). Harvey Schwartz, chief financial officer, pointed out that the bank had reduced assets in the fixed income unit by a quarter since 2013, along with similar cuts in pay and headcount there. Yet he reiterated his commitment to the costly, capital intensive and volatile division, from which others, including rival Morgan Stanley, have retreated.

Goldman's dominance comes in part from sticking with its strategy through short-term choppiness. Its shares traded up 2 per cent yesterday, so its confidence seemed to be appreciated. But the bank has not produced consistent revenues in FICC since the 2008 crisis. It faces real questions about its approach, and not just from cranky populists running for office.

FT Lex on the web
For notes on today's breaking stories go to www.ft.com/lex

WEATHER



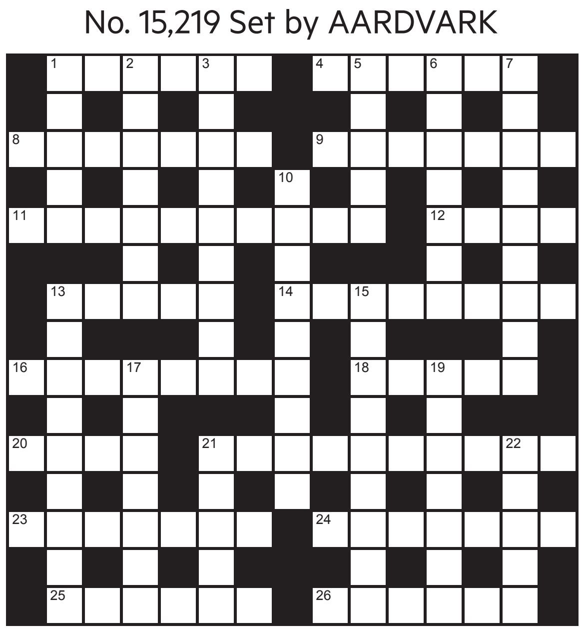
Forecasts by MeteoGroup

Today's temperatures Maximum for day °C & °F Warm front Cold front Occluded front

Abu Dhabi	Sun	32	90
Amsterdam	Sun	13	55
Athens	Sun	27	81
B'ham	Sun	15	59
Bangkok	Fair	36	97
Barcelona	Fair	20	68
Beijing	Sun	25	77
Belfast	Sun	15	59
Belgrade	Fair	16	61
Berlin	Fair	13	55
Brussels	Sun	14	57
Budapest	Sun	16	61
Buenos Aires	Sun	23	73
Cardiff	Sun	15	59
Chicago	Shower	20	68
Cologne	Sun	15	59
Copenhagen	Sun	12	54
Delhi	Sun	40	104
Dubai	Sun	31	88
Dublin	Sun	13	55
Edinburgh	Sun	15	59
Frankfurt	Sun	15	59
Geneva	Sun	17	63
Glasgow	Fair	14	57
Hamburg	Fair	10	50
Helsinki	Sleet	7	45
Hong Kong	Fair	27	81
Istanbul	Rain	24	75
Jersey	Sun	14	57
Lisbon	Shower	18	64
London	Sun	15	59
Los Angeles	Sun	29	84
Luxembourg	Sun	14	57
Lyon	Sun	21	70
Madrid	Rain	15	59
Manchester	Sun	16	61
Miami	Fair	27	81
Milan	Sun	23	73
Montreal	Sun	13	55
Moscow	Shower	12	54
Mumbai	Sun	33	91
Munich	Sun	14	57
New York	Sun	18	64
Nice	Sun	19	66
Paris	Sun	17	63
Prague	Fair	11	52
Reykjavik	Shower	6	43
Rio	Sun	34	93
Rome	Sun	21	70
San Francisco	Sun	22	72
Stockholm	Fair	11	52
Strasbourg	Sun	17	63
Sydney	Sun	25	77
Tokyo	Sun	18	64
Toronto	Sun	14	57
Vancouver	Sun	19	66
Vienna	Sun	15	59
Warsaw	Fair	12	54
Washington	Sun	21	70
Zurich	Sun	18	64

CROSSWORD

No. 15,219 Set by AARDVARK



JOTTER PAD

ACROSS

1 Assistant's experiment to make cake (6)
4 Expression of reservation about armed fleet in battle (6)
8 Look frantically in bird's place for files, clippers etc (7)
9 Notice displaying vehicle described by youngster after parking (7)
11 Rash children pick one novel by unknown (7,3)
12 Article about sport, portraying English runner (4)
13 Project written before 1st of April about new military government (5)
14 Piece of meat buttery in the middle, with crackling perhaps (8)
16 Small table, pick of the bunch, mostly stays around office zone (8)
18 Type of tooth woman wanted, with gold filling (5)
20 Bones revealed by map-makers when travelling west (4)
21 Old pop group avoiding the spotlight here? (3,7)
23 Sudden eruption faculty reported at college (5-2)
24 Play pontoon regularly, attracting the underworld (7)
25 Recall missing sappers, part of army unit? (6)
26 Left winger's disguising sudden pain (6)

DOWN

1 Dog loves constant resident in pub (5)
2 Sort of chip is thrown over, cold, eaten by cat (7)
3 Being fine and dry inside, showers hit the roof (5,4)
5 King welcomes the French moderate (5)
6 Amount of land at this point keeping to Reform Act? (7)
7 Decorative work to get spliced outside still lacking centrepiece (9)
10 Jack handles this type of bowler maintaining attack at both ends (9)
13 Japanese certain to knock back meal when roaming ancient city (9)
15 Murdoch, on strike, obtains street food for Paddy? (5,4)
17 Plan shows Indian city with simple housing (7)
19 See about book owned by college fellow, my good friend (3,4)
21 Character in Marathon training in shade (5)
22 Writer of Dublin's expansive about mouth of Liffey (5)

Solution 15,218

M	I	N	N	E	S	O	T	A		B	R	E	A	D
A		A		A		P		T		E		N		A
T	I	T	U	S		A	B	S	T	A	I	N	E	R
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F	R	A	I	L	T	Y		E	V	O	L	V	E	R
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P	O	S	I	T		D	I	S	I	N	F	E	S	T

Companies & Markets
FINANCIAL TIMES

The Firm Market should woo family businesses
LOMBARD, PAGE 20

TDK Corp	Pioneer	Netflix	German 10-year Bund	Nikkei 225	Korea won/ US dollar	Brent crude	Silver
8.24%	0%	11.84%	1bp	3.7%	1.4%	2.24%	4.4%
¥6,440	¥318	$95.56	0.17%	16,874	Won1,127.4	$43.87	$16.91

Goldman's profit fall caps glum season for Wall Street

- First-quarter income plunges 56%
- Bank revenue down across the board

BEN MCLANNAHAN — NEW YORK

Goldman Sachs' profits more than halved after across-the-board falls in revenues, bringing down the curtain on a sobering first-quarter earnings season for the big US banks.

Executives at the Wall Street group had prepared the market for big falls in key trading and investing businesses, blaming the rocky start to the year across stocks, bonds and commodities.

In the end, earnings per share for the period were better than analysts had feared, thanks largely to a one-off gain from refinancing preferred stock. But in terms of revenues, which fell about 40 per cent from a volatility-boosted period a year earlier to $6.34bn, the quarter was the worst in more than four years for Goldman.

Revenues from investment banking dropped 23 per cent to $1.46bn, equity trading was down 23 per cent to $1.78bn, and revenues from the core bond-trading unit plunged 47 per cent to $1.66bn. Net income for the period was 56 per cent lower at $1.2bn.

Guy Moszkowski, analyst at Autonomous Research, said the "terrible" period in bond trading had underlined Goldman's exposure to institutional investors, rather than big multinationals that keep trading through tough periods.

Such transactional "flow" business softened year-on-year falls in debt trading for universal banks such as JPMorgan Chase, Citigroup and Bank of America.

Goldman's earnings of $2.68 a share, down 56 per cent from last time's $5.94, were ahead of analysts' estimates of an average of $2.45, completing a clean sweep of brighter than expected earnings among the six biggest US banks.

But analysts said that all the big banks had talked down their prospects in the weeks before earnings, meaning they had very low bars to clear. Each of Goldman's four core units showed double-digit falls from a year earlier.

The weakest result came from the investing and lending unit, a set of businesses trying to make good returns on Goldman's own capital. It posted net revenues of just $87m, down 95 per cent from a year earlier, as the bank struggled to exit investments and wrote down the value of many of the remaining assets on its books.

Harvey Schwartz, chief financial officer, accepted that the quarter had been "tough" but said that things were looking up. "March was better than February and February was better than January," he said. So far in April, he said, "the market feels a little fragile . . . but for the most part it feels like that is behind us". He stressed that the bank had kept a lid on costs during the period. Pay dropped 40 per cent, exactly in line with revenues, while non-payroll costs amounted to $2.1bn, the lowest since the second quarter of 2009.

Even so, Goldman's annualised return on equity during the period came to 6.4 per cent, well short of its double-digit target, prompting some analysts to ask why Goldman was not considering more radical measures to boost profits. The market expects Goldman to make an 8.3 per cent ROE for the full year, which would mark its worst return since 2011.

Shares in Goldman were up about 1.5 per cent by midday in New York.

Lex page 14
Lenders suffer revenue fall page 16

Out of bounds FCA warns asset managers to stay off golf course in crackdown on high-value gifts

The FCA's review found executives were spending too much wooing clients with hospitality

AIME WILLIAMS AND MADISON MARRIAGE

Fund managers have been warned to stay off the golf course by regulators in a sign that the good times continue to roll for some in the City.

The Financial Conduct Authority said in its 2015 review into conflicts of interest in asset management that executives were spending too much wooing clients with hospitality, despite rules published in 2014 cracking down on offering gifts or hospitality that are "of unreasonable value".

The report found that fund managers were still offering social events not directly helpful for business — such as inviting advisers to attend rugby games or play golf. "Hospitality provided or received did not always appear to be designed to enhance the quality of service to the client," it said.

Asset managers insisted the industry had tightened its belt greatly since the days when, according to one, clients were flown by helicopter from the British Grand Prix to the 1998 World Cup final in Paris.

"Soon we will be having a golf day without golf balls, a fishing day in the gym and we will be watching Formula One on the office TV," scoffed Justin Urquhart Stewart, head of Seven Investment Management.

Short View

Dan McCrum

The euro has spent much of 2016 accumulating value compared with the dollar. It is in good company.

Five central banks have surprised many of the investors and economists who try to predict their actions this year by announcing bigger and bolder measures designed to stimulate economies, nourish inflation and — some argue — suppress exchange rates.

Lower interest rates might be expected to weaken currencies. Yet policymakers in the eurozone, Japan, New Zealand, Sweden and Norway have all seen the value of their currencies rise in response. Signs that markets are beginning to lose faith in the powers of central banks, perhaps: the strengthening of the yen appears odd only until the price is compared with the less than ¥80 a dollar purchased before the arrival of Abenomics at the end of 2012.

But if it seems that the gods of money live in markets too deep and ineffable to fathom, an even longer-term perspective provides a different guide. The average rate against the dollar this century is ¥106, not far from the ¥109 where it was trading yesterday.

Think about the euro in similar terms and it could easily be stronger. Worth $1.23 on average since the millennium, the level would be a halfway house between where the euro has traded since the European Central Bank announced its quantitative easing programme at the start of 2015 and the much higher price that preceded it.

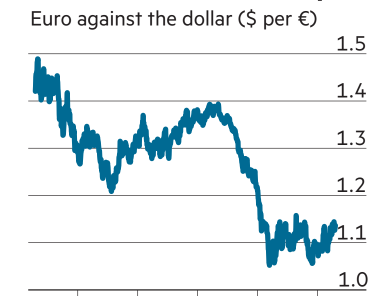
Yet monetary policy also gives reason to think further euro strength is possible. Inflation has been picking up in the US even as the prospect for further increases in interest rates has diminished, lowering bond yields.

Subtracting the level of inflation from that of nominal interest rates produces a calculation of the real interest rate faced by businesses and consumers. So, rising US inflation has served to push real interest rates further below zero, and further below the level in the eurozone where inflation remains moribund, according to BNP Paribas.

A stronger euro would in turn mean cheaper imports and even less inflation in Europe. There would be further pressure on the ECB to act, but also fresh questions about the power of policy if it does.

The level best for Europe

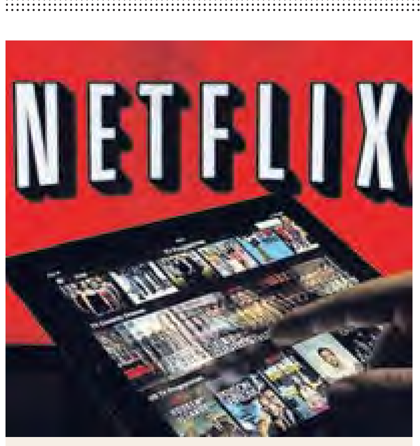
Euro against the dollar ($ per €)



Source: Thomson Reuters Datastream

Monetary policy gives reason to think the euro could rise further, which would put pressure on the ECB to act again.

dan.mccrum@ft.com



Amazon and Netflix lock horns in streaming battle

Amazon and Netflix are battling to capture television audiences that are moving away from traditional TV in favour of digitally streamed, on-demand viewing. The question is whether they can each prosper in an increasingly competitive environment.

Lex ►PAGE 14; **Analysis** ►PAGE 19

EDF fears exposed as managers warn board over legal risks of Hinkley Point

MICHAEL STOTHARD — PARIS

A group of managers at EDF has sent a letter to the French utility's board of directors warning they could face legal action if the company pushes ahead with its £18bn Hinkley Point nuclear project in the UK.

The letter, dated April 19 and seen by the Financial Times, said that if a board decision in favour of Hinkley Point led to "destruction of value" at EDF then its directors could be held personally responsible.

Most EDF board members are expected to vote in favour of the final investment decision on Hinkley Point at a meeting scheduled for May 11. But the managers' letter comes before a board meeting on Friday, at which directors are expected to discuss the funding of the project.

François Hollande, the French president, is meeting ministers at the Elysée Palace today to discuss financing options for Hinkley Point. The French state has an 85 per cent stake in EDF.

The letter by the EDF managers highlights the ferocity of the internal battle that has raged over Hinkley Point, with Thomas Piquemal, chief financial officer, resigning last month over his concerns that the UK project might endanger the company's future.

Three people familiar with the letter confirmed its contents to the FT. It recommended that the board should commission a series of extra studies on Hinkley Point, convene a special shareholder meeting and talk to the French market regulator and lawyers.

The FT approached EDF to comment on the letter to EDF. The company said: "This is an anonymous document that we have never seen and so we cannot comment."

The letter was not signed, with one of the people involved saying that was because the managers feared for their jobs if they publicly warned on the dangers of Hinkley Point.

Critics of Hinkley Point have raised concerns over the cost of the project, given EDF's stretched balance sheet. The group's €37bn of net debt dwarfs its €19bn market capitalisation.

Clean-up costs weigh on EDF page 17

Companies / Sectors / People

COMPANIES

Financials

Paulson funds' assets tumble by $2bn

Soured bets on Allergan and Valeant take toll on total sum managed

LINDSAY FORTADO — LONDON
MARY CHILDS — NEW YORK

John Paulson's losing bets on Allergan and Valeant have contributed to a near-$2bn fall in his funds' assets in the space of five months — taking the total amount managed by his hedge fund business to its lowest level in almost 10 years.

Paulson & Co — one of the titans of the US hedge fund industry — made billions of dollars betting against subprime mortgages ahead of the financial crisis. Its Advantage Plus fund returned 17 per cent in 2010, following gains of 21.5 per cent in 2009, 37.6 per cent in 2008 and 158.5 per cent in 2007.

But fund documents show that the company's assets under management had fallen to $14.3bn as of March 1 — down from $16.1bn in November, and from a high of $36bn back in 2011.

These numbers are unlikely to have improved since March, given sharp falls in the price of Mr Paulson's pharmaceuticals holdings.

His funds were down about $250m after a 17 per cent plunge in Allergan shares — his largest holding — on April 5, on news that tough new tax rules from the Obama administration had scuppered a takeover bid from Pfizer.

At the same time, Valeant, once a Wall Street darling, has suffered a series of share price falls following fears over its business model and ability to repay debt. Its shares are currently trading at about $32.60, having stood at $262.50 in August. Paulson was the sixth-biggest shareholder as of the end of December, according to regulatory filings.

Paulson & Co's Advantage Plus fund is now down 15 per cent this year and Mr Paulson is tapping his own fortune as additional collateral for his firm's funds as a guarantee for its credit line, according to a person familiar with the returns.

He is faring worse than most event-driven and activist funds this year, as well. Hedge Fund Research's event-driven index advanced 2.7 per cent in the first quarter, while its activist index gained 3.1 per cent.

Paulson & Co declined to comment.

$14.3bn
Assets under management at March 1, according to fund documents

15%
Reduction in value of Paulson & Co's Advantage Plus fund this year

But Mr Paulson is not alone in his woes — 2016 has been a rocky year for hedge funds, with sharp losses incurred by marquee names.

Many managers trimmed their bullish bets and added short positions as markets fell in the first six weeks, only to have those short positions hurt them when the market reversed course.

"Bad things happen when you're the least prepared for them," Alexandra Coupe, head of asset allocation research at Pacific Alternative Asset Management Company, said of this year's turmoil.

Part of Mr Paulson's current strategy is focusing on specialty pharmaceutical companies that may be takeover targets.

Banks. Slowdown test

US lenders suffer biggest revenue fall in 5 years

Net income plummets 24% as consumer gains fail to offset trading and dealmaking woes

ALISTAIR GRAY — NEW YORK

The six biggest US banks have suffered their steepest decline in quarterly revenues since 2011, after a profound slump on Wall Street overshadowed better results in their consumer businesses.

JPMorgan Chase, Bank of America, Citigroup, Goldman Sachs, Morgan Stanley and Wells Fargo generated total revenues of $98bn in the first quarter, down 9 per cent from a year earlier — the steepest fall in five years, according to a Financial Times analysis of Bloomberg data.

Deep cost cuts failed to counteract the fall in revenue so the six lenders also saw their collective net income plummet 24 per cent year on year to $18bn.

Goldman became the latest victim of the slowdown in trading and dealmaking yesterday when the investment bank posted its lowest first quarter revenue since Lloyd Blankfein became chief executive in 2006. Net earnings dropped more than half, echoing a similar decline at competitor Morgan Stanley.

Analysts have forecast a second-quarter dip but some executives are more optimistic

Money worries: Goldman Sachs and the five other big US banks saw revenues fall by 9 per cent in the first quarter compared with 2015 — Richard Drew/AP

The aggregate figures for the big six banks illustrate the sector's reliance on turbulent securities businesses. Banks that have sizeable consumer divisions held up significantly better. Net income at the retail arms of JPMorgan Chase and Bank of America rose 12 per cent and 22 per cent respectively.

But the overall results from the big six were not as bad as feared, spurring an 8 per cent rally in bank stocks since JPMorgan started the reporting season last Wednesday.

Of the six banks, only Wells Fargo, which has the smallest investment banking arm, increased revenues from a year earlier — by 4 per cent, and that was thanks in large part to the acquisition of loan books from GE Capital.

Debt trading was particularly hard hit in the first quarter as uncertainty over US monetary policy combined with jitters over China's economic growth and sinking commodity prices to put investment banks' clients off dealing.

The collective performance stands in contrast to the first quarter of 2015, when a revival of trading desk revenue stirred hopes that investment banks had finally put a long period of depressed returns behind them. While the battering was caused largely by difficult markets, the drops also reinforce fears that post-crisis regulation and a shift to electronic trading platforms have permanently damaged investment banks' fortunes.

Analysts have forecast another year-on-year dip in total revenues in the second quarter. But some executives are more optimistic. They said trading businesses had recovered in March and April. Some also said they expected advisory and underwriting fees from deals, initial public offerings and debt raising to recover. John Gerspach, Citigroup's chief financial officer, said the bank had a "significant backlog" of investment banking deals.

Gerard Cassidy, analyst at RBC, pointed to Bats Global Markets' successful IPO last week. "This could be a signal that the window may reopen," he said.

Whether or not investment banks make a recovery, analysts expect retail and commercial operations to continue to act as a ballast.

Several financial executives said they believe American consumers are resilient so they plan to increase lending through credit cards, mortgages and car loans. "The consumer is in good shape," said Tony DeSpirito, portfolio manager of the BlackRock Equity Dividend Fund, which manages $21bn.

He argued that large banks were among the most attractive areas of the stock market: they are trading at or near all-time lows as measured by the ratio of their share prices to their tangible book value — a closely watched valuation metric.

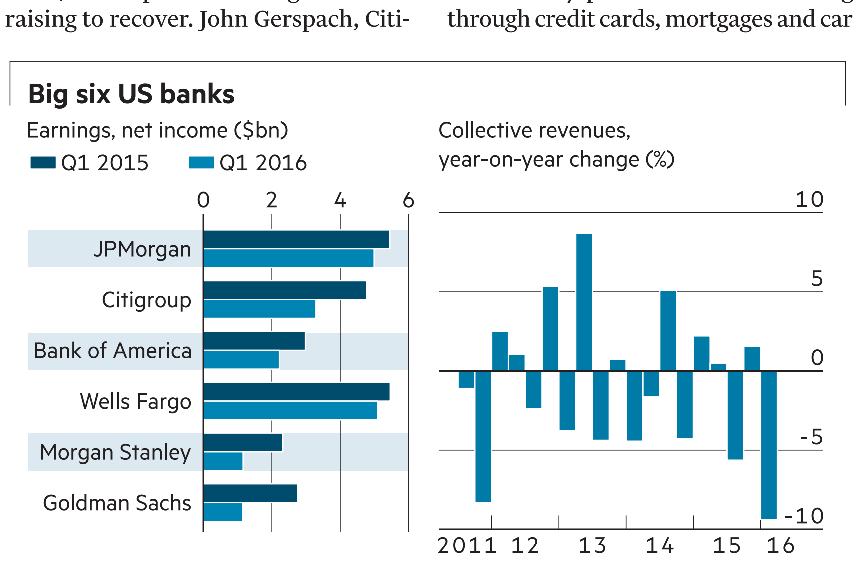
Mr DeSpirito said dividends were underpinned by stable retail divisions and that share prices could rally even if the Federal Reserve did not increase rates this year.

"The Fed raising rates is great for the banks. But it's all upside. There's really no expectation for interest rates rises this year [pointing to consensus forecasts]," he said.

However, support from the consumer and commercial divisions is unlikely to last.

Wells Fargo, Bank of America and JPMorgan all increased reserves for energy losses in the quarter by $500m. So far, losses have been largely contained to energy.

"Most segments are doing relatively well," said Brian Charles, analyst at RW Pressprich. "Right now losses are almost at historic lows." But he added: "Eventually losses are going to creep up."



INSIDE BUSINESS

ASIA

Jennifer Hughes

It'll be no easy ride for banks as they try to court Asia's wealthy

The multimillionaire sputtered into his wine when asked about the quality of his bank's services. "Are you kidding?" he asked, as he detailed a litany of complaints about hassles and complications likely to be familiar to anyone with a bank account and access to a helpline. But this millionaire is from Asia, and thus belongs to one of the world's most-courted set of bank customers. If he doesn't like his current set-up, he has choices. Bank executives around the world are lining up to tell their shareholders they are looking east in search of higher profits.

The case is at first glance a strong one. Last year, Asia's wealthy — those with at least $1m in investable assets, excluding their primary home — overtook those in the US to become the largest group in the world, according to a report by Capgemini and RBC Wealth Management. Their wealth is growing more quickly too, at 11.4 per cent in 2014 compared with 7.2 per cent globally.

In absolute numbers, Asia is home to 4.7m of the world's rich people who hold $15.8tn that should be in search of management and other services. Private bankers estimate perhaps as much as half of this is not being professionally managed. The region is also embarking on an unprecedented generational transfer of wealth as the current set of patriarchs prepares to hand over the reins.

"If you are a wealth manager you want to be where the wealth is being created. And wealth is being created on a huge scale in emerging markets whichever way you want to look at it," said Tidjane Thiam, chief executive of Credit Suisse, this month before embarking on a five-day visit to the bank's most-valued Chinese clients. Credit Suisse has drawn back from the US and parts of Europe, but has doubled the growth rate of its 600-strong army of Asia-based relationship managers. UK-listed rival Standard Chartered, meanwhile, plans to use its decades-old corporate relationships in the region to support its push into private banking.

But how easy will it be for banks to establish lasting — and profitable — relationships? Not all multimillionaires offer the same opportunities. JPMorgan became a case in point this month when it cut one-fifth of its Asian private bank relationship managers (RMs) and refocused on customers with more than $10m. "The economics are such that for most private banks, unless you have somewhere starting between $7m and $9m to invest, offering a full private banking service is probably unprofitable," says Chris Harvey, global head of financial services at Deloitte.

Last year the region overtook the US as home to the most rich individuals

Yet most banks do not know how best to deploy their employees. While 90 per cent of them can track revenues attributable to each relationship manager, fewer than one in 10 can measure individual profitability, according to a study by BCG. Scale matters as well. Geneva-based Union Bancaire Privée this week said that its $10bn assets under management (AUM), mostly acquired from its takeover of Coutts' international operations, were about half the level it would need to be comfortably profitable. Getting to $20bn would rank UBP 17th in the region, according to Asian Private Banker. UBS, Citigroup and Credit Suisse are the largest competitors with $274bn, $210bn and $150.6bn under management, respectively.

Regional competition is also toughening. Singapore's DBS acquired Société Générale's wealth management business two years ago and OCBC this month added Barclays' Singapore and Hong Kong units to its Bank of Singapore brand. Those two lenders now have roughly $75bn AUM apiece — and they too boast deep relationships around the region.

The last challenge for wealth managers is the nature of the clients themselves. They are slow to entrust assets, favouring old-style long-term relationships, which can be expensive for the banks involved. They also like to hold more cash than the rich elsewhere, cutting into fees, according to Capgemini, and they expect their bank to extend more credit than their peers do elsewhere.

"The margins have come down since the financial crisis," says Michael Blake, head of UBP's private banking operations in Asia. He attributes this to costs such as compliance as well as competition. "It is, however, absolutely possible to be profitable in this market. Clients will pay for advice and they value the networking effect of a private bank, too."

Given the strains on business models elsewhere, even the possibility of profits from Asia's wealthy will keep banks coming. But they shouldn't expect it to be easy.

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Media

Publicis buoyant as it eclipses sales forecast

ADAM THOMSON — PARIS

Publicis shares recorded their biggest single day gain in seven years, as the French advertising group reported forecast-beating sales growth during the first quarter.

Shares closed 6.8 per cent up yesterday as the group, which has brands including Saatchi & Saatchi and Leo Burnett, said that organic revenue grew 2.9 per cent to €2.29bn in the first quarter compared with the same period last year.

That was much higher than consensus forecasts of just 0.3 per cent and came on the back of better than expected revenue figures for Publicis at the end of last year.

Maurice Lévy, chief executive, described the first three months as "a promising start to 2016", and attributed the strong numbers to accounts won at the end of last year as well as to "good momentum" in the media market.

However, he cautioned about the next two quarters, which would be more affected by losses in last year's media account reviews.

Publicis said yesterday that it would maintain previous pledges to improve all of its financial indicators, including dividend payout, this year.

Thomas Singlehurst, media analyst at Citi Research, said in a note: "The group is clearly participating in the generally better media trends."

The sales results hint at a change in fortune for Publicis, whose performance last year was deeply affected by the 2014 decision to call off a proposed $35bn merger with long-time US rival Omnicom.

In December, fast-moving consumer goods group Procter & Gamble, the world's largest advertiser, said it was shifting almost all of its North American media planning and buying business from Publicis to the US group.

Mr Lévy, who is expected to step down next year, announced that same month an overhaul of Publicis's structure aimed at breaking down what he described as the "silos" within the organisation.

Banks

Popolare di Vicenza discounts €1.75bn offering

RACHEL SANDERSON — MILAN

Banca Popolare di Vicenza, the struggling regional lender at the heart of Italy's bank rescue deal, has priced its €1.75bn capital raising at as little at €0.1 per share — citing a lack of willing buyers among the big institutions.

The bank's board said yesterday it had set a price range of €0.1 to €3 for its new share offer because "in the process of pre-marketing with significant international and domestic investors, there were not sufficient indications of interest to determine a price range".

Popolare di Vicenza's fundraising, which was demanded by the European bank supervisor in Frankfurt to fill a capital hole, is due to run for two weeks, after which time the bank plans to list its shares on the stock exchange in Milan.

But last week a crisis meeting of Italy's top financiers and officials pulled together a rescue fund worth €4bn-€6bn, made up of equity contributions from the country's financial sector, amid fears that the Popolare di Vicenza capital raising would flop.

This fund, known as Atlas, is intended to head off concerns that a failed fundraising could trigger a wider panic that harms the capital ratio of its sole underwriter, UniCredit, which is Italy's largest bank by assets and its only globally significant financial institution.

Atlas has since joined UniCredit as an underwriter on the deal, and is expected to end up holding most of Popolare di Vicenza's shares.

Concerns about Popolare di Vicenza's capital levels have come amid greater scrutiny of the bad loans run up during Italy's crippling three-year recession.

Worries about non-performing loans have already hit bank share prices hard.

Italian banks have made €200bn of loans to borrowers now deemed insolvent, of which €85bn has not been written down on their balance sheets.

A broader measure of non-performing debt, which includes loans unlikely to be repaid in full, stands at €360bn, according to the Bank of Italy.

Technology

Verizon leads the crowded race for Yahoo

Private equity and media groups among potential bidders for internet group

JAMES FONTANELLA-KHAN AND MARY CHILDS — NEW YORK
HANNAH KUCHLER — SAN FRANCISCO

US telecoms group Verizon is the leading contender to take over Yahoo, but the internet company is also considering rival bids from more than a dozen suitors, including private equity groups TPG and Apollo, marketing company YP Holdings and the British publisher of the Daily Mail.

The first round of bids for part or whole of the dotcom pioneer, which has struggled to adapt to a fast-changing internet market, closed on Monday night.

Potential offers will help determine the value of Yahoo's core business, excluding its 15 per cent stake in Alibaba, the Chinese ecommerce group. Yahoo's share in Alibaba was worth about $30bn yesterday, while its overall market value was $35bn.

Analysts have valued the core business, which includes search and digital media units such as Tumblr, Yahoo Finance and Yahoo News, at between $1bn and $10bn, depending on which valuation metrics are used.

Some of the bidders have complained that the sale process has been disorderly. One person involved described it as "a total mess . . . just all over the place".

Despite Yahoo's lacklustre performance in recent years, several companies are convinced they can leverage the brand into a new era of growth.

Verizon has long been touted as the most likely buyer. People familiar with the matter confirmed that the telecoms group was a frontrunner but they stressed that it was not the only serious contender.

Other bidders, including the Daily Mail and General Trust and YP Holding, the online advertising company previously named Yellowpages.com, are interested in buying parts of Yahoo's core units.

These potential strategic buyers would be happy to work in co-ordination with a private equity group to buy the assets they find most useful for their existing operations.

Yahoo was due to report earnings after markets close yesterday.

Sales at the Silicon Valley company are forecast to fall 12.2 per cent to $1.1bn in the quarter, according to the average analyst estimate, with earnings forecast at 7 cents per share, just over half the previous year's figure.

Investors will be watching for any indication of what bids Yahoo has received and how seriously these are being considering.

Yahoo's board is pursuing a spin-off of the core company but has formed a separate committee to explore a sale following pressure from shareholders. The committee of independent board directors is being advised by Goldman Sachs, JPMorgan Chase and PJT Partners.

Shares in Yahoo, which have fallen 18 per cent in the past year, ticked up 0.3 per cent to $36.62 in morning trading in New York but were slightly down at lunchtime.

Yahoo declined to comment.

Health. Blood testing

Theranos battles to get ahead of criminal probe

Silicon Valley start-up says it is confident it can address investigators' concerns

DAVID CROW — NEW YORK

Federal prosecutors are investigating whether Theranos, the Californian blood-testing company, misled investors about the state of its technology

Just hours before it emerged that Theranos, the Silicon Valley blood-testing start-up, was under investigation by federal prosecutors and the US securities regulator, its founder appeared on national television to issue a mea culpa.

Elizabeth Holmes, 32, who dropped out of Stanford university in 2003 to set up Theranos, said she was "devastated" by its failings in an interview with NBC, which aired on Monday afternoon.

She was referring to an inspection report in November from CMS, the US Centers for Medicare and Medicaid Services. The regulator in charge of laboratory testing in the US found that Theranos's California facility had put patients' lives at risk by issuing inaccurate results.

The television interview was part of an orchestrated attempt to get ahead of another damaging revelation: federal prosecutors have opened a criminal probe into whether the company misled investors about the capabilities of its proprietary system, which can purportedly produce accurate results from just a few drops of blood.

After working in secret for a decade, Ms Holmes lifted the lid on the technology in 2013, and claimed that Theranos would be able to dispense with the needles and venous draws that have underpinned blood testing for decades.

Instead a few drops of blood would be collected in a tiny glass vial known as a nanotainer and the samples would be run through proprietary machines to generate accurate results, Ms Holmes said. She promised prices between 50 and 90 per cent lower than at established rivals such as Quest Diagnostics and the Laboratory Corporation of America.

Plaudits quickly followed and investors rushed to back the company, which attained a $9bn valuation in 2014 after a $400m funding round that made Ms Holmes a billionaire on paper through her 50 per cent stake.

At the time the company signed a high-profile agreement with Walgreen and proceeded to open more than 40 "wellness centres" in drugstores in Arizona, where legislators have changed the law so patients can order their own tests without first seeing a doctor.

According to two investors who have received subpoenas from the US attorney's office for the Northern District of California, the probe centres on whether Theranos misled investors over the capabilities of its technology during the 2014 capital raising and prior funding rounds.

The company said it "continues to work closely with regulators and is co-operating fully with all investigations".

Last November Theranos suspended the use of nanotainers for all but one of the more than 260 tests it offers. It is currently running the vast majority of diagnostics using commercially available machines.

In a memo sent to customers and partners, seen by the Financial Times, Theranos said it was under "investigations or inspections" by several regulators, including the attorney's office, the SEC and the CMS.

Last month regulators from the CMS proposed banning Ms Holmes and Sunny Balwani, the company's president, from the blood-testing industry for at least two years as part of a package of sanctions related to the violations they had identified in November.

The regulator has not yet made a final decision on whether to implement the ban.

Theranos, meanwhile, says it is confident that it can address investigators' concerns.

Walgreen executives, worried about the company's reputation, have instructed their lawyers to find a way of forcing Theranos to close the outlets in its stores, according to a person familiar with the matter.

The drugstore group was awaiting the final word on sanctions from the CMS but had resolved to terminate the partnership, the person said.

In the autumn the Food and Drug Administration also censured the company for using the nanotainer, which it deemed an "unapproved device", to collect patient blood.

A recent independent study found that the company was producing "systematically lower" cholesterol results than Quest and LabCorp.

Regulatory problems became public six months ago, shortly after the Wall Street Journal published a front-page story alleging that the company's technology was badly flawed.

The Financial Times subsequently reported that the group was employing two scientists with apparently inappropriate qualifications to run its labs.

Supporters of Theranos point out that it has survived previous investigations, including from health departments in Pennsylvania and Arizona and the FDA.

This month it appointed six medics to a beefed-up advisory committee to address concerns that its board lacked scientific experience and was dominated by ageing establishment figures, such as Henry Kissinger, the former US secretary of state.

But yesterday some commentators were already writing obituaries. Dr Eleftherios Diamandis, head of clinical biochemistry at Mount Sinai hospital in Toronto, said "negative publicity, based on facts, is going to bring this company down very quickly".

Jeffrey Sonnenfeld, a management professor at Yale, predicted that the company would "soon run its course, leaving a wake of foolish, famous investors in its wake".

$9bn	50%-90%
Group valuation in 2014 following a funding round worth $400m	Savings promised by Theranos based on prices of established rivals

Technology

Apple hires former Tesla top engineer for its electric car project

TIM BRADSHAW — SAN FRANCISCO

Apple has lured a former top Tesla engineer to its electric car team, according to people familiar with the move.

The recruitment of Chris Porritt, who left Aston Martin to become Tesla's vice-president of vehicle engineering three years ago, is a boost for the Apple car project after the departure of Steve Zadesky, the team's leader, this year.

Mr Porritt worked on the Model S and Model X at Tesla, which has been engaged in a war for talent with the iPhone maker for the past 18 months.

Apple, which has not acknowledged the existence of a car project, declined to comment. He left the electric car pioneer a few months ago, according to one person close to the company. His move was first reported by Electrek, an electric-car news website.

Tesla described Mr Porritt in May 2013 as a "world-class leader" and "outstanding engineer". He spent 16 years at Aston Martin and worked on the DB9, having been at Land Rover for a decade.

Traditional carmakers including Toyota, Ford and Renault-Nissan have opened Silicon Valley research and development centres.

Last year Apple poached engineers who had worked on self-driving systems at Tesla and Volkswagen, suggesting that any vehicle it produced would have a degree of autonomous capability. And it hired Doug Betts, a 25-year auto industry veteran who had worked at Fiat Chrysler.

But in January it emerged that Mr Zadesky was leaving Apple's car project for personal reasons. One person close to the team cautioned against seeing Mr Porritt as a direct replacement.

Tesla has fought back, recruiting former Apple staffers in security, sensors, chip design and materials. Last year Elon Musk, founder and chief executive, said Apple was known as the "Tesla graveyard" among his staff.

But the tech group's growing automotive team and resources suggest an increasingly serious initiative.

Since the Financial Times first reported on Apple's secret car R&D lab outside its Cupertino headquarters last year, the company is said to have been snapping up real estate in neighbouring Sunnyvale. Buildings in the area have been given names from Greek mythology, such as Zeus and Medusa, in a possible reference to the car initiative's code name, Project Titan, according to a report in the Silicon Valley Business Journal this month.

In 2014 a Sunnyvale city manager's blog post disclosed that Apple would be using a building there "as a testing facility for new electronic technologies that are integrated into high-end cars" and as an "auto testing centre".

Apple has previously released a system called Carplay for integrating the iPhone into a dashboard.

Reports in the German media this week again linked Apple with Magna Steyr, the automotive contract manufacturer that has been working with BMW to produce versions of the Mini. This partnership was set to end this year, noted Apple-watcher Neil Cybart in his newsletter Above Avalon.

Pharmaceuticals

Roche upbeat on new cancer drug prospects

ANDREW WARD
PHARMACEUTICALS CORRESPONDENT

Roche said its efforts to catch up with Merck and Bristol-Myers Squibb in cancer immunotherapies was on track as fresh data reinforced excitement over the new generation of tumour-fighting drugs.

The Swiss group yesterday highlighted the potential of its atezolizumab medicine, which has recently won fast-track reviews from the US Food and Drug Administration for its use in bladder and lung cancers — paving the way for potential approvals this year.

Daniel O'Day, head of Roche's pharmaceuticals division, said that he was "very optimistic" about prospects in immuno-oncology, which involves drugs that help the immune system kill cancer cells. These immunotherapies are forecast by analysts to generate tens of billions of dollars a year in sales within the next decade.

His comments came as Roche announced that sales rose 5 per cent to SFr12.4bn ($13bn) in the first quarter, slightly ahead of analysts' expectations.

Immunotherapy is at the heart of efforts to refresh Roche's business as older products, such as its Lucentis eye drug, lose momentum while others, such as its Herceptin breast cancer medicine, face looming competition from copycat "biosimilar" drugs.

Merck and BMS of the US already have immunotherapies on the market, but Roche says the greater breadth of its oncology portfolio will give it an advantage in the long-run. It has nine immunotherapies in development and 50 separate clinical studies under way.

Data issued at the annual meeting of the American Association for Cancer Research in New Orleans this week has provided further evidence for those who see immuno-oncology as the most important breakthrough against the disease for decades — and a welcome fresh source of growth for the pharmaceuticals industry.

One-third of people with advanced melanoma treated in a study of BMS's Opdivo immunotherapy have survived for at least five years, researchers said — double the average proportion for people with that condition.

Andrew Baum, analyst at Citigroup, said the data had resolved any remaining doubts about the durable effect of so-called PD-1 drugs, such as Opdivo and Roche's atezolizumab, which work by disabling the "checkpoint" in cancer cells that normally blocks the immune system from attacking.

Much of the industry's focus is now on combining immunotherapies with other cancer drugs in an effort to extend the benefits to the two-thirds of patients who do not respond to the first generation of treatments.

A study published yesterday showed 69 per cent of patients with advanced melanoma treated with Opdivo and another BMS immunotherapy called Yervoy were alive after two years, and a fifth had no signs of tumours. However, half suffered serious side-effects.

Mr O'Day said approval for atezolizumab in bladder cancer would open a new front in the immuno-oncology market, which has until now been focused mainly on melanoma and non-small cell lung cancer. "For the past 30 years there has not been anything new for patients with advanced bladder cancer," he said. "We are looking forward to providing that opportunity."

Roche is also optimistic about prospects for its new ocrelizumab treatment for multiple sclerosis, which is on course to hit the market in the next year.

Airlines

Malaysia Airlines loses chief

JEEVAN VASAGAR — SINGAPORE

The chief executive of Malaysia Airlines, Christoph Mueller — brought in to turn the business round after two aviation disasters — is to step down in September long before his three-year contract expires.

Yesterday Mr Mueller, who took the helm at the airline last March, said he was leaving for personal reasons. But a person familiar with the situation said the German chief executive — the first non-Malaysian to hold the post — had come under intense pressure from stakeholders as he tried to transform the struggling national flag carrier.

He has cut 6,000 jobs, slashed pay and focused on Asia, moving away from the former strategy of linking European cities to Australia.

Mr Mueller urged rebranding after the disasters of 2014. But the airline's sole shareholder, Khazanah — Malaysia's sovereign wealth fund — disagreed.

Shukor Yusof of Endau Analytics, a Malaysian aviation consultancy, said the airline needed to be free from state interference if it was to succeed on commercial terms. "It's a disgrace," he said. "The best turnaround specialist in the aviation business is leaving the company. Whoever replaces Christoph — whether a Malaysian or a foreigner — needs a free hand."

Mr Mueller appeared to have put the toughest parts of the project behind him. In an interview this month he said the company had posted a profit in February — its first positive monthly result in years. Last summer he had said the airline was on track to return to annual profitability by 2018, and had finished laying off employees.

In a statement yesterday Mr Mueller said: "I am proud of what we have achieved as a team in such a short time."

Malaysia Airlines said he had asked to step down because of "changing personal circumstances" but intended to stay on as a non-executive director after serving his six-month notice period.

The lossmaking group suffered a sustained decline in passenger demand after the disappearance of flight MH370 over the southern Indian Ocean in March 2014 and the shooting down of MH17 over Ukraine four months later.

At Malaysia Airlines Mr Mueller, who is credited with having transformed Aer Lingus, cut routes to Frankfurt, Brisbane and Istanbul.

Retail & consumer

Japan's Seven & i appoints activist-backed president

Head of 7-Eleven division wins conglomerate's top job in victory for Loeb

KANA INAGAKI — TOKYO

Seven & i has named an executive backed by US activist Daniel Loeb as president of the Japanese conglomerate, two weeks after a boardroom spat led to the departure of its chairman.

Analysts said that the management changes announced yesterday marked a victory for shareholder activists and Prime Minister Shinzo Abe's campaign to improve corporate governance.

But the succession dispute at the retail conglomerate behind the 7-Eleven convenience store chain has exposed the challenges that many Japanese companies face in finding new talent to replace ageing chief executives.

The Seven & i board chose 58-year-old Ryuichi Isaka, president of its core 7-Eleven Japan unit, to run the conglomerate, in line with the selection made by its nomination committee last week. The appointment is effective from May 26.

The management reshuffle came after Toshifumi Suzuki, the 83-year-old chairman and chief executive of Seven & i, resigned abruptly on April 7 having failed to win the board's backing to remove Mr Isaka.

The ousting attempt by Mr Suzuki, who has overseen the conglomerate for nearly 25 years, came under fire from the group's founding family members and external directors who had backed Mr Isaka due to his role in strengthening the convenience store operations.

The boardroom clash was thrust into the spotlight after Third Point, the hedge fund run by Mr Loeb, wrote to Seven & i over concerns that Mr Suzuki was seeking to replace Mr Isaka in an effort to position his son as his successor. Mr Suzuki has denied the accusation of nepotism.

In a recent report, Daiwa Securities analyst Kazunori Tsuda said the board's rejection of Mr Suzuki's proposal to remove Mr Isaka was evidence that governance by the nomination committee and outside directors was effectual.

Mr Tsuda said it was a defining moment "not only for Seven & i but for the history of governance at Japanese businesses".

The top-level changes have not, however, eliminated concerns about a leadership vacuum after the exit of a charismatic executive who had maintained a firm grip over the retail empire.

While the 15-member board, including four external directors, had agreed on the choice of Mr Isaka as group president, Seven & i left the chairman position vacant and scrapped the chief executive role.

Ryuichi Isaka: president of 7-Eleven Japan will now run the conglomerate

Until the recent succession battle, Mr Suzuki had been considered one of the most respected business leaders in Japan and a pioneer in the convenience store sector. With innovative marketing and product development strategies, 7-Eleven has expanded its operation to more than 18,000 stores in Japan.

Analysts say the challenge is whether Mr Isaka can respond to calls from Mr Loeb and other investors to take more drastic measures to fix its struggling supermarket and retail divisions.

Media. Video streaming

Amazon and Netflix lock horns in battle for the living room

As the two US companies compete for subscribers, new rivals appear on weekly basis

MATTHEW GARRAHAN — NEW YORK

The battle for the living room is hotting up. This week Amazon fired a shot across the bows of Netflix with the launch of its Prime digital video package as a standalone subscription in the US, untethering it from its express delivery service as it bids to attract more customers.

A day later, Reed Hastings, Netflix's chief executive, said his company was on course to hit 100m subscribers "sometime" next year.

The two companies are duking it out to capture television audiences that are moving away from so-called "linear" television — or tuning in at a pre-set time — in favour of digitally streamed, on-demand viewing. Both have invested vast sums to produce and license original content. Amazon spent an estimated $3bn last year on movies and shows such as *Transparent*, while Netflix is on course to spend $6bn in 2016, building on demand for series like *Making a Murderer*, *Narcos* and *Daredevil*.

The question is whether they can each prosper in an increasingly competitive environment in which new digital subscription services are launching on a near weekly basis — and where established broadcasters have large, built-in audiences.

In Europe, for example, "cord-cutting" is not as prevalent as in the US, and operators such as Sky, which has 21.5m customers across the UK, Ireland, Austria, Italy and Germany, has a customer base already well-served with on-demand content.

Mr Hastings hinted that digital groups can thrive in a more competitive environment. When asked about Amazon's standalone subscription on the company's first-quarter earnings call, he said it was evidence that "growth in the internet TV market" was "displacing linear TV". Increased competition was "all part of the natural evolution from linear TV to internet TV", he added.

Netflix has a considerable head start on its rival having begun its international video push four years ago. But its path to hoped-for global success is littered with potential stumbling blocks.

In January it turned its service on simultaneously in 130 countries, a move that helped add 6.74m new subscribers in the first quarter, of which 4.6m came from outside the US. The international push helped lift its total subscribers above 81m.

However, Netflix expects to add fewer subscribers in the second quarter than in the same period a year ago, at its launch in Australia and New Zealand. It is forecasting 2m new international subscribers for the second quarter, compared with 2.37m a year ago.

This admission spooked investors and sparked a 10 per cent fall in Netflix shares on Monday.

Michael Nathanson, an analyst with MoffettNathanson, wrote in a research note: "International subscriber guidance was considerably lower than the most bearish forecasts." Yet despite occasional periods of potentially slower growth, Netflix is still expected to grow: Enders Analysis said it would double its subscriber base to 150m by 2020.

Netflix has sacrificed earnings growth for investments in original content, generating net income of just $27.7m in the first quarter on revenues of close to $2bn.

Investors have been willing to accept such a low margin as Netflix has pursued international growth. At some point, however, it will have to make its investments pay.

"Netflix has to move quickly along its tightrope to stay ahead of the growing chasing pack of other online subscription video on demand services," Enders analysts Toby Syfret and Alex Fenton wrote. "The question is whether it can get to the end and reach the promised land without falling on the way."

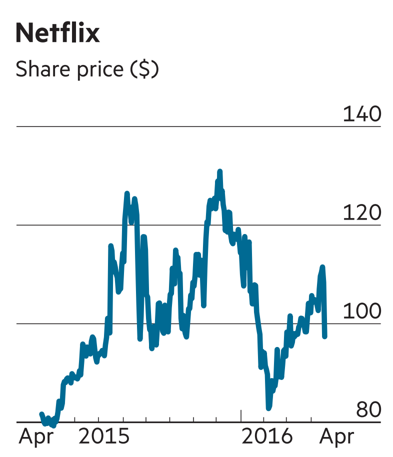
In the US, NBC, Showtime, Starz and HBO are among the channels to have launched standalone video subscription services that are available without a cable or satellite television subscription. They are all in the market for original content, which has increased the pressure on Netflix but been a boon for Hollywood studios and other producers.

Amazon outbid Netflix and other broadcasters to pay an eye-watering $250m to sign the three presenters of *Top Gear*, and has a enlisted Woody Allen to write a comedy series. Netflix will this year premiere *The Crown*, a series about the life of Queen Elizabeth II, outbidding UK broadcasters for the rights. This year also marks the start of its deal to air first-run Walt Disney movies in the US, making it the home of new release films after they have screened in cinemas and been released on DVD, such as the new adaptation of *The Jungle Book* and the upcoming *Captain America: Civil War*, as well as older titles.

These investments should ensure Netflix keeps adding subscribers. But Amazon and the rest of the chasing pack are snapping at its heels.

See Lex

Quest for viewers: Netflix has secured the rights for new Disney films including 'The Jungle Book' while channels also spend large sums on original content



Source: Thomson Reuters Datastream

Prime mover
Retailer seeks to draw in lower-income customers

In Amazon's most mature markets, Prime has become its secret weapon. Prime members in the US, who pay $99 annually for the service, spend nearly twice as much per year as non-Prime members.

The services included in Prime include unlimited video and music and expedited shipping.

Estimates put Prime membership at 25-40 per cent of US households.

However, by introducing a new $10.99 monthly pricing option last weekend, Amazon is trying to expand Prime to lower-income customers who might otherwise balk at the annual fee.

"Amazon Prime is likely somewhat saturated for above-income households in the US," wrote Ben Schachter, an analyst at Macquarie, in a client note.

He expects that the company "will continue to experiment with ways to attract more lower-than-average-income households".

This demographic is a key customer base for Amazon's rival Walmart, whose stores have been struggling to find growth.

Walmart started testing its own Prime-like shipping subscription last year, but the service has not been rolled out. *Leslie Hook*

Legal Notices

SAirGroup AG in debt restructuring liquidation / publication of provisional distribution list for the fourth interim payment

The provisional distribution list for the fourth interim payment in the debt restructuring proceedings with assignment of assets concerning **SAirGroup AG in debt restructuring liquidation**, Hirschengraben 84, 8001 Zürich, will be open to inspection by the creditors concerned between 20 April 2016 and 2 May 2016 at the offices of the liquidator, Karl Wüthrich, attorney-at-law, Wenger Plattner, Goldbach-Center, Seestrasse 39, 8700 Küsnacht. For inspection, please call the hotline on +41 (0)43 222 38 50 to arrange an appointment.

Appeals against the provisional distribution list must be lodged with the District Court of Zürich, supervisory authority for debt enforcement and bankruptcy, Wengistrasse 30, P.O. Box, 8026 Zürich, within ten (10) days of the list's publication, i.e. by 2 May 2016 (date of postmark of a Swiss post office). If no appeals are lodged, the fourth interim payment will be made as provided for in the provisional distribution list.

Bondholders of SAirGroup AG and beneficiaries of SAirGroup AG's guarantees for the benefit of Euro-bonds issued by SAirGroup Finance (NL) B.V. and SAirGroup Finance (USA) Inc., who have not yet registered their claims with SAirGroup AG, find information on claiming the fourth interim payment on the liquidator's website (www.liquidator-swissair.ch, heading "Bonds").

Küsnacht, 20 April 2016

SAirGroup AG in debt restructuring liquidation

The Liquidator:
Karl Wüthrich

www.liquidator-swissair.ch

SAirGroup AG in debt restructuring liquidation / publication of supplement no. 4 to schedule of claims

In the debt restructuring proceedings with the assignment of assets concerning **SAirGroup AG in debt restructuring liquidation**, Hirschengraben 84, 8001 Zürich, the creditors concerned will be able to inspect the supplement no. 4 to the schedule of claims until 10 May 2016 at the offices of the liquidator, Karl Wüthrich, attorney-at-law, Wenger Plattner, Seestrasse 39, Goldbach Center, 8700 Küsnacht. For inspection creditors are asked to call the hotline on +41 (0)43 222 38 50 to arrange an appointment.

Actions to contest the supplement no. 4 to the schedule of claims must be lodged with the single judge court at the District Court of Zürich, Wengistrasse 30, P.O. Box, 8026 Zürich, within 20 days of the official notice of the publication in the Swiss Official Gazette of Commerce dated 20 April 2016. The 20-day period will thus run until 10 May 2016 (date of postmark of a Swiss post office). If no actions are lodged, the supplement no. 4 to the schedule of claims will become final.

Küsnacht, 20 April 2016

SAirGroup AG in debt restructuring liquidation

The Liquidator:
Karl Wüthrich

www.liquidator-swissair.ch

Notice of Annual General Meeting

J.P.Morgan Asset Management

JPMorgan Investment Funds

The meeting will be held at the location and time stated in the right-hand column. All appointments being voted on are for terms that end at the next annual general meeting.

Agenda for Meeting and Shareholder Vote

1. Presentation of the report from Auditors and Board for the past fiscal year.
2. Should shareholders adopt the Audited Annual Report for the past fiscal year?
3. Should shareholders agree to discharge the Board for the performance of its duties for the past fiscal year?
4. Should shareholders approve the Directors' fees?
5. Should the following Directors be reappointed to the Board?
   Jacques Elvinger,Jean Frijns, John Li, Massimo Greco, Iain Saunders, Peter Schwicht, Daniel Watkins
6. Should shareholders re-appoint PricewaterhouseCoopers Société cooperative as its Auditors?
7. Should shareholders approve the payment of any distributions shown in the Audited Annual Report for the past fiscal year?

To vote by proxy, use the proxy form at jpmorganassetmanagement.com/extra. Your form must arrive at the registered office, via post or fax, by 1800 CET on Wednesday, 27 April 2016.

To vote in person, attend the meeting in person.

THE MEETING
Location Registered office of the Fund (see below)
Date and time Friday, 29 April 2016 at 12:00 CET
Quorum None required
Voting Agenda items will be resolved by a simple majority of the votes cast

THE FUND
Name JPMorgan Investment Funds
Legal form SICAV - **Fund type** UCITS
Auditors PricewaterhouseCoopers Société coopérative
Registered office 6, route de Trèves
L-2633 Senningerberg, Luxembourg
Fax +352 3410 8000
Registration number (RCS Luxembourg) B 49 663
Past fiscal year 12 months ended 31 December 2015

Notice of Annual General Meeting

J.P.Morgan Asset Management

JPMorgan Liquidity Funds

The meeting will be held at the location and time stated in the right-hand column. All appointments being voted on are for terms that end at the next annual general meeting.

Agenda for Meeting and Shareholder Vote

1. Presentation of the report from Auditors and Board for the past fiscal year.
2. Should shareholders adopt the Audited Annual Report for the past fiscal year?
3. Should shareholders agree to discharge the Board for the performance of its duties for the past fiscal year?
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To vote by proxy, use the proxy form at jpmorganassetmanagement.com/extra. Your form must arrive at the registered office, via post or fax, by 1800 CET on Wednesday, 27 April 2016.

To vote in person, attend the meeting in person.

THE MEETING
Location Registered office of the Fund (see below)
Date and time Friday, 29 April 2016 at 11:00 CET
Quorum None required
Voting Agenda items will be resolved by a simple majority of the votes cast

THE FUND
Name JPMorgan Liquidity Funds
Legal form SICAV - **Fund type** UCITS
Auditors PricewaterhouseCoopers Société coopérative
Registered office 6, route de Trèves
L-2633 Senningerberg, Luxembourg
Fax +352 3410 8000
Registration number (RCS Luxembourg) B 25 148
Past fiscal year 12 months ended 30 November 2015

UK COMPANIES

Travel & leisure

Pret A Manger serves up double-digit sales growth

Sandwich chain's bet on more vegetarian options reaps appetising returns

PAUL McCLEAN

Booming avocado sales and rising demand for vegetarian food helped sandwich chain Pret A Manger to deliver tasty double-digit growth in sales last year.

The chain, which is owned by private equity group Bridgepoint, said avocado was its fastest-growing ingredient, with customers eating 5m in 2015. Its best-selling item was a vegetarian Beets, Squash & Feta SuperBowl, selling 17,000 a week and outperforming both chicken and salmon options.

Overall sales were up 13.9 per cent to £676.2m, while earnings before interest, tax, depreciation and amortisation rose 14.5 per cent to £84.3m in the 52 weeks to December 31 2015. Like-for-like sales rose 7.5 per cent year on year.

"Last year thousands of customers told us they were trying to eat less meat," said Clive Schlee, Pret A Manger's chief executive. "This year we have challenged ourselves to increase our vegetarian options in all shops, as well as opening a veggie-only pop-up shop to learn more from our customers.

"People are becoming more aware about the health and environmental aspects around vegetarianism. We've always thought that if vegetarian food was more attractive and more available, more people would eat it," he said. "We're not getting rid of our meat options, we're simply saying, here's an alternative."

While the new minimum wage has seen companies cut employee benefits — with Caffè Nero staff losing their free lunch, for example — Mr Schlee said no such cuts would be made at Pret.

"I'm very conscious about how hard our staff work — how cheerful they are and how motivated they are when buttering the bread — all that is very important, and you simply can't afford to alienate your staff. Under no circumstances will we risk that — we haven't cut any of our bonuses."

Pret opened 23 new shops in the UK last year, and Mr Schlee denied that the sandwich chain was close to saturation. "It's easy to assume we're everywhere due to our presence in London, but in actual fact we have about half as many shops as the big coffee shops and pizza chains," he said. "We're now building outside of London, and focusing on university towns, such as Exeter, Nottingham, Durham, Manchester and Birmingham."

International sales were strong, with like-for-like sales in the US, Pret's fastest-growing market, up 13.8 per cent.

Last year, Pret began serving dinners with wine, jazz and "really posh olives" at one of its central London branches. Mr Schlee said that despite the popularity of the scheme, the company had concluded "that Pret works best when it sticks to its current format of service".

Energy. Renewables

Drax challenges ministers with offer to drop coal

Chief says power generator is ready to switch to wood by 2020 if subsidies are awarded

PILITA CLARK
ENVIRONMENT CORRESPONDENT

Heat of the moment

Burning question: Drax wants to convert its coal boilers to use biomass, or wood pellets, as seen above at its generating station in North Yorkshire

The head of the UK's largest power station has thrown down the gauntlet to government ministers with an offer to stop using climate-warming coal in as little as three years in return for more green energy subsidies.

Dorothy Thompson, chief executive of the Drax group, told the Financial Times the company could easily beat the 2025 deadline for phasing out coal power that ministers set in November, by converting more boilers at its huge North Yorkshire power plant so they burn wood pellets instead.

"We have project plans that we could execute within three years, so you could take our coal units off the system by 2020 if not before," Ms Thompson said in an interview ahead of Drax's annual shareholder meeting today.

The company has already turned its 42-year-old Selby power station into one of the world's biggest renewable generators over the past four years, by upgrading nearly half its six coal-fired boilers to burn wood pellets, or biomass, mostly imported from the US.

But it has only done this after receiving subsidies and other support worth £451.8m in 2015, or 17 per cent of revenues at the power plant, which supplies about 8 per cent of the UK's electricity.

It is a corporate transformation that has not been for the faint-hearted. Exposed to endless shifts in government green energy policies, Drax's daily share price has tumbled sharply at least five times in the past two years, on one occasion by as much as 28 per cent in a day. That was on the day of last year's July Budget, when a climate change tax was applied to renewable generators, a step Ms Thompson likens to "putting an alcohol tax on apple juice".

> Overall, the company's share price has fallen 60 per cent over the past two years

The climate change tax reduced Drax's earnings before interest, tax, depreciation and amortisation by an estimated £30m in 2015 and is expected to have double the impact this year.

Drax has also been hit by lower wholesale power prices — which fell by about 30 per cent in 2015 — damping gross profits at its Selby station, which sells electricity into the market.

Overall, Drax's share price has fallen 60 per cent over the past two years, while pre-tax profits dropped from £166m in 2014 to £59m last year.

The company confirmed on Monday that it examined several financing options last year to boost its biomass plans and "optimise its balance sheet".

Drax abandoned the effort after finding a high volume of deals being attempted ahead of the May UK election and other market dislocation, it said, adding that it was right to test the market "but not something that we needed to do".

But the question of future subsidies remains vital. Ms Thompson says switching Drax's remaining three coal boilers to burn wood would be impossible unless the company received more of a newer type of subsidy structured as a contract for difference, or CFD, that guarantees long-term power prices for renewable power companies.

Drax was awarded one CFD for its third boiler conversion two years ago but is still awaiting state aid approval for it, a delay Ms Thompson says is "shocking".

Approval is widely expected because Brussels waved through support in December for a coal-to-wood pellet conversion at the smaller Lynemouth power station. A positive decision could make a £70m difference to Drax's annual revenues from 2017, say analysts at Jefferies. The government is due to offer three more batches of CFD contracts over the next four years but these are expected to go to offshore wind farms, not big biomass generators.

Asked if Drax could expect more subsidies, the energy department says: "We are already supporting over 5 gigawatts of biomass technologies, providing nearly a quarter of our renewable electricity."

Ministers want "a sensible level of support" to keep "bills as low as possible for hardworking families and businesses", he adds.

The government is also facing pressure from environmental activists who argue that burning wood pellets is not as green as Drax claims and that its hunger for imported wood is threatening forests in the US. Drax rejects these claims, saying its switch to wood cuts its carbon emissions by more than 80 per cent compared with coal and does not harm forests.

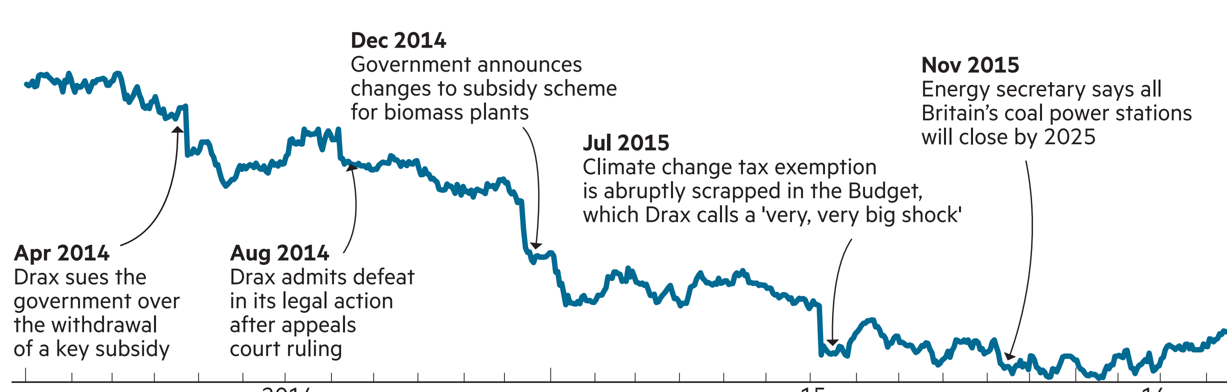
But the company faces other tests as ministers consider how to close the eight coal stations selling power to the market, which together supply more than 19 per cent of the UK's electricity.

Ms Thompson says it is not clear if the government will close down all the coal stations in one go or shut them progressively, which could cause problems.

"You can't say, 'well, I'm going to close this one and not that one'. There are competition issues that will stop you doing that," she says.

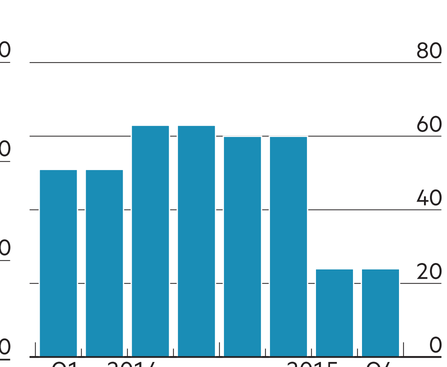
Steep falls at Drax

Share price (pence)



Drax profits

Earnings before interest, tax, depreciation and amortisation (£m)



Sources Thomson Reuters Datastream; S&P Capital IQ

Property

Zoopla to buy supplier of software for estate agents

JUDITH EVANS

Zoopla, the internet property portal, is to buy the market leader in estate agency software for £75m as it battles with Rightmove and OnTheMarket for the loyalty of agents.

The acquisition of Property Software Group would link Zoopla with a back-office system used by 8,000 branches, which might then join its portal, analysts said.

Alex Chesterman, founder and chief executive, said: "For those who want it, we will provide a complete end-to-end solution."

Zoopla and Rightmove, its larger listed rival, are among the UK's most popular websites but have faced competition during the past year from OnTheMarket, set up by a consortium of estate agents to break their stranglehold on an area that has become crucial to home sales in the UK.

About 2,000 agents ditched Zoopla for OnTheMarket, which allows members to list on only one other big portal. But Zoopla's numbers have been rising again, while OnTheMarket faces a mutiny from a group of agents unhappy with its service and fees.

Rightmove has started providing software, "cementing the links with the agents' back office and IT systems", according to Anthony Codling, analyst at Jefferies.

But with the purchase of PSG, Zoopla appears to have leapfrogged its rival. About 5,000 of the software company's customers do not use Zoopla, offering a chance of bundled selling.

Zoopla said it expected full-year results "at the higher end of expectations" as falling energy prices boosted uSwitch, the price comparison website it bought last year.

While Zoopla, whose main portal is used by 16,700 agents, has made acquisitions, Rightmove, used by 19,700, has grown organically. OnTheMarket, launched in January 2015, is used by about 6,000 agents.

PSG — backed by LDC, the private equity arm of Lloyds — generated revenues of £15.9m in the year to the end of March, and boasts a customer retention rate of more than 97 per cent.

The acquisition, conditional on Financial Conduct Authority approval, will be funded by existing cash and a £50m extension of its debt facility.

Mark Goddard, PSG chief executive, will become head of Zoopla's property services division.

Mining

Polymetal on the lookout for further deals

JAMES WILSON

Polymetal International has said it is open to more acquisitions after its second deal this year to increase gold production in central Asia.

The UK-listed precious metals miner is on the verge of starting construction at its large new mine in Kazakhstan, and has said it will consider extending its portfolio after completing that $350m project.

"We probably have a bit of appetite for longer-dated growth options — say to be built in 2019 or 2020 — that would be interesting to provide a longer-term pipeline," said Vitaly Nesis, chief executive. "We are OK for 2019-20, and then we have a gap."

Shares in Polymetal have increased 20 per cent this year — helped by the rising gold price — giving it a market capitalisation of £2.9bn. The company has been one of the most active acquirers of gold assets in recent months, spending relatively small sums to extend its focus in Russia and beyond.

The gold and silver producer bought the Kapan gold mine in Armenia from Dundee Precious Metals in March, and this month agreed to buy Glencore's Komarovskoye deposit in Kazakhstan, where it already operates its only mine outside Russia.

The acquisitions, for combined upfront payments of $125m, are likely to add to Polymetal's output this year.

Growth appetite: Vitaly Nesis, chief executive, says Polymetal has a pipeline 'gap' after 2019-20

The miner said it would review 2016 production guidance when the deals completed in the coming months.

Polymetal intends to start building Kyzyl, another mine in Kazakhstan, next month. The project, which was acquired in 2014 and should launch in 2018, has added 50 per cent to the group's ore reserves. It is expected to propel group output from 1.2m ounces of gold this year to 1.6m oz in 2020.

Mr Nesis said Polymetal was close to agreement with a Russian bank — either VTB or Sberbank — to provide $280m to $300m of project finance for Kyzyl.

Polymetal struck a deal in December with Polyus Gold for potential joint development of Nezhdaninskoye, Russia's fourth-largest gold deposit.

Mr Nesis said Nezhdaninskoye could be one of the next mines Polymetal was involved in constructing and would be "relatively capital-light".

Russian gold miners have been supported by big cost reductions as the rouble has fallen. But they have been hit by the perception of greater political risk in the past two years since relations between Moscow and the west soured over the crisis in Ukraine.

Mr Nesis said the perception of Russian risk was "starting to shift" with "sentiment creeping back up". Borrowing costs for Polymetal had fallen and there were signs of wider investor interest, he added.

"Our pitch is that we have been stable performers, our operational performance has been very solid," he said.

Capital markets

Brexit hedgers are wasting their money, says bond guru

The UK is not going to vote to leave the EU, according to Jeffrey Gundlach, the influential bond investor.

The founder of DoubleLine Capital, which manages more than $84bn of assets, adds that any investors who are hedging against such an outcome are wasting their money.

In a freewheeling interview at his group's Los Angeles headquarters, Mr Gundlach expounds on the UK and US political landscapes and negative interest rates.

Brexit
"It's not going to happen," he says definitively. "People like to complain, they like to say what's wrong. But when it comes down to actually pulling the lever they sit there and they say, 'What exactly am I doing here? What is going to happen?'

"The devil you know is better than the devil you don't know. Look at what happened with Scotland. People aren't going to pull a lever for Brexit, so I don't even think that's worth

Jeffrey Gundlach, founder of DoubleLine

considering." The cost of protection against a fall in sterling has risen towards the high of 2010 after the UK election resulted in a coalition government. Mr Gundlach says investors are being foolish pushing up the cost of such insurance.

"Remember all the tail risk insurance that pension plans put on in 2009? What a waste of money."

It will prove the same with Brexit insurance, he says. "The odds are less than what people have embedded into their protection so it's likely to lose money.

"And nobody knows what would happen under a Brexit anyway. So often things go the opposite way from what people expect. Maybe your hedge is actually in the anti-hedge."

Donald Trump
Mr Gundlach says: "Trump is the unconstrained bond fund of the political arena."

Managers of this newly popular kind of fund do not have to adhere to a bond market benchmark.

"[They] became popular because traditional alternatives were deemed to be unattractive. With an unconstrained bond fund I have no idea what I'm going to get but it's better than getting something I know I don't like."

Mr Gundlach recalls how he told traders on the day Mr Trump announced his candidacy: "The greatest long in the entire world is Trump's odds to win the presidency."

DoubleLine cannot play the political betting market, but Mr Gundlach predicts that Mr Trump will win the White House if his nomination is confirmed at the Republican convention — and defence stocks would then do well.

"Trump is very squishy on ideas and offers contradictory ideas week to week. But two things he has said clearly and consistently are build a wall and build the defence.

"I think Trump would have much higher deficit. He talks about leaving social security completely alone, cutting taxes and spending a lot of money. Donald Trump's a debt guy; he knows about borrowing a lot of money."

Negative rates
Expectations of low interest rates are so embedded in financial market assumptions that it smacks of "complacency", Mr Gundlach says.

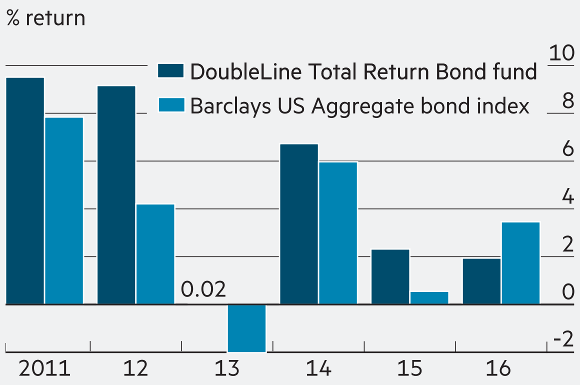
If it becomes clear that the Federal Reserve will not follow other central banks in considering negative rates for the next downturn, investors could get burnt.

"The odds are very low that the US will go to negative interest rates, not based on some great economic growth belief but on their failure in Europe and Japan," he says.

"Those central banks will have to get out of it, but what is the path out? Raising interest rates against the global economic backdrop seems hard to justify."

Terrorism
The one thing that could shake Mr Gundlach's scepticism over Brexit is if more terrorism inflames concerns about the free movement of people in the EU. *Stephen Foley*

Gundlach v the index
% return



Source: Morningstar

Capital markets

Argentina returns with $16bn debt sale

Holdout creditors will be paid in cash as Buenos Aires ends conflict

ELAINE MOORE — LONDON
BENEDICT MANDER — BUENOS AIRES
ERIC PLATT — NEW YORK

Argentina was welcomed back to international capital markets yesterday with the largest sale of debt by any developing nation and one of the biggest order books ever recorded.

Fifteen years after it was locked out of markets as the result of debt default and conflict with creditors, it returned with a $16.5bn sale of dollar-denominated debt, upsized from a planned $15bn as demand totalled close to $70bn.

Investors said they were impressed by Argentina's new investor-friendly government, and the story of an emerging market nation with potential for economic improvement at a time when others are mired in recession and scandal.

Claudia Calich, fund manager at M&G, called the sale a positive step in normalising Argentina's financial relations with the international markets.

"In order for the macroeconomic outlook to improve, it is important that foreign direct investment picks up as a result," she said.

Alfonso Prat-Gay, Argentina's finance minister, said demand was the highest for any emerging market debt issue. He also clarified that the government was not planning to issue any more debt this year, despite uncertainties generated by the complicated economic inheritance left by the previous administration.

Part of the proceeds of the sale will be used to settle a dispute with investors who own debt on which Argentina defaulted and who fought for full repayment until a deal was reached this year. Argentina will pay the holdouts in cash on Friday. "This is just the starting point . . . to begin on the road to achieving zero poverty," Mr Prat-Gay said.

A breakdown of the sale revealed that benchmark 10-year bond was the most popular offered, allowing the country to tighten the yield from 8 per cent to 7 per cent. Investors who bought 30-year bonds will earn 8 per cent a year, rather than 8.85 per cent as initially indicated while five-year bonds came with a yield of 6.875 per cent.

Three-year Argentine bonds, which were only recently added to the country's sale plan, attracted fewer bids and were sold with a yield of 6.25 per cent.

Ahead of the deal being priced yesterday, the scale of the order book provoked a scramble for a piece of the transaction in the so-called grey market — where investors can buy and sell the debt before it is officially issued.

Bids on the 30-year bond reached 3 points above its yet to be decided issue price. Bids on the 10-year bond hit 2 points above its issue price.

Traders said the grey market activity implied the bonds would rally in price once they were allocated.

The bonds have been issued under New York law, which means investors have recourse to international courts if the country does not pay them back. But clauses within the bonds have been altered to clarify that equal treatment of creditors does not mean equal ratable payment, correcting the confusion that enabled holdouts to successfully sue Argentina in the first place.

Additional reporting by Lucinda Elliott

$70bn
The demand as Argentina returned after a long absence caused by debt default and conflict with creditors

7%
Yield offered in the 10-year bond, the most popular in the largest sale of debt by any developing nation

Analysis. Capital markets

Ultra looks beyond gap in Treasury futures

Strong debut of CME's new contract highlights increasing dislocation in post-crisis era

PHILIP STAFFORD AND JOE RENNISON

A futures contract at CME Group that tracks the world's primary government bond benchmark has flourished since its launch in January as investors adjust to a world of low interest rates and hefty capital costs for holding bonds.

The new contract from CME, the world's largest futures market, has "gone like a bat out of hell", according to a senior executive.

In the first seven weeks of its life, the "10-year Ultra Treasury note" contract, which tracks the US government security that is used as a benchmark all over the world, has notched up more than 1m trades.

The success of the contract — the fastest-growing product in the CME's 148-year history — reflects a shift in the structure of the US interest rate market, between cash and futures products, following post-financial crisis regulation.

A longstanding 10-year Treasury futures listed contract at the CME remains popular, so the market is not simply switching to the Ultra.

The ultimate success of the new contract will rest on broader market participation from asset managers, which tend to wait and see before committing to a product.

"As liquidity grows, there will be more pull to switch to the Ultra 10-year," says James Ong, a derivatives strategist at Invesco Fixed Income. "We would like to see liquidity grow. As it does I think we will be using it more frequently."

The Ultra fills an important gap for investors and traders in Treasury futures. Such derivative trades are often closed out near the expiry of the contract by finding an old cash Treasury security and delivering that to the other party. The Ultra contract provides greater flexibility in settling futures trades in the current climate of low interest rates.

In trading, however, the crucial element is cost, particularly in the current regulatory climate as the effects of banking and market reforms resonate for investors.

With banks facing higher capital charges for trading over-the-counter derivatives, the use of futures offers a cheaper alternative, according to a report by Greenwich Associates, a capital markets consultancy. Using futures also appeals greatly to high-frequency traders, who have become bigger participants in the US bond market.

"Financing is a really, really important part of the ecosystem that has been a little bit overlooked," says Paul Hamill, global head of fixed income, currencies and commodities at Citadel Securities. "And that is where we will almost certainly see innovation. [Financing is] where many investors are substantially more focused."

The concern over financing is being exacerbated by a breakdown in the industry's fundamental tool: market activity that links Treasury bonds and OTC derivatives, notably interest rate swaps.

In the vast US fixed income market there are various ways for buying and selling interest rate exposure, via OTC and listed derivatives, and cash Treasuries. A crucial area of trading, which has received relatively little attention, is the funding of positions via the repurchase, or repo, market. New rules on capital ratios make it more expensive for banks to undertake such activity. The US repo market is 40 per cent smaller than it was at the height of the financial crisis.

A dislocation between government bonds and swaps has taken place, with Treasury yields being quoted above swap rates, a negative relationship that upends financial theory. Under normal market conditions this would be reversed swiftly, but it has been entrenched for nearly six months, indicating how higher capital costs are reinforcing dislocations.

"Total cost analysis is going to become very, very complex," says Mike du Plessis, global head of credit execution at UBS. "The question of how they're best going to use their margin will determine which trade they do. The tail may start to wag the dog, so to speak."

Sean Tully, senior managing director for financial and OTC products at CME, says: "Unsecured bank financing in three months . . . is lower than where the US Treasury is issuing its debt on a yield basis. So, Houston, there's an issue in the repo market. We've never had a situation like that before."

Some people envisage a shift away from the use of swaps for hedging in certain circumstances, or a move to using futures such as the CME Ultra, rather than just cash Treasuries.

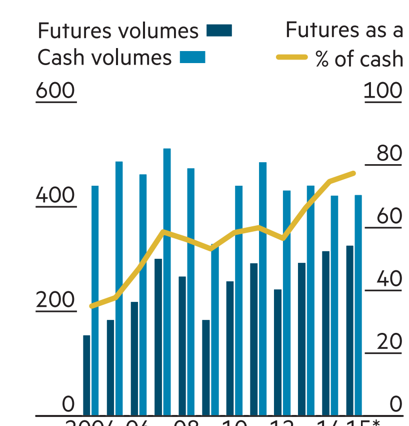
RJ O'Brien, a futures broker, says this situation could continue for several years. The answer, it says, lies in using futures such as the Ultra, which can be cleared at the CME and offset against other Treasury futures.

Others, however, point out that swaps can be customised for specific rate exposures, whereas futures are a blunter tool.

"You'll have futures and OTC markets working symbiotically, as they always were," says David Clark, chairman of the Wholesale Markets' Brokers Association, a trade body.

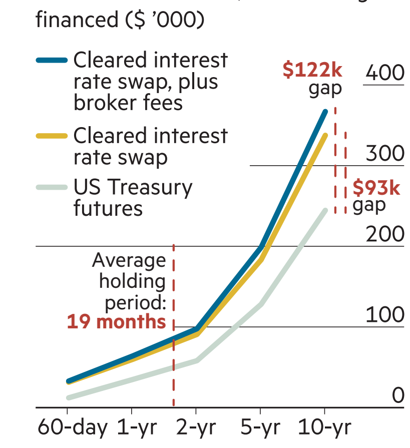
The 10-year Ultra Treasury note from CME has reportedly 'gone like a bat out of hell'
Frank Polich/Bloomberg

Client trading of Treasury futures compared with cash
Average daily notional ($bn)



* Year to date

Estimated total cost of trading
Trade size of $100m, 30% of margin financed ($ '000)



Sources: CME Group; Thomson Reuters Datastream

Commodities

China's gold price benchmark to rival London

HENRY SANDERSON

China, the world's largest gold consumer, has launched a gold price benchmark to compete with London's almost century-old process as the country seeks to have a greater influence over pricing of the precious metal.

The twice-daily auction for the renminbi-denominated Shanghai Gold Benchmark Price started yesterday on the Shanghai Gold Exchange.

It involved 18 banks, including international groups Standard Chartered Bank and ANZ Banking Group.

The launch could eventually reduce the influence of the London gold price, which started in 1919 when bankers at NM Rothschild & Sons in London sat down to calculate a fair level. That became the global gold benchmark, used by miners, central banks, jewellers and the financial industry to trade gold bars.

Last year the London price moved to an electronic auction system. In 2014 the Financial Conduct Authority found that a Barclays trader had manipulated the London gold fix and the British bank was fined £26m.

"China needs a gold benchmark that reflects local market flows and reduces gold's price dependency on the US dollar," Roland Wang, managing director for China at the World Gold Council, an industry body, said. "An Asian-focused, yuan-denominated benchmark will significantly increase the liquidity and efficiency of the gold price discovery mechanism."

Commodity pricing is increasingly moving to China, as trading has expanded in its domestic futures contracts. Six of the top 10 globally traded futures contracts are now on Chinese exchanges. Prices from iron ore to copper are increasingly set in the country.

This year, China's first crude oil contract is expected to start trading. A number of exchange traded funds and other long-only funds that track commodities are also expected to start, according to Citi, including a fund based on copper and an exchange traded fund tracking agricultural products, under consideration by the regulator.

"Huge increases in open interest and daily trading in Chinese commodity futures markets have had a large impact on global prices, enhancing short-term price volatility and shifting more pricing power to the east," the bank said. "This trend has primarily played out in base metals and iron ore, with more commodities to be affected in the future."

Oil & gas

Venezuela disruption set to cut crude output

ANDRES SCHIPANI
ANDES CORRESPONDENT

Venezuela's economic and political woes are set to curtail the Opec member's oil production, adding to a growing list of supply disruptions that are helping to prop up global crude prices.

Analysts believe chronic power shortages in the country could soon affect the oil sector, with output declining 100,000-200,000 barrels per day this year.

Dangerously low water levels at Venezuela's giant Guri dam — which provides more than a third of the country's electricity — may also force it to shut the site to avoid turbine damage, which is likely to hit oil production and could force the redirection of some oil exports to electricity supplies and diesel generators.

"We have to consider that Venezuela is less than 20 days away from a major power production disruption," Olivier Jakob of Petromatrix, a Swiss-based consultancy, wrote in a report. "Crude and product production could be negatively impacted and the country might have to increase imports of petroleum products for generators."

Unplanned production stoppages are picking up among Opec members, with oil prices around $40 a barrel. A strike in Kuwait and pipeline fire in Nigeria have added to the disruptions that analysts estimate stand at almost 2.8m b/d — the highest in nearly two years.

Supply issues have provided a powerful prop for the oil price after some of the world's leading producers failed to agree to freeze production — a deal that Venezuela helped bring to the negotiating table to try to prop up its finances.

The country's oil minister, Eulogio del Pino, has blamed Saudi Arabia for the collapse of the talks, claiming its delegation had "no authority to decide on anything" as they were under strict instructions from Riyadh not to give any ground to Iran, another Opec member.

Crude production in Venezuela, which has the biggest oil reserves in the world, according to the BP Statistical Review, is already decreasing.

According to Opec, Venezuela's production dropped to 2.52m b/d in February from 2.59m b/d in December. Average output in 2015 was 2.65m b/d, down from 2.68m b/d in 2014.

While the power shortages may increase domestic consumption of fuels such as diesel, electricity rationing is likely to hit oil production, says Francisco Monaldi, a Venezuelan energy expert with the Houston-based Baker Institute for Public Policy.

TRADING POST

Jamie Chisholm

There are two ways to look at the low cost of market protection.

It is either a good thing that shows investors' risk appetite is robust, and which allows portfolio positions to be held because they can be cheaply hedged. Or it is a bad thing because it suggests the market is too sanguine and vulnerable to a negative shock.

Naturally, those with a tendency toward bullishness will favour the former; the bearish will veer towards the latter.

So, with that said, traders can make their mind up about the following.

The CBOE Vix index, a measure of the cost of S&P 500 implied option volatility, closed on Monday at 13.09, its lowest finish to a session since August 17.

By August 24, 2015, the Vix had spiked above 50 as the S&P 500 tumbled 9.7 per cent in just four sessions. The Vix's long-term average is about 20.

The CBOE Oil Vix hit 79 on February 12, around the time West Texas Intermediate, the US-based oil contract, touched a 12-year low of $26.05 a barrel.

With WTI back to $40 a barrel, the Oil Vix is down to 46. It has averaged 37.5 over the past 10 years.

The JPMorgan Global FX volatility index is 11.4, against 10.5 for its 10-year average. Helping to keep currency market volatility percolating is uncertainty over central bank action, and politics. Sterling/dollar three-month volatility remains elevated at more than 15 ahead of June's vote on UK membership of the EU.

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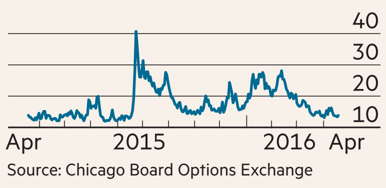
Volatility index

CBOE Vix index



Source: Chicago Board Options Exchange

Global overview

Equities remain elevated as firmer oil price continues to set the tone

S&P 500 briefly exceeds 2,100 as Goldman beats consensus while robust Brent crude puts pressure on government bonds

FT REPORTERS

A barometer of global equities climbed to its highest level of the year yesterday as a firmer oil price continued setting the tone for broad markets.

The broadly risk-positive mood put pressure on government bond prices, which nudged yields higher, and weakened the Japanese yen. Gold rose $21 to $1,254 an ounce as the dollar weakened, and silver jumped 4.1 per cent to $16.88 an ounce as it broke out of a multimonth trading range.

A big driver of sentiment across global markets is the resilient performance of oil since the collapse of a production freeze deal on Sunday. Brent crude rose 2 per cent to $43.77 a barrel as worries about a strike by Kuwaiti energy sector workers continued to underpin the international energy benchmark.

The FTSE All-World equity index gained 0.9 per cent to 269.4, its highest level since early December. The pan-European Stoxx 600 advanced 1.5 per cent while the S&P 500, which briefly surpassed the 2,100 threshold, eased backed and was little changed in afternoon trade.

With earnings season dominating the attention of investors, the Wall Street benchmark stands within 2 per cent of last May's record. Analysts had forecast a poor batch of results and many companies have beaten expectations.

Not all the earnings news has been well received, however. Netflix took a hit yesterday when the media group warned of slowing subscriber growth. In contrast Goldman Sachs rallied after beating lowered expectations, completing a string of consensus-beating results among the six biggest US banks.

Shamil Zhumatov/Reuters

Oil in the driving seat: FT.com/video

Michael Mackenzie tracks the apparent rebalancing of crude price and how it sets the pace for wider market sentiment

Japanese equities reversed a poor start to the week as the Nikkei 225 rallied 3.7 per cent, with investors noting that the economic impact of the earthquakes on the island of Kyushu might be counteracted by more stimulus measures from the Bank of Japan.

"With big carmakers forced to suspend production nationally by the disruption of supply chains caused by the quake, industrial production is likely to contract in April, increasing the probability that the economy could succumb to negative growth in the second quarter," said BNP Paribas.

The bank's economists forecast a 0.2 per cent contraction in Japan's gross domestic product during the second quarter.

With the BoJ due to deliver its latest policy decision at the end of the month, the possibility of interest rates being pushed further into negative territory has hurt the yen.

After hitting ¥107.81 per dollar on Monday, the Japanese currency was 0.3 per cent softer on the session at ¥109.12.

The dollar index fell 0.5 per cent to 94.04, hovering just above six-month lows as investors continue to weigh the shift to a more dovish tone from the Federal Reserve.

It is a stance that has helped suppress Treasury yields, though the more chipper mood across markets yesterday crimped demand for some fixed income assets and the two-year Treasury yield — among the most sensitive to US policy — added 1 basis point to 0.75 per cent. The 10-year Treasury was roughly flat at 1.78 per cent.

Yields on equivalent-maturity German Bunds were 1bp higher at 0.17 per cent ahead of tomorrow's monetary policy decision from the European Central Bank.

Such historically low bond yields have supported stock markets, because they make shares seem attractive in comparison.

In foreign exchange, South Korea's won was among the best-performing Asian currencies, up 1.2 per cent, after the Bank of Korea kept rates on hold but downgraded growth and inflation forecasts for the second time this year. The Kospi Composite was flat.

The Malaysian ringgit, which has been sensitive to moves in the oil price, rose 1.1 per cent, with commodity currencies including the Aussie dollar also firmer.

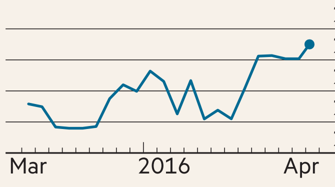
Sydney's stock market benefited from strength in resources stocks, the S&P/ASX 200 added 1 per cent, while in greater China the Shanghai Composite rose 0.3 per cent and Hong Kong's Hang Seng climbed 1.3 per cent.

Reporting by Jamie Chisholm in London, Eric Platt in New York and Peter Wells in Hong Kong

Markets update

S&P 500 index

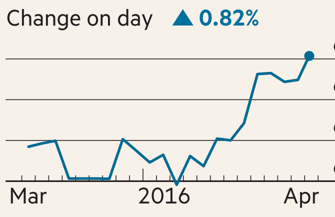
Change on day ▼ 0.07%



US equities Miners including Freeport-McMoRan and Newmont Mining were among the top performers as a rise in metals prices helped the S&P 500.

FTSE 100 index

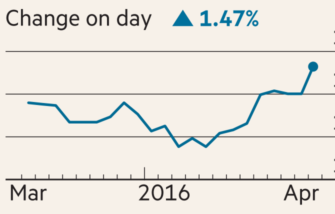
Change on day ▲ 0.82%



UK equities A second straight day of gains, led by Anglo American and Glencore, left the FTSE 100 blue-chip index up almost 3 per cent on the year.

Eurofirst 300 index

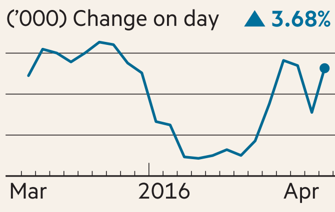
Change on day ▲ 1.47%



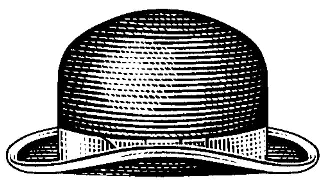
European equities French, German, Italian and Spanish equity markets have continued to dig out from losses recorded at the beginning of the year

Nikkei 225 index

('000) Change on day ▲ 3.68%



Asian equities Japanese stocks reversed their recent losses to show a strong rally as the volatility in oil eased.



London

Glencore rises 7.5% as miners prop up FTSE 100

Bryce Elder

Miners powered the FTSE 100 to its highest close since early December yesterday, with **Glencore** among the top performers.

The resources group rose 7.5 per cent to 169.9p as traders picked up on news that annual coal-supply negotiations with Tohoku Electric Power of Japan had delivered a better than expected result.

Tohoku agreed to pay $61.60 a tonne for imported Australian thermal coal — down 7 per cent from a year ago but still far above a spot price of about $11.

"This marks the largest premium to spot that we have on record," said Macquarie, which called it "a massive coup for Glencore and other producers selling on Japanese fiscal year terms."

Bernstein Research this week put a 250p price target on Glencore, more than double its previous estimate. The group would meet debt reduction targets even if it decided not to sell the Lomas Bayas copper mine in Chile, the broker said.

The rest of the commodity stocks pushed the FTSE 100 higher by 0.8 per cent, or 51.83 points, to 6,405.35. **Anglo American** was 8.5 per cent firmer at 752.5p and **Antofagasta** rose 7.6 per cent to 492.8p.

Having hit a three-year low in mid-February, the FTSE has rebounded 15.7 per cent. Large-cap miners had reached a 13-year low a month earlier and have since surged 78 per cent.

Rio Tinto added 2.8 per cent to £23.33 even after cutting its 2017 iron-ore shipment target. While Rio blamed problems with the introduction of a fleet of driverless trains, the suspicion among dealers was that Jean-Sebastien Jacques, the incoming chief executive, was resetting expectations ahead of his official appointment in July.

BHP Billiton gained 5.2 per cent to 964.5p ahead of its fiscal third-quarter production report overnight. Analysts expect it to trim 2016 iron ore guidance while saying that quarter-on-quarter production for all its main commodities except oil has been stable or slightly improved.

Rolls-Royce rallied 4.7 per cent to 696.5p on news of a $1.2bn jet engine order from Garuda Indonesia.

RBC advised caution, saying Rolls was still viewed as a "special situation" rather than a normal aerospace and defence company. At 20 times 2017 earnings, the stock might be mispricing industry trends such as a weak after-market and sluggish demand for private jets and power systems, the broker said.

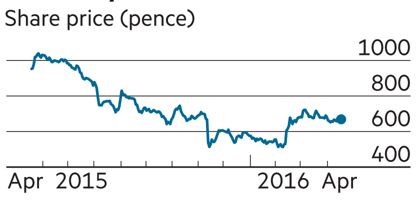
Sector peer **Meggitt** rose 6.2 per cent to 413.2p after the aircraft engineer repeated full-year guidance ahead of an investor day. First-quarter numbers were better than expected thanks largely to a more robust than feared performance for its civil after-market operations, which had been the cause of a profit warning in October.

Aveva was sent 9.1 per cent higher to £16.61 after the design software maker reassured on trading.

The statements from Meggitt and Aveva helped lift engineers including **Weir,** the pumpmaker, which rose 6.3 per cent to £11.96 ahead of an update due on April 28.

Rolls Royce

Share price (pence)



Source: Thomson Reuters Datastream

Indices	Close	Day's change
FTSE 100	6405.35	51.83
FTSE 250	17044.25	154.50
FTSE 350	3556.06	29.36
FTSE All-Share	3502.70	28.47
FTSE All-Share Yield	3.70	-
FTSE 100 Futures	6357.00	52.00
10 yr Gilt Yield	1.64	0.03
20yr Gilt All-Share Ratio	0.60	-

Wall Street

IBM declines after fall in legacy sales

Adam Samson and Pan Yuk

IBM shares declined yesterday, eating into a sharp gain over the past two months, it disclosed its 16th-straight quarterly sales fall.

Big Blue said its revenues had dropped 5 per cent year on year to $18.7bn as growth in newer businesses failed to offset the deterioration in legacy units. The figure topped expectations of $18.3bn, but was the lowest in 14 years, according to Bloomberg data.

Net profits fell to $2bn from $2.3bn in the same period in 2015. Adjusted profits, which exclude certain items, of $2.35 a share also beat Wall Street expectations of $2.09 a share.

However, a "closer look shows results were generally of low quality, with more than half of the EPS beat coming from a tax benefit", said Sherri Scribner, an analyst at Deutsche Bank.

The strategic imperatives unit, which houses the cloud and data analytics divisions, logged a 14 per cent year-on-year rise in quarterly revenues. Cloud sales soared 34 per cent.

However, the cognitive solutions division, which aims to create software and services that can "think" more like humans than computers, and is a significant part of chief executive Ginni Rometty's turnround efforts, underwhelmed. Revenues fell 1.7 per cent to $4bn.

Legacy units, which helped IBM grow into a technology powerhouse, are suffering as companies move to cloud-based solutions instead of hosting software and hardware in-house. But Stifel analyst David Grossman contended that the results pointed to "signs of stabilisation" for the company, which is more than a century old.

IBM shares declined 5.1 per cent to $144.75. They are still up 22.7 per cent since February 11.

Elsewhere **Netflix** shares plunged nearly 12 per cent to a one-month low of $96.87 after it issued surprisingly weak subscriber growth guidance.

The streaming company said it expected to add 2m international subscribers in the current quarter. That was below analysts' estimates for 3.45m and sharply slower than the 4.5m added in the first three months.

Disappointing guidance overshadowed what was otherwise a solid set of first-quarter results.

In midday trading, the S&P 500 rose 0.3 per cent to 2,100.2, surpassing the closely watched 2,100 level for the first time this year. The broad market index sits less than 2 per cent from its all-time high last May. The Dow was up 0.3 per cent at 18,050.7, while the Nasdaq Composite fell 0.2 per cent to 4,950.6.

Markets & Investing
FINANCIAL TIMES

INSIGHT

John Plender

Cautious consumers fail to reap full benefit of falling crude costs

One of the great non-events in the global economy in the past 18 months has been the failure of consumers in the developed world to spend enough of the windfall from a falling oil price to generate a powerful boost to growth.

In the US and Japan households have saved much of the increase in income stemming from cheaper oil. The potency of the windfall in the eurozone has not been enough to obviate the need for extreme monetary easing, including negative interest rates.

Explanations are not hard to find. With a large energy sector, the US has sustained a significant hit to investment. At the same time, deleveraging in the aftermath of the financial crisis and worries about an uncertain future have blunted Americans' urge to spend.

In Japan, the increase in the consumption tax in 2014 took away more from consumers than the oil windfall delivered. As for the eurozone, austerity still reigns and animal spirits are at a low ebb.

Economists at the International Monetary Fund, meanwhile, argue that what brought about past windfalls was not just the falling oil price but its combination with falling interest rates. The trouble today is that rates had already declined to extremely low levels before oil caved in. With interest rates low, the incentive to spend the windfall is reduced because consumers do not fear prices are about to rise. They may also seize the opportunity to save more because, in a low interest world, a bigger pot of savings is needed to achieve a given target return on investment.

> The trouble today is rates had already declined before oil caved in

Is it possible that the windfall effect has simply been delayed and that the dynamics of the transfer of resources from oil producers to consumers is about to change?

Maybe, but it is hard to see much happening in Japan, where massive quantitative easing has failed to break the deflationary psychology and not managed to prevent an appreciation of the yen in recent weeks. The eurozone would be a more natural place for oil-induced buoyancy because, unlike the US, it is not struggling with the burden of a big energy sector. By the same token, if it was going to happen in Europe it would surely have happened by now.

The US is where the case might be arguable. Recent labour market data offer some hope of more buoyant consumption. Note, too, that while households' savings continued to rise as oil prices fell further in January and February, consumers did not pull in their horns as they had done previously. Spending growth picked up. The fall in retail sales in March, driven by a decline in auto sales, does not help the thesis, but it could be rationalised by reference to tightening financial conditions and the prevailing fear of recession that has since waned.

Also helpful is the weakening of the dollar against the yen and the euro, which enhances earnings prospects in the corporate sector. Until recently, capital flows danced to the tune of currency manipulation by central banks. But as I have noted here before, markets have recently taken to neutralising competitive devaluations. And as Benn Steil and Emma Smith of the Council on Foreign Relations point out, the markets now seem to be reacting rationally to movements in interest rate differentials.

Though the policy rates of the Bank of Japan and the European Central Bank have fallen well below the federal funds rate, US inflation readings have been on an upward trend. This has pushed real inflation-adjusted US policy rates below those in Japan and the eurozone.

Though the ECB has been ploughing deeper into negative rate territory, falling eurozone inflation means that real eurozone rates have risen this year. So the yen and the euro are not just havens in a storm. Rate differentials make Europe and Japan attractive destinations for savings and are a cause of dollar weakness.

Given that inflation in the US looks set to rise faster than in Japan or the eurozone, dollar weakness may be with us for some time — though that assertion has to be accompanied by the standard health warning that attaches to all currency forecasts.

Does this add up to a case for a bigger windfall effect to come? Not, I'm afraid, a wholly convincing one — the headwinds are just too powerful at present.

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Analysis. Equities

Asia volatility traders in hunt for liquidity

Wild swings have highlighted the lack of a Vix counterpart for the region's investors

JENNIFER HUGHES

When markets plunged in January, led by China, one index in Asia was hit more than most — a move that sent shudders through the region's growing band of volatility traders, as the world braced for a re-run of the turmoil that overtook the market the previous September.

The index that volatility traders were watching most closely was the Hang Seng China Enterprises Index (HSCEI), made up of Hong Kong-listed mainland companies. In 2015, when China's markets were soaring, it had become the reference point of choice for "autocallable securities" in South Korea, a popular and risky retail product.

The worst fears of traders did not materialise as the global mood subsequently recovered. But this year's wild market swings have awakened interest in Asia's lack of a liquid tool that can help protect portfolios and trading positions held by banks and hedge funds from bouts of turmoil.

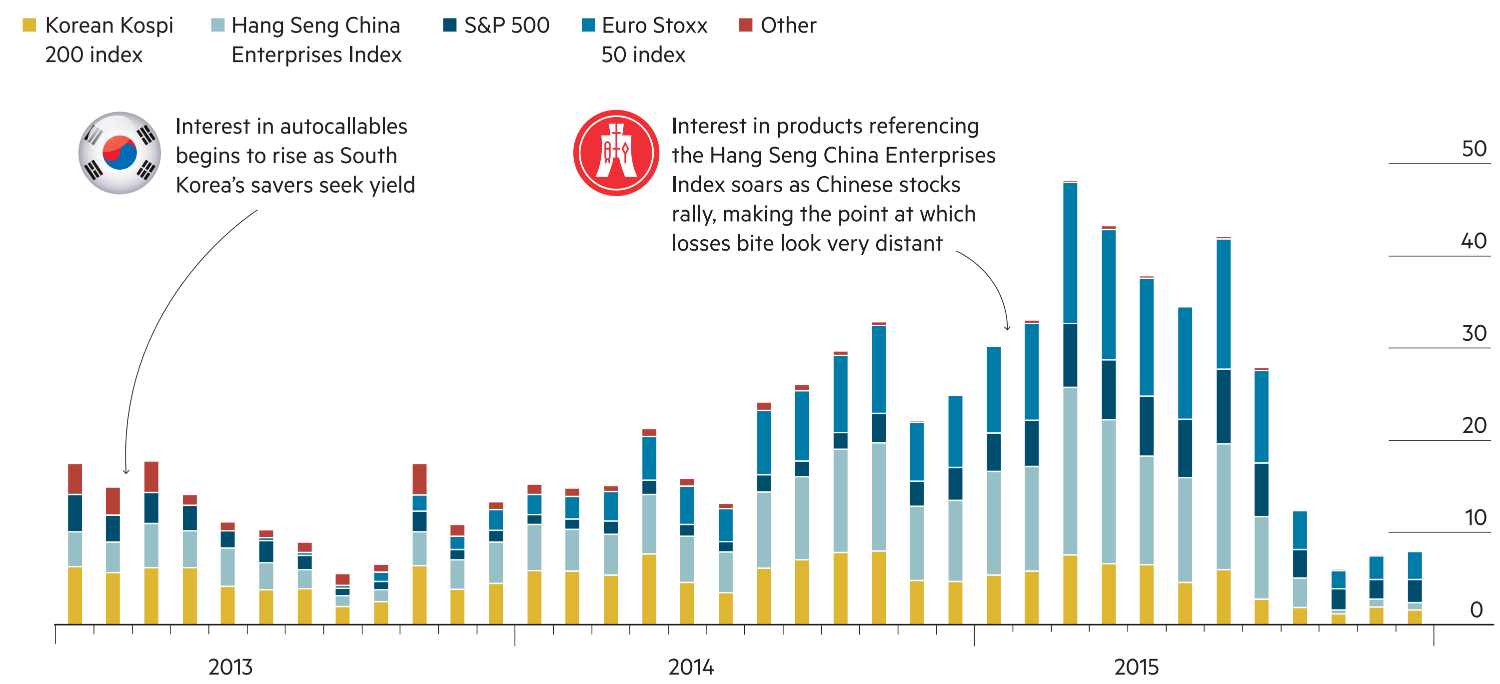
"In periods where we have volatility and uncertainty then asset managers and hedge funds are looking to take advantage of that," says Shane Carroll, derivatives strategist at Société Générale, who adds that interest had been rising for several years.

Investors in the US can turn to the CBOE's Vix, a gauge of implied S&P 500 volatility. Across US markets there is a range of participants, such as banks and credit investors, keen to limit risk to hedge funds focused on potential arbitrages, not to mention retail investors trading options.

Although Asian exchanges have created indices that seek to replicate the Wall Street equity model, including the V-Nikkei and the V-Hang Seng, the market in products based on them is illiquid, according to hedge funds.

Linked indices

South Korean structured finance issuance
Korean structured products written on selected Asian indices (€m)



FT graphic Source: SG Flow Strategy & Solutions

> 'What we see for the coming year is that the volatility of volatility will be very high'

That leaves banks as the key mediators, as holders of volatility risk, between the buyers of the structured products they have sold — huge markets in the likes of South Korea, Taiwan and Japan — and those hedge funds with an interest. As the banks selling the products to clients have effectively gone long implied volatility, they need a liquid market that can allow them to hedge that risk.

The limited number of volatility traders in the region and the scale of South Korea's retail structured products market is such that "vol" is normally cheaper in Asia. That helped autocallable sellers to hedge by attracting interest from hedge funds keen on the low prices offered on products such as variance swaps. These allow investors to place bets on future levels of volatility relative to current levels.

However, when the HSCEI began to plunge in the weeks following China's surprise devaluation, the trades were structured such that the speed of the decline in effect wiped out the banks' hedge by increasing their overall sensitivity to the sharp moves.

The result has been a shift to other products that seek to better match banks' risks as well as a rise in the price of volatility in the region. Instruments called corridor variance swaps, which are active only when indices are in a certain range, are one such answer.

Investors are also expressing rising interest in dividend futures as a way of coping with market volatility that may not reflect, or even affect, the underlying economy. These exchange traded contracts are based on expected dividend payouts by a calendar date, allowing traders to hedge dividend exposure or place bets on whether or not a company will pay out.

For now, with markets in more buoyant mood, the volatility landscape has quietened down in Asia. Even the HSCEI is back above 9,000 after its lurch as low as 7,500 in February, although still short of the 10,000 rule of thumb used by bankers as a gauge of risk appetite deal.

But those in the market warn this is just the calm before the next storm.

"What we see for the coming year is that what is called the 'vol of vol', or 'volatility of volatility', will be very high," says Govert Heijboer, co-chief investment officer at True Partner, who manages a specialist volatility fund.

"People should remember that when the 2007, 2008 crisis started happening we had an intermediate period when it was somewhat quiet before it all started again."

Commodities

Oil price buoyed by supply disruptions

ANJLI RAVAL

A strike that has temporarily halved Kuwait's crude output and global supply disruptions propelled oil prices higher yesterday.

Brent, which had sunk to almost $40 a barrel on Monday after talks between producers in Doha collapsed, rose as much as $1.34 to $44.25. West Texas Intermediate, the US benchmark, rose $1.49 to $41.26 a barrel.

Many market participants expected prices, which have rallied 45 per cent since mid-February, to come under fresh pressure after the failed deal to freeze output.

But Brent is back at levels before the meeting, supported by the Kuwait strike and reaction to outages in Nigeria and Venezuela.

"The market is increasingly pricing supply risk as spare capacity has disappeared," said Olivier Jakob of Petromatrix, a Switzerland-based consultancy.

Global unplanned disruptions, which Energy Aspects estimates at almost 3m b/d, are near a two-year high.

Meanwhile production from non-Opec nations has taken a hit from the collapse in oil prices.

"We are back in an environment where the only spare capacity left is in storage tanks, and if those barrels start to be used then the crude oil structure tightens," said Mr Jakob.

Kuwaiti oil workers downed tools for a third day in protest at public-sector pay reforms. The country's crude production has fallen to 1.5m barrels a day, from an average 2.8m b/d in March.

The protest had led to a temporarily balanced oil market, said Carsten Fritsch, analyst at Commerzbank. But the strike was unlikely to last for weeks because the economy was "too reliant on oil revenues", he said.

Kuwait hopes to bring production back up to normal levels in the coming days, and is planning to take legal action against the strikers.

The disruption adds to supply issues in Nigeria, Venezuela and elsewhere.

Exports of Nigeria's Forcados crude are expected to stay down until June, while reports at the weekend said *force majeure* had been declared again on Brass River cargoes after a pipeline leak. About 400,000 b/d of supply has been lost.

Venezuelan declines of about 200,000 b/d are expected to accelerate following news that Schlumberger, the oil-services company, will decrease activities amid insufficient payments.

Lost supply in Iraq and Libya has also tightened the market.

Summer maintenance in the North Sea is expected to add pressure on supplies, especially of the crude grades that underpin the Brent futures contract.

Contracts for June delivery have moved to a premium over those for July. This market structure, known as backwardation, is associated with tighter market balances.

However, a Reuters report said maintenance on the Buzzard field in the North Sea had been delayed from early July to September. Buzzard is the largest contributor to the Forties crude oil stream — one of the four grades that make up the benchmark.