December 2 — December 8, 2013 | businessweek.com

Bloomberg Businessweek

J.Crew
Teaching the world to dress American p50


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SAMSUNG

"There's no group or individual saying, 'Let's screw the black guys today'"

p56

"This is not a store for college kids anymore. That woman over there—look. She's buying three pairs of £375 leather ankle boots"

p50

"Give me 30 to 35 days, and I'll build you a kidney"

p39

"I never take my grandchildren to the woods, because they're full of holes"

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Cover Trail

How the cover gets made

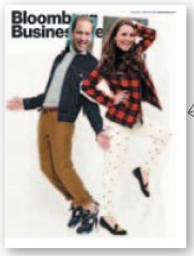
"How about we have the Duke and Duchess of Cambridge, future heirs to the throne of England, themselves symbolic of all that is wholesome and holy and English, and clothe them as J.Crew catalog models?"

For this you need:
❶ Some pictures of Wills and Kate

❷ Two models of similar body shapes as the royal couple

❸ We then take this torso from a shoot,

❹ Then you bolt them together to make that



❺ Which is then sent to a retoucher to become this

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THIS ISN'T ENOUGH

A higher minimum wage would boost workers and bring America in line with the rest of the world. Helping the least fortunate will require a whole lot more

By Peter Coy and Susan Berfield

Tom Wolfe himself couldn't have imagined a better New York juxtaposition. Pizza, Pepsi, and hot chicken wings were out on the table one November evening at Strive New York, an agency in East Harlem that helps ex-convicts and other chronically unemployed people get and keep jobs. Luz Droz, 32, who has a 10-month-old son, explained that she was trying to turn things around after "a little situation in my life," which turned out to be two prison sentences totaling eight years for dealing drugs and passing bad checks. She detests being on welfare but was turned down recently for a minimum-wage job at Burlington Coat Factory. "I thought I was going to get it," she said. "Once I get a job, I'm off to the races."

The same evening, one stop south on the 4 express subway line, waiters were serving hors d'oeuvres of tuna tartare and basil-slathered shrimp in the Upper East Side apartment of billionaire George Soros. The guest of honor was Soros's fellow billionaire David Sainsbury, the former chairman of the family-founded British supermarket chain J Sainsbury. He has a new book, *Progressive Capitalism*. Sainsbury will probably never meet Luz Droz, but he, too, had minimum-wage employment on his mind. To compete with China, he said, "the West must race to the top" and not try to "screw down the wages."

The down-on-her-luck mom who can't land a job at minimum pay and the billionaire who can't imagine paying so little are two voices in a global debate over not only the minimum wage, but also the bigger challenge of helping the least fortunate members of society. The federal minimum wage is $7.25 an hour. President Obama called for a $9 federal minimum by 2015 in his State of the Union address in February and then this fall endorsed a more ambitious bill, which is stuck in House and Senate committees, to raise it to $10.10 by 2015. California, New York, Connecticut, Rhode Island, and New Jersey voted to raise state minimums this year. Last August fast-food workers in almost 60 cities struck or walked out in a bid for starting pay of $15 an hour. In recent weeks two of the nation's largest private employers, Wal-Mart Stores and McDonald's, have taken heat for paying many of their workers so little that they need government benefits and charity to get by.

Raising the minimum wage is neither as wonderful as its advocates claim nor as dangerous as its detractors warn. On the upside, it would increase pay for millions of Americans, not only those earning the minimum but also those at fixed increments above it. These are people who could really use a raise. Contrary to what

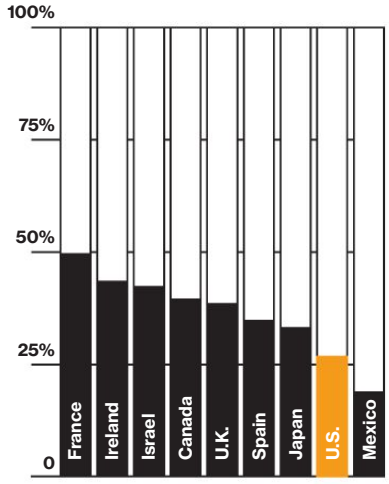
Raising the minimum wage is neither as wonderful as its advocates claim nor as dangerous as its detractors warn

generations of students were taught in freshman econ, new research finds that minimum-wage increases at the state level have caused little, if any, harm to employment. "Outside of the simple Econ 101-type environment, increasing workers' pay can improve the functioning of the low-wage labor market," Arindrajit Dube, a University of Massachusetts economist, testified before Congress in March.

On the downside, a higher wage floor would undoubtedly price some marginal workers out of the market. Interns, for example, aren't allowed to work for less than the minimum while they learn the ropes. (They can be unpaid, but then they're not allowed to do real work.) A higher minimum wage would do nothing for the unemployed, among whom are the poorest of the poor. For them, other solutions are needed. "The search for a silver bullet is a mistake. We need lots of bullets," says Steven Pressman, an economist at New Jersey's Monmouth University.

Raising the wage to catch up with inflation invariably polls well, because most Americans perceive it as a matter of justice. Their hearts go out to the likes of Shawndraka Mack, 40, who works full time at $7.60 an hour for a McDonald's in Charleston, S.C. She and her disabled fiancé are raising two teenagers in the trailer home she inherited from her mother. "I love what I do," she says, "but I don't want to work for nothing."

The minimum wage as a percentage of the national average pay in 2012



Obama appealed to that sentiment in his State of the Union address when he said, "Tonight, let's declare that in the wealthiest nation on earth, no one who works full time should have to live in poverty." A Gallup poll in November found that 76 percent of Americans would vote for a $9 federal wage floor.

The public images of low-paying employers such as Wal-Mart and McDonald's take a hit during the holidays, when Americans are seized by a spirit of charity. Stephen Colbert mocked Wal-Mart after employees at one of its stores started a Thanksgiving food drive for fellow workers. "Now, some critics out there say Wal-Mart isn't doing enough, but they're wrong," Colbert said, "because Wal-Mart isn't doing anything."

Recognizing that they can't get on the wrong side of their customers, many of whom have below-average incomes, Wal-Mart and McDonald's are attempting to change the narrative. Both say they pay above the minimum to the vast majority of their employees. "Nationally, there has been an erosion of middle-class jobs, and we want to be part of the solution," David Tovar, Wal-Mart's vice president for communications, e-mailed journalists on Nov. 21. The same day in Chicago, McDonald's chief executive officer, Don Thompson, pointed out at Bloomberg's The Year Ahead: 2014 conference that 60 percent of the company's franchisees started in hourly jobs.

Ultimately, the case for higher minimum pay should be evaluated on its economic merits. "Wages are a market price—determined by supply and demand, the same as the price of apples or coal," one economist wrote in 1998. "The amorality of the market economy is part of its essence and cannot be legislated away." (That economist—surprise—was Paul Krugman, who was skeptical about living-wage ordinances but today says a healthy jump in the minimum wage is justified on economic grounds.)

The latest support is based on the economic theory of "search frictions," which won a Nobel Prize in 2010 for Peter Diamond, Dale Mortensen, and Christopher Pissarides. It's the idea that employers and job seekers don't find each other immediately. Fact: Some 3.9 million job openings went unfilled at the end of September, according to the Bureau of Labor Statistics. Raising the minimum wage makes workers less likely to quit, which reduces the number of openings at any given time, the theory goes. That boosts employment, offsetting layoffs of workers who are no longer worth their pay at the higher minimum. "There's a widespread recognition that ▶

PHOTOGRAPH BY 731; GRAPHIC BY BLOOMBERG BUSINESSWEEK DATA: OECD

we need models with search frictions to really understand the labor market," says Dube, the Massachusetts economist, who's part of a new generation of scholars studying the minimum wage.

America's minimum wage is 27 percent of the U.S. average pay, a lower ratio than that of any other member of the Organisation for Economic Co-operation and Development except Mexico. That doesn't prove that the U.S. floor is too low—only that it can be higher without the sky falling. In Denmark, among the leading countries in income equality and national happiness, the minimum pay set by negotiations between employer groups and unions is the equivalent of about $20 an hour. Despite that, the World Bank has ranked Denmark as the easiest place in Europe to do business for three years running.

Still, raising the minimum wage is an inadequate response to the larger challenge of reducing poverty. "It's just irrelevant to the real, first-order problems such families face," writes John Cochrane, a University of Chicago economist. Brazil has a minimum wage, but it's been far less effective in alleviating poverty than the renowned Bolsa Família program, which gives families cash payments as long as they get their children educated and vaccinated and meet other conditions, says Marcelo Côrtes Neri, president of the Institute of Applied Economic Research in Brasília.

The deeper problem for today's poor isn't low pay. It's that many have lost any connection to the world of work. In 1968, when the U.S. minimum wage hit its inflation-adjusted peak of $10.70 an hour, 81 percent of men aged 20 and older had jobs. Now 67 percent do. In October the unemployment rate for black teenagers was 36 percent. "Raising the minimum wage is a short-term fix," contends Wal-Mart's Tovar. The long-term solution, he says, involves "expanding education, training, and workforce development."

The minimum wage can never be more than a piece of the social safety net. It's attractive to liberals because it doesn't require getting a tax increase through Congress: The cost to society shows up instead in the prices that employers raise to cover their higher costs. Because it's only for workers, however, it can't possibly fill the void of inadequate food stamps, welfare, and housing assistance.

In arguing for a higher minimum wage, Bloomberg View columnist Barry Ritholtz recently blasted Wal-Mart and McDonald's as "welfare queens" because some of their employees, as a result of their meager pay, live partly on government benefits. (Families of McDonald's workers have received an average $1.2 billion a year in benefits, according to an academic study funded by Fast Food Forward, which helped organize the summer strikes.)

A protest in Los Angeles on Nov. 7

LUCY NICHOLSON/REUTERS

True, those hidden subsidies to employers would shrink if the minimum wage rose, but it's unreasonable to think they would disappear entirely. Britain's New Poor Law of 1834 tried to end subsidies to employers by preventing recipients of relief from working for them. It locked them up instead in poorhouses of Dickensian cruelty. That's hardly an example to follow. The other way out of inadvertently subsidizing private employers would be to cut off benefits to anyone who got a job. But that would penalize people who landed work or induce them to stay unemployed.

Although a favorite of liberals, the notion of raising the minimum wage is in some ways deeply conservative. It's grounded in the traditional ethic that able-bodied people should support themselves by the sweat of their brows—and private employers, not the government, should be responsible for workers' livelihoods. But what if technology throws some people out of work not temporarily, but permanently? What if many service positions follow manufacturing jobs into obsolescence? (There's already a hamburger-making robot for sale.) If that happens, society will have to develop new ways to share its abundance with people whose services are no longer needed, speculates Brian Arthur, a nonresident professor at the Santa Fe Institute.

The deeper problem for today's poor is that many have lost any connection to the world of work

One up-and-coming solution is what advocates term unconditional basic income—an annual grant of fixed size that goes to every person in a country, rich or poor, regardless of whether they work or not. It's a big step away from the minimum wage. Milton Friedman, the late libertarian economist, favored a variant—a payment that would phase out at higher incomes—to replace the intrusiveness of the welfare state.

Europe is headquarters for the unconditional basic income movement. This fall petitioners managed to get it on the national ballot in Switzerland. (The date hasn't been set.) Giving people money unconditionally could start an epidemic of shirking work. But backers say most people would still want to work if they could, either to earn a standard of living above the spartan one guaranteed by the government, or to fulfill themselves, or both.

In the U.S., an increase in the minimum wage is far more likely than adoption of a universal basic income. A higher wage floor is right for low-skilled workers and harmless to the economy. But it's only one piece of a very large economic puzzle. Ⓑ —*With Mark Gimein*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The Case for Legalizing Online Gambling

Federal oversight is the best way to make the industry more rational

In a victory for fun, liberty, and sound fiscal policy, New Jersey has become the third state after Delaware and Nevada to permit online gambling within its borders. A dozen or so other states will consider doing so next year. By 2023, according to a forecast by Bloomberg Industries, annual online gambling revenue could reach $23 billion nationwide. In a just world, it would be legal in all 50 states.

Online gambling, like everything else on the Internet, is inherently interstate commerce. That makes federal regulation sensible.

Two bills in Congress are on the right track. One would legalize all forms of online gambling, except sports, and create an oversight office at the U.S. Department of the Treasury. It would also allow states to opt out of permitting such wagering. The other bill proposes a 4 percent federal tax on operators and permits states to collect an additional 8 percent in taxes. Combined, the two bills offer the outline for a rational federal approach.

Of course, there will be plenty of objections. Sheldon Adelson, who made his zillion-dollar fortune separating casino-goers from their money, has recently discovered moral objections to gambling (online, anyway). He should stop whining. Casinos—like every other industry from music to media to retail—will have to adjust to the Internet's ruthless disruption. Some states may not like the idea, either. They might depend on tax revenue from casinos to shore up their budgets, for instance, or they might object to online gambling on moral grounds. Yet states will be able to raise substantial new revenue from online wagering, and traditional casinos will still be producing cash for a long time to come. If state officials find gambling sinful, they can always opt out.

At any rate, problem gambling and other harmful side effects will probably be easier to prevent online than they have been with casinos. If would-be players are required to open an account and have their identities verified, imposing loss limits should be fairly manageable from a technical perspective. (As with most things digital, convenience comes at the expense of privacy.) Online operators could also more easily comply with laws targeting money laundering and prohibitions against underage gambling. Again, it wouldn't be foolproof, but neither are real-life casinos.

Finally, a federally regulated system would help move online gambling toward licensed—and taxed—domestic operators. Gamblers could be assured that their financial transactions are safe and legal and that the games aren't rigged. Public officials, meanwhile, would be rewarded with a windfall: Taxing online wagers could lead to as much as $41 billion in revenue over 10 years.

People clearly like gambling. Letting them do so where they want would make them happy. Regulating it properly would keep them safe. And taxing it will make lawmakers smile.

Keep a Close Eye on Iran's Next Move

The test of the country's intentions will be how aggressively it pursues a final agreement

Of all the details about the historic deal announced on Nov. 24 in Geneva limiting Iran's nuclear program, the most salient one may be its scope: It's intended to last for only six months. Iran agreed to take the essential steps required to freeze its progress, which include halting enrichment of uranium to 20 percent, just a short leap from weapons-grade, and converting its stockpile of the fuel to less dangerous forms. Iran also agreed to accept more intrusive inspections—in some cases daily—by the International Atomic Energy Agency. In exchange, the so-called P5+1—China, France, Russia, the U.K., the U.S, and Germany—have relaxed about $7 billion of the $100 billion sanctions.

Israeli Prime Minister Benjamin Netanyahu is correct that the agreement clearly establishes any final pact will leave Iran with an enrichment capacity, albeit one that is limited and monitored. This is a departure from United Nations Security Council resolutions in place since 2006 and the zero-enrichment demands made by the U.S. and its European allies for the last 10 years. That strategy, however, failed. The tacit acceptance that Iran will be allowed to go on enriching uranium up to 5 percent merely recognizes this failure.

A permanent settlement needs to meet the legitimate concerns of Israel, Saudi Arabia, and others in the Middle East—and it must enforce the repeated pledges of President Obama that Iran never become a nuclear-armed state. Critics of the interim agreement are right that Iran may use the negotiations to run out the clock, gradually wearing down sanctions but leaving the country with the freedom to develop nuclear arms. The best way to prevent this is to make clear to Iranian leaders that failure so late in the game would mean military action, while success could lead to other deals Iran craves on trade and regional security.

The real test of Iran's intentions comes now, not just in whether it implements the terms of the interim deal, but also in how aggressively it pursues a final agreement. That's what supporters and critics of this first-step accord should be watching. Ⓑ

ILLUSTRATION BY BLOOMBERG VIEW

December 2 — December 8, 2013

In Ukraine, Desperate Workers Turn to Illegal Mines

▶ People die and streets collapse as the mines proliferate

▶ "I never take my grandchildren to the woods, because they're full of holes"

A woman drops trash into the gaping mouth of a defunct illegal coal mine. Below, the funeral of Andrey Kandourov, who died in a mine.

When Andrey Kandourov started working in an illegal coal mine near the eastern Ukrainian city of Torez on Oct. 1, he wouldn't let his mother buy him a respirator, because he thought it was too expensive. Two weeks later he was dead. The police told his family he died of a heart attack, even though another worker died in the mine with him at the same time. The family says it never received any compensation from the state social insurance fund.

Kandourov, who was 44, is one of many casualties of Ukraine's illegal coal business, a nightmarish world where day laborers—some in their teens—toil underground in narrow, crudely dug shafts without proper structural support or ventilation. The miners usually labor without safety equipment, and they have no hope of a pension when they can no longer work or health insurance if they're injured. They work for as little as 150 hryvnia ($18) a day, below the regional average of 185 hryvnia. Mining and energy experts estimate that hundreds die every year in such unlicensed mines, which produce anywhere from 3 million to 10 million tons of coal, or about 4 percent to 12 percent of the country's annual total.

"Andrey kept telling me, 'Mom, I can't find any work,'" Valentina Kandourova says as she shares photos of her son in her small, tidy apartment in a concrete, Communist-era housing block in the town of Shakhtarsk. She weeps bitterly as she describes the depth of her son's desperation. "That mine had been closed once before by a court order because it was too dangerous," she says.

Most illegal mines, called *kopanki*, are in the Donetsk region in eastern Ukraine. The birthplace of the Stakhanovite movement, designed to inspire workers under Stalin, the area became the Soviet Union's major supplier of coal and a hub of steel mills, foundries, and chemical factories. By Soviet standards it was a prosperous place. The social fabric frayed after the 1991 fall of the Soviet Union. Many state mines and factories shut down, and jobs became scarce. Crime and drug use skyrocketed, bringing with them HIV and tuberculosis.

The provincial capital of Donetsk is surrounded by towns like Shakhtarsk, with row after row of drab residential blocks linked by crumbling roads decorated with monuments of miners and soldiers. Oleksandr Kendyukhov, head of the economic management department at Donetsk National Technical University, says that the area needs massive investment and that Ukraine as a whole needs a complete restructuring of its coal industry. Where the investment will come from is unclear. The country's leaders had been negotiating a trade agreement with the European Union, but the government has recently turned away from the EU, looking to Russia for assistance.

The kopanki started in the early 1990s as a way for families to get a bit of extra coal for the winter, but they've turned into a big organized business, according to Dmytro Marunych, co-chairman ▶

PHOTOGRAPHS BY JOSEPH SYWENKYJ FOR BLOOMBERG BUSINESSWEEK (5)

An elderly woman (left) who works as a guard at a kopanka, stands in the doorway of her small trailer home. A worker (right) repairs a cable at the entrance of an illegal mine near Davydovka.

◀ of the Kiev-based consultant Energy Strategies Fund. He says that most of the unlicensed mines are owned and run by loosely connected criminal networks that hire the workers and bribe local police to keep quiet. Since they don't pay taxes, social security, or health insurance, or invest in safety equipment, the coal is four to five times cheaper than what comes from the highly inefficient state mines, which spend about $200 to produce a ton of coal. The Ukrainian Parliament has just passed a law that could lead to a crackdown on the kopanki, but it remains to be seen whether it will have any effect.

According to Marunych, the state mines indirectly buy coal from the kopanki through an official trading agency, Coal Ukraine. Kopanki operators sell coal to traders, who in turn sell it on the internal Ukrainian market, where it's eventually bought by Coal Ukraine. This coal is counted as part of the state mines' production: The state mines get government subsidies for each ton of coal they produce. So Ukrainian taxpayers end up subsidizing kopanki owners. "Since 2009 the government has spent 60 billion hryvnia on coal subsidies," Marunych says. "It's so huge it destabilizes the country's budget. And it's only making the kopanki thrive." Coal Ukraine did not have an immediate comment.

Because the kopanki are shallow and dug by profiteers rather than professional mining engineers, they cause environmental damage, says Anatoly Akimochkin, first deputy chairman of the Independent Trade Union of Miners of Ukraine in Donetsk. "Real mines exploit the coal layer much deeper underground, so they pose no immediate threat to the environment," he says. "Kopanki are in areas where no one should have the right to extract coal, often right by people's houses." ▶

Valentina Kandourova, holding a picture of her son, recalls how joblessness drove him into the mines.

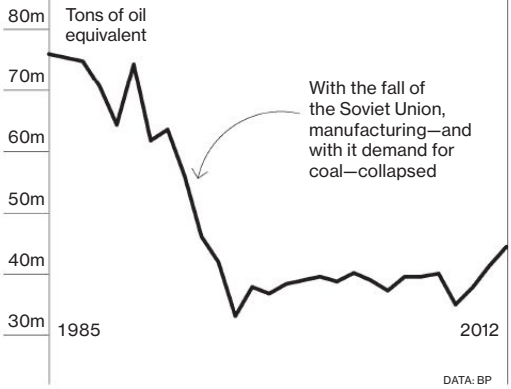
◀ Part of the street where Zinaida Trofimova lives near Snizhne has caved in as a result of illegal mining in the yard of a neighboring house. The pensioner has complained to authorities many times but says they've always turned a blind eye. "I was showing it to the police, and they said, 'Eh, what do you want?' " she says. "Sometimes when I go to bed, and the night is quiet, I hear the walls cracking." A short walk into a protected nature preserve reveals more makeshift mines. "I never take my grandchildren to the woods, because they're full of holes," Trofimova says. "Once a cow fell into one of the holes." Yet even she can't imagine life without the mines: Her son works in one to feed his three children.

For a supposedly illegal activity, the kopanki are very visible. Trucks loaded with coal rumble down country roads, while unregulated open-pit mining has turned parts of the countryside into a lunar landscape. One reason the police rarely arrest anyone could be that some highly placed politicians are involved in the trade, according to Yuriy Korolchuk, a member of the advisory board of the Institute of Energy Strategy in Kiev. The Ministry of Social Policy, which works on employment issues, including those of miners, had no immediate comment. The energy and coal minister did not find time to meet in October, nor did the ministry answer written questions.

In the Davydovka settlement near Torez, not far from the mine where Kandourov lost his life, rickety barrels filled with coal are fastened to a worn steel cable and pulled up from a depth of about 180 meters (591 feet) by an engine from an old Lada, the ubiquitous car of the Soviet era. Igor, the youngest of the three workers aboveground, adds the coal to a growing pile. Nikita revs up the coughing Lada motor, while Aleksandr, a supervisor with 35 years of experience in state mines, talks on a walkie-talkie to the two men working underground. Due to the illegal nature of their work, no one will give his last name. "This mine is operated under conditions that aren't too different from what we had under the Czar," Aleksandr says, wiping soot from his face. "These kids, they don't know what they're doing. Can life get any worse than this?" —*Ladka Bauerova and Kateryna Choursina*

The bottom line As much as 12 percent of Ukraine's coal production comes from illegal mines run by criminal networks.

Ukraine Coal Consumption



Skills

Mexico's Surprising Engineering Strength

▶ The country's auto industry gets a boost from homegrown talent

▶ "We are transitioning from Made in Mexico to Designed in Mexico"

As global automakers pour billions of dollars into their Mexican factories, Marcos Perez is trying to make sure the nation's future goes beyond assembly lines. The head of product development at **Ford Motor**'s Mexico unit, Perez has helped the company almost triple its local engineering staff, to nearly 1,000, since 2010. His engineers have filed for 40 U.S. patents in the last three years, including one for a low-cost crash protection system that boosts safety ratings without adding much weight or cost. "It's an inflection point," Perez says. "We used to be a simple-assembly kind of country, and we moved to a truly core manufacturing country, where most of our assembly plants are hitting record numbers on productivity, on quality, on cost. Now we are transitioning from Made in Mexico to Designed in Mexico."

In a cubicle at a Ford assembly plant on the outskirts of Mexico City, Gerardo Rodriguez, a 24-year-old mechanical engineer, is working on reducing noise in the Ford Fiesta, which is exported from the factory to the U.S., Canada, and Latin America. He participated in a Ford trainee program as an undergraduate at Universidad Iberoamericana and was hired two weeks before graduating. "I went into the program knowing almost nothing," he says. "I knew quite a lot by the time I started working here."

Made in Mexico, From Scratch

Mastretta MXT

Mexico had 579,814 students enrolled in engineering programs in 2011, double the number five years earlier and more than Brazil or Germany, according to data from the United Nations Educational, Scientific, and Cultural Organization (Unesco). The country has almost 4.9 engineering students per 1,000 people, compared with 3.6 in the U.S. A Mexican company, **Mastretta Cars**, has used local engineers to design and build most of a high-powered sports car, the Mastretta MXT, which sells in Mexico and the U.S. for $63,000.

It typically takes 1.3 engineers in Mexico to do the work of one in the U.S., says Cary Leslie, **Chrysler Group**'s director of engineering for Mexico. In part that's a function of experience: Engineers in Mexico have been on the job an average of about eight years, compared with 25 in Michigan. Labor costs including benefits for Mexican engineers are typically 40 percent of U.S. costs, according to Ford and Chrysler.

Automakers hiring engineers in Mexico are catching up to companies such as **General Electric**, which has about 1,600 engineers working in Querétaro on turbines to sell to makers of jet engines and power plants. **Siemens** has opened three engineering centers in Mexico in the last three years to work on electrical systems, according to Louise Goeser, chief executive officer at the company's Mexico and Central America unit.

More such jobs will open up routes to the middle class. Engineering graduates, the most sought-after by employers, usually make as much as 45 percent more than people with nontechnical degrees, according to the Mexico City office of Michael Page International, a recruitment company. "As that value chain expands, from manufacturing to suppliers, from manufacturing to research and development, you get a much broader, stronger economy," Goeser says.

Price
$63,000
base price

2014 production
51 cars
up from 15 cars in 2013

"All the engineering is done here in Mexico. Obviously, we bought some parts abroad, but it's all designed in Mexico." —*Mastretta Cars CEO Conrad Giesemann*

Outside a few world-class companies and universities, Mexico has a long way to go to match educational levels in the U.S., Germany, and South Korea. Its 8.5 average years of schooling for people older than 25 is almost a year less than in Argentina and almost five years less than in the U.S., according to Unesco. With the exception of Chile, Mexico spends the smallest share of gross domestic product on research and development among the 34 countries in the Organisation for Economic Co-operation and Development.

The expansion of auto manufacturing could sharpen competition for the highly skilled, says Ricardo Haneine, an auto consultant with A.T. Kearney in Mexico City. "We can get a lot of low-level assembly workers, and we can train them with the basic skills," he says. "But if you go to more advanced technical skills, we don't have enough people."

Global automakers have announced $12.7 billion in Mexican investments over the last three years, according to the Center for Automotive Research in Ann Arbor, Mich. That includes a $2 billion **Nissan Motor** plant in Aguascalientes that opened in November, the company's third in Mexico. **Honda Motor** and **Mazda Motor** are opening factories in a nearby state next year, and **Volkswagen**'s Audi is building a $1.3 billion plant east of Mexico City.

After gaining a few years' experience, engineers at a **Delphi Automotive** technical center in Ciudad Juárez, across the border from El Paso, have a similar skill level as those in developed countries, says Duane Collins, the center's director. About 1,300 engineers in Ciudad Juárez design engine parts, transmission components, fuel pumps, and electronics for use in auto factories around the world.

General Motors is increasing its emphasis on design in Mexico. About 400 of its 640 engineers in Toluca, 40 miles west of Mexico City, design components such as door panels, air conditioning systems, and noise reduction equipment, says David Rojas, head of GM's Toluca engineering operation. The city is also home to a Nissan technical center with almost 500 engineers and a Chrysler operation with 350.

The next step may be for Mexico to play a leading role in developing an entire vehicle for mass production, from the chassis to the body, says Juan Santillan, who oversees product-development engineering for the Ford Fiesta at its Cuautitlán plant. Santillan returned to Mexico in 2009 after spending nine years at Ford plants in Michigan, Japan, and Germany. "When I left Mexico, we were 60 or 70 engineers," he says of the product-development group. Now they have the critical mass to do something memorable—and Mexican.
—*Brendan Case*

The bottom line Carmakers have invested $12.7 billion in Mexico in the last three years. Skilled engineers are one reason.

Commodities

A Dismal Bordeaux Vintage Hits the Market

▶ A disappointing harvest may deflate prices further

▶ "Old-fashioned ... buyers are not prepared to pay the new prices"

Wine producers in France's Bordeaux region have enjoyed some fat years. Vintages from 34 top labels were fabulous enough to command average price hikes of 204 percent and 12 percent in 2009 and 2010, respectively. Chinese demand sustained the momentum.

The vintages of 2011 and 2012, though, were not so fabulous: British wine critic Jancis Robinson calls 2011 "a forgettable year," and says most Bordeaux from 2012 "have a lack of depth and persistence."

Prices have dropped some, but not nearly enough to please customers who are still paying 30 percent more than in 2008, before the great takeoff. Demand has fallen, and the middlemen and châteaux have been stuck with unsold stock from 2011 and 2012.

The 2013 Bordeaux looks the least fabulous of all the recent vintages. Damaged by cold weather in May, summer hailstorms, and rain and rot at harvest time, the grapes that survived were picked early and yielded the smallest harvest since 1991. Wine produced in Bordeaux, France's most important wine region, will drop 23 percent this year, to 543 million bottles, according to French government data. Top-ranked châteaux may cut prices for the 2013 vintage more than 25 percent starting next April, when the wine's price is determined. Weakened demand and perceived lower quality are behind the probable price drop, says Allan Sichel, the chairman of Bordeaux's guild of wine merchants, the Union des Maisons de Bordeaux (UMB).

The crummy harvest comes as investors have soured on Bordeaux. After reaching a record in 2011, London's Liv-ex Fine Wine 50 Index of leading Bordeaux wines, which received their current classifications (a ranking by quality) under Emperor Napoleon III in 1855, is heading for a third straight annual decline, tumbling 7.9 percent from a recent peak in March.

Sales of red Bordeaux to China, the biggest importer, fell last year for the first time since 1999. The Chinese haven't lost their appetite for French reds; they've just been hit with ▶

Liv-ex Fine Wine 50 Index

GRAPHIC BY BLOOMBERG BUSINESSWEEK. DATA: LIV-EX

Correlations

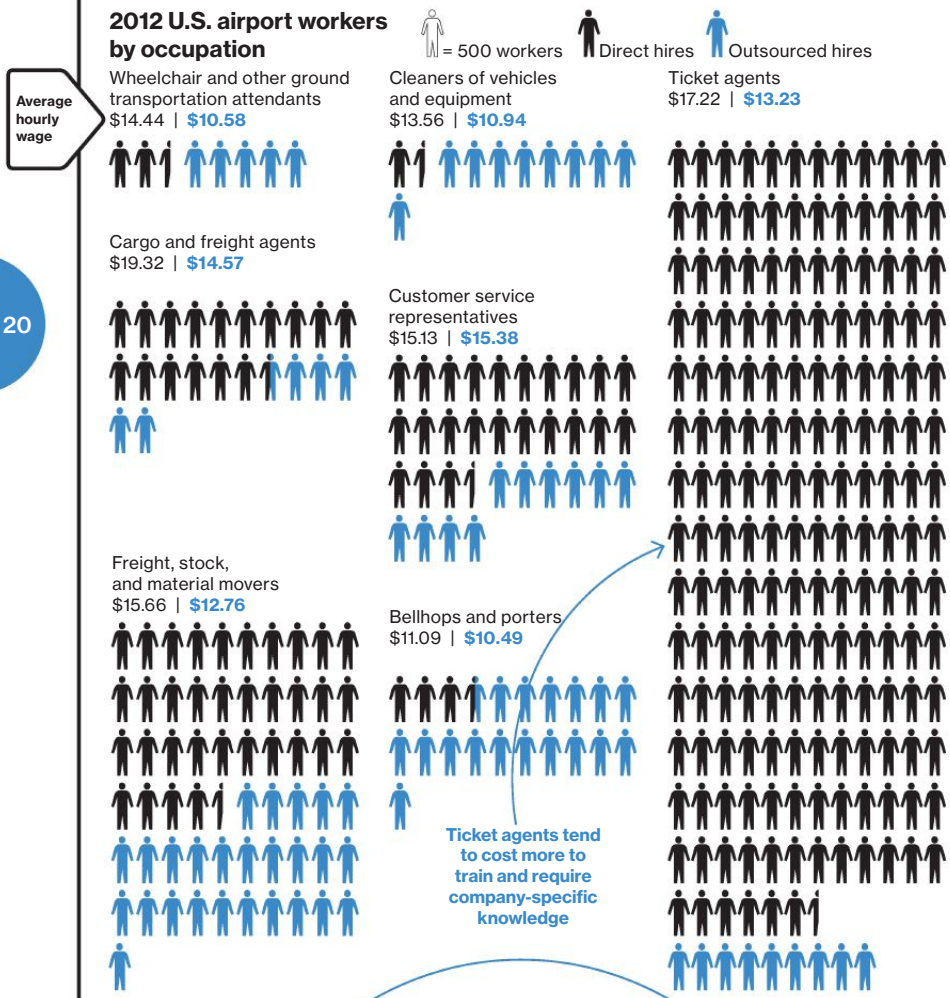
By Mark Glassman

One Job, Two Wages

Researchers have long suspected outsourcing is linked to a decline in pay, but it's hard to prove. A recent study from the University of California at Berkeley and Simon Fraser University in Vancouver used the U.S. Department of Labor's employment database to study outsourcing at American airports. The study, funded by the Service Employees International Union, found outsourced workers tend to make less than direct hires in the same job.

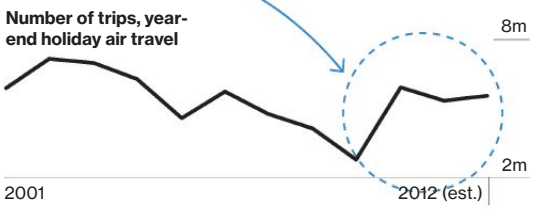
26% Air-transport-related jobs outsourced in 2011

2012 U.S. airport workers by occupation



Passenger flights during the Christmas and New Year's period

Outsourced or not, airport staffers have been dealing with many more holiday travelers since the end of the recession



GRAPHIC BY BLOOMBERG BUSINESSWEEK. DATA: UNIVERSITY OF CALIFORNIA; SIMON FRASER UNIVERSITY; DEPARTMENT OF LABOR; AAA

◀ sticker shock over the prices of high-end Bordeaux. Exports to China of less expensive French wines from the regions of Languedoc-Roussillon and Côtes du Rhône rose, trade data show.

Miles Davis, a partner at Wine Asset Managers in London, says buyers aren't willing to absorb the Bordeaux that the Chinese no longer want. "The old-fashioned Bordeaux buyers are not prepared to pay the new prices," says Davis of the mostly British and French consumers who find it too expensive now. A 12-bottle case of 2009 Château Lafite Rothschild sold for £6,750 ($10,864) on the Liv-ex market on Oct. 18, a record low for that wine. That's down from £10,000 in May 2010, immediately after the vintage's release, and less than half the £14,300 reached in November 2010 when Chinese demand was peaking.

Bordeaux's classified estates—the top producers, including châteaux Margaux, Haut-Brion, and Lafite Rothschild—sell wine *en primeur*, or still in the cask, to merchants in a futures market. Many 2012 Bordeaux wines quoted on the Liv-ex exchange have dropped below the prices at which they were first offered. The average price of all 344 Bordeaux wines from 2012 offered en primeur was down 7.6 percent from the 2011 vintage, *Decanter* magazine reported in June, citing data from wine broker Tastet & Lawton.

The high prices of top-classified Bordeaux of recent years have sent investors looking for more affordable wine from other regions such as Champagne and Italy's Tuscany, as well as older Bordeaux vintages. "The Bordeaux market is dead. People are fed up with en primeur pricing," Davis says.

The latest vintage may bring the aggressive pricing to a halt. "No one will be excited about the 2013 vintage, so it'll be complicated to justify high prices," says Sichel, of the UMB. The young wine that he's tasted so far doesn't have "a lot of depth," Sichel says, and may have difficulty developing much complexity as it ages. Says Chris Smith, an investment director at the Wine Investment Fund in London: The châteaux need to price the 2013 Bordeaux "realistically" or "risk losing the market completely." Ⓑ

—*Rudy Ruitenberg*

The bottom line Overly ambitious pricing and China's diminishing thirst for fancy Bordeaux are weakening producers' pricing power.

Ⓑ **Edited by Christopher Power**
Businessweek.com/global-economics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December 2 — December 8, 2013

Golden Hellos

▶ **Big CEO signing bonuses are the latest compensation practice to draw criticism from activists**

▶ **"It's up to the board to make sure it's good for shareholders. I consider a request for cash a red flag"**

For years corporate boards have used so-called golden handcuffs (retention incentives) to keep treasured chief executive officers in the fold or provided golden parachutes (severance packages) to ease their departures. Lately, another gilded pay practice has taken hold: golden hellos, or multimillion-dollar signing bonuses used to get CEO candidates to join the team. The number of U.S. companies in the Russell 3000 Index and Canadian ones in the S&P/TSX 60 Index making upfront payments to executives has risen to more than 70 this year, from 41 in all of 2012, according to governance advisory firm GMI Ratings. Among this year's biggest: **Zynga**'s $45 million package to attract game industry veteran Don Mattrick.

Yet high-profile flameouts such as Ron Johnson show that such tactics can quickly lose their glitter—at least for shareholders. **J. C. Penney** fired CEO Johnson in April, 17 months after giving him a signing bonus of $52.7 million in shares to recruit him from Apple. "Investors should be skeptical of golden hellos, which represent pay decoupled from performance and provide no retention incentives," says Lucian Bebchuk, a Harvard Law School professor who has studied CEO pay.

Some welcome payments can yield disappointing returns: J. C. Penney shares slumped 50 percent during Johnson's reign, while **Hewlett-Packard**'s dropped 46 percent under Léo Apotheker, ousted in 2011 just 10 months after getting $8.6 million in a signing bonus and relocation benefits. In total, he was entitled to $34.7 million in cash and stock for less than one year's work.

Some directors agree front-loading such largesse is bad governance. "The incentive should be they will come to the company and perform and be rewarded," says Jon Luther, chairman of Arby's Restaurant Group, a director at Six Flags Entertainment and Brinker International, and former CEO of Dunkin' Brands. Candidates for high-level positions who asked for signing bonuses where he's been a board member have been rejected in favor of those who didn't, he says, declining to identify the companies and candidates. Luther says he never asked for a bonus to take a job and was never offered one: "I said I'll get it done, and you can take care of me when I succeed."

Golden hellos are often a sign ▶

ILLUSTRATION BY STEPH DAVIDSON

The former Apple Stores chief lasted 17 months

Biggest CEO Signing Bonuses

Company	CEO	Previous position	Signing bonus	Stock price during tenure
J. C. Penney Plano, Tex.	**Ron Johnson*** Age: 55	Head of retail at Apple; formerly an exec at Target	$52.7m	11/1/11 **$31.71** — 4/8/13 **$15.87**
Zynga San Francisco	**Don Mattrick** Age: 49	President for interactive entertainment at Microsoft	$45m	7/8/13 **$3.29** — 11/25/13 **$4.50**
Best Buy Richfield, Minn.	**Hubert Joly** Age: 54	CEO of hotelier Carlson, after a stint at Vivendi's video game unit	$16.3m	9/4/12 **$18.02** — 11/25/13 **$39.73**
Chesapeake Energy Oklahoma City	**Robert Lawler** Age: 47	Senior vice president at Anadarko Petroleum	$9.5m	6/7/13 **$22.00** — 11/25/13 **$26.27**
Hewlett-Packard Palo Alto, Calif.	**Léo Apotheker*** Age: 60	CEO of German software maker SAP	$8.6m	11/1/10 **$42.49** — 9/22/11 **$22.80**

*DEPARTED; DATA: COMPILED BY BLOOMBERG

◀ of other compensation dysfunctions, says Greg Ruel, a GMI senior research analyst. On average, companies dinged by GMI for giving out big upfront payments also have received grades of D for their overall pay practices. **Chesapeake Energy** and **Best Buy**, two that have been flagged by GMI for offering golden hellos, also in recent years lost so-called say-on-pay votes, nonbinding stockholder polls on pay plans granted by their boards. Those ballots were evidence of shareholder dissatisfaction—and ultimately prompted changes in the companies' compensation practices.

In April, the same month as Johnson's ouster, golden hellos again were thrust into the spotlight, this time at Toronto-based **Barrick Gold**. Dissenting investors, including Canada's six largest pension funds, opposed an $11.9 million cash welcome package to Co-Chairman John Thornton, a former Goldman Sachs president. (Although the bonus wasn't rolled back, Barrick did adopt other governance changes.) "This is the kind of situation where you are not getting anything in advance, but yet you have to pay upfront for the hopes and the aspirations of what will be delivered down the road," says Robert Gill, a Toronto-based fund manager at Aston Hill Financial, which manages $7.6 billion in assets, including Barrick shares. "We don't think that's commensurate with how the industry should remunerate people."

> "This is the kind of situation where you are not getting anything in advance, but yet you have to pay upfront for the hopes ... of what will be delivered."
> —*Robert Gill*

GMI decided to include golden hellos in its rating system in April because of evidence the bonuses were getting bigger, Ruel says. The payouts have risen even as CEO turnover last year fell to the lowest level since at least 2004.

Companies often justify golden hellos by saying they compensate for pay that new CEOs had to forgo for leaving their previous employers. Such payments partly explain why hiring an outside CEO costs about one-third more than promoting from within, says Chris McGoldrick, a senior research analyst at compensation tracker Equilar. Board compensation committees may have to consider that as they search to fill CEO vacancies at **Microsoft**, **Lululemon Athletica**, and J. C. Penney, which is seeking a replacement for its interim CEO. Last year about 26 percent of new S&P 500 CEOs were hired from outside the company, according to executive recruiter Spencer Stuart.

"The board has to decide if they want to pay the freight to move the CEO from one job to another," says David Larcker, a Stanford Graduate School of Business professor who has done research on executive compensation. "It's up to the board to make sure it's good for shareholders. I consider a request for cash a red flag, though."

Barrick Chairman Peter Munk told investors who opposed Thornton's bonus at an April shareholders' meeting that he needed the former banker, "a highly desirable, well-known commodity," to secure access to governments and protect against possible losses of mineral rights. Some investors aren't so sure. Says Aston Hill's Gill: "I do realize Thornton has a big name, but now he really has to deliver." In an e-mail, Barrick spokesman Andy Lloyd said the gold producer's board is in the process of strengthening governance practices through the addition of independent directors and improvements to executive compensation.

At J. C. Penney, Johnson got his November 2011 signing bonus in restricted stock to make up for the compensation he had to forfeit at Apple, where he'd led retail operations. Johnson couldn't be reached for comment. Kristin Hays, a J. C. Penney spokeswoman, declined to comment.

Sometimes golden hellos do pay off for investors. Best Buy's shares have more than doubled since the consumer electronics retailer lured former hospitality and video game executive Hubert Joly to be its CEO in 2012 with a welcome package that included a $3.5 million cash bonus and equity grants and options valued at almost $13 million. For Zynga, a social gaming pioneer whose games have faded in popularity, it's too soon to tell whether shareholders will benefit from Mattrick's hiring. Although the stock has risen since the former Microsoft president of interactive entertainment arrived in July and began cutting expenses and engineering a restructuring, it still trades at less than half its 2011 initial public offering price. Dani Dudeck, a Zynga spokeswoman, declined to comment.

Some management experts say directors must try harder to compare potential CEOs' relative value. "The board has to be careful not to fall in love with any one candidate," says James

Post, a governance and ethics professor at Boston University School of Management. "You have to look for a good candidate at a good price, not a good candidate at any price." —*Jeff Green*

The bottom line The number of companies granting CEO signing bonuses is up more than 70 percent so far in 2013 from last year.

Nutrition

Will Nobody Speak Up for Wheat?

▶ As gluten has come under attack, food makers have remained silent

▶ "Large companies have learned not to overreact to these flash trends"

Although fewer than 1 percent of Americans suffer from celiac disease, an autoimmune disorder that requires them to avoid gluten, almost one in three people say they are cutting back on products containing the protein found in wheat, barley, and rye, according to NPD Group. Many are influenced by antigluten books such as *Wheat Belly* and *Grain Brain*, as well as celebrities who have embraced the gluten-free lifestyle, such as actors Zooey Deschanel and Gwyneth Paltrow. Consumption of flour in the U.S. is at a 22-year low, says the U.S. Department of Agriculture.

That's created a conundrum for cereal and other makers of products that contain gluten. Fight back, and they risk offending people with celiac disease or calling attention to antigluten activists such as William Davis, author of *Wheat Belly*, who calls wheat "the world's most destructive dietary ingredient." Instead, companies including **General Mills** and **Kellogg** are creating pricier gluten-free versions of their products, while leaving industry groups to defend their regular fare. The U.S. market for gluten-free foods will climb from $4.2 billion in 2012 to $6.6 billion by 2017, according to researcher Packaged Facts.

"Large companies have learned not to overreact to these flash trends," says Mark Lang, a food marketing professor at Saint Joseph's University in Philadelphia. "There is nothing to gain, and you have everything to lose."

Fifteen years ago, diets that limited carbohydrates sent sales of white bread and pasta plummeting. Out of that crisis rose organizations such as the Whole Grains Council, which encourages consumers to eat more brown rice and whole wheat bread. The group counts General Mills and **PepsiCo**'s Frito-Lay snack unit among its members. Cynthia Harriman, the group's director of food and nutrition strategies, says her initial reaction to *Wheat Belly* was that it was "such nonsense." Once she realized gluten-free "was not going away," she used the council's website to point consumers toward grains such as rice and corn that contain no gluten.

1 in 3

Americans cutting back on gluten, though just 1 percent of the population has celiac disease

Spying an opportunity, Kellogg introduced a gluten-free version of its Rice Krispies cereal in 2011. A variety of PepsiCo's Doritos nacho cheese tortilla chips without the protein came out the same year. General Mills sells more than 400 gluten-free products, including versions of its Pillsbury cookie dough and Betty Crocker baking mixes. Sales of its Chex cereal, available in seven varieties without gluten, have jumped by at least 10 percent in each of the past three fiscal years, while the $6 billion breakfast cereal category has remained stagnant. Still, General Mills has been careful not to align itself with any of the antigluten gurus. "There's a new diet book every week, and most of them really should go without comment," says company spokeswoman Kirstie Foster. "We're responding as we think we should."

The reluctance of grain producers to defend gluten surprises Michael Pollan, author of *The Omnivore's Dilemma* and other books on nutrition. "The industry has been flat-footed in their response," he says. "They should be reminding people that gluten is protein, generally thought of as a healthy nutrient compared to fats or carbs." —*Matthew Boyle*

The bottom line Major U.S. food companies have refrained from challenging the gluten-free trend for fear of sparking a backlash.

U.S. sales of gluten-free products

Travel

An Unlikely Captain Takes Carnival's Helm

▶ With no prior cruise experience, Arnold Donald is sailing upstream

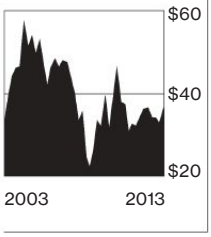
▶ "I had to think about whether I was the right person at this time"

Arnold Donald had been on the board of **Carnival** for 12 years when he got a call in June from the cruise company's lead director, Stuart Subotnick. It was an offer to succeed Micky Arison as Carnival's chief executive officer, and Donald was incredulous. "OK, what's the call really about?" he asked.

Donald's skepticism was understandable. Arison, the son of Carnival's founder, had run the company for 34 years; Donald, a former **Monsanto** executive, had no prior cruise-operating experience. Carnival—the world's largest cruise company with 10 brands ranging from the low-cost Carnival to the pricey 173-year-old British Cunard Line—had been in crisis since its *Costa Concordia* ran aground off the Italian coast in 2012, killing 32 people. That was followed by more incidents this year, including a fire aboard the *Carnival Triumph* in February that further tarnished the company's ▶

BREAD: FRANK BEAN/GETTY IMAGES (2); DONALD: CW. GRIFFIN/MIAMI HERALD/MCT/NEWSCOM; SKY, ROPE, HAT: GETTY IMAGES (3)

Carnival's stock treads water



◀ image with extensive news video of passengers stranded at sea. Says Donald, who pondered the offer for two days: "I had to think about whether I was the right person at this time for Carnival."

Since taking over on July 3, he's been implementing changes that include a $700 million investment in shipboard fire prevention and backup power systems, a new marketing campaign, and an effort to get Carnival's various cruise lines (which target different economic or demographic groups) to collaborate and become more efficient. "We started out with a few ships," he says. "We grew to a fleet. And now we have an armada. We have huge opportunities to take advantage of our scale in terms of creating demand and creating new revenue."

Carnival shares have risen 3.1 percent on Donald's watch. Yet the stock remains more than one-third below its 2004 peak. Since the Feb. 10 *Triumph* mishap, Carnival's shares are down 7.7 percent, lagging the advances of rivals **Royal Caribbean Cruises** (23 percent) and **Norwegian Cruise Line Holdings** (22 percent).

Although a novice in the travel industry, Donald is no stranger to consumer businesses. After earning a mechanical engineering degree from Washington University in St. Louis, he joined Monsanto in 1977. He supervised the company's Roundup weed killer business—helping transform it into a lawn-care staple for suburban homeowners—before agreeing to lead a private equity firm's acquisition of Monsanto's Equal sweetener operation in 2000.

Carnival was already deep into a public-relations makeover when Donald became CEO. After the *Triumph* incident, which left 3,100 passengers without enough food or working toilets for four days, the company introduced a "vacation guarantee," promising to refund money and fly guests home if they're not happy with their cruise.

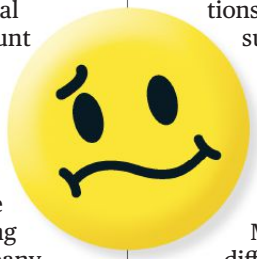
"We have huge opportunities to take advantage of our scale in terms of creating demand and creating new revenue"
—*Arnold Donald*

In September, Carnival rolled out a $25 million ad campaign, its largest in five years. The line sought heartwarming stories from customers, and more than 30,000 responded. The resulting Moments That Matter spot is a montage of home movies taken by passengers on its ships. "This marketing campaign is very different than anything we've ever done before," says Gerald Cahill, CEO of the Carnival Cruise Lines brand. "We said, 'Let's let our guests tell our story for us.' "

Among Donald's first steps were meetings with travel agents to repair relations frayed in recent years as the company put more emphasis on automated online bookings. That strategy reduced agent commissions. In recent months Carnival has enhanced its travel agent website and created a bonus program for salespeople. "Carnival had been sort of aloof, but now they're coming back," says John Maguire, founder of online agency CruiseDirect.com.

Donald's also looking for ways that the company's cruise lines can work together, such as jointly obtaining space at ports. Currently, each line negotiates separately. Together they could get better locations and pricing, he says. Still, Wells Fargo analyst Timothy Condor says it likely will be 2015 before the benefits from such changes and the brand rebuilding begin to bear fruit.

In addition to about $50 million in rescue and refund costs for the *Triumph* incident, the Carnival line has been forced to discount prices to fill its ships. The average cost of a Carnival brand cruise is down 15 percent this quarter from a year earlier and 9 percent for voyages scheduled for the first quarter of 2014, according to Barclays. The parent company has lowered its 2013 earnings forecast three times, warning in September that it may lose up to $17 million this quarter. It said advance bookings are down through the first half of 2014.



Jeffrey Sonnenfeld, a management professor at Yale University who sat on the board of rival NCL, says Carnival's board erred in choosing industry novice Donald and should have explored other candidates. He doubts the steps taken so far will win back customers. "Their ad hoc stabs in the dark aren't going to rebuild the fabric of trust that's been unraveled," he says.

Donald says that ultimately customers will be the judge of whether Carnival's board should have tapped one of its own. If he succeeds, the CEO says, "shareholders will be happy, and no one will care how I got this job."
—*Christopher Palmeri and Carol Massar*

The bottom line To draw travelers, Carnival's midmarket cruise brand has had to cut prices by 15 percent this quarter from last year.

Retailing

Wal-Mart's New Chief Faces Old Woes

▶ Doug McMillon has big challenges abroad and at home

▶ "He's ... one of the few most senior executives who knew Sam Walton"

The incoming chief executive officer of **Wal-Mart Stores**, 47-year-old Doug McMillon, is a company man and a native of Arkansas—the retailer's home base. By most accounts he's well-liked, engaging, and accessible. The $470 billion empire he'll be running come February, when Mike Duke retires, could use a good dose of all that. But it also needs a lot more: The world's biggest retailer must contend with slowing sales in the U.S. and abroad, an underwhelming digital presence, allegations of corruption at its Mexican subsidiary, and worker protests over low wages. "Wal-Mart, and all of retail, is at a crossroads," says Carol Spieckerman, the founder of Newmarketbuilders, a retail strategy firm. "Wal-Mart's sheer size makes it difficult to drive growth. Most retailers are happy if they're not going backward."

McMillon first worked at Wal-Mart as a warehouse employee during the summer of 1984. He graduated from the University of Arkansas, and in 1990, while earning an MBA from the University of Tulsa, he returned to the retailer—and never left. After holding various merchandising positions, McMillon was named CEO of Sam's Club in 2006. He replaced Duke as head of Wal-Mart's international operations three years later. "He's really been a CEO in training," says David Schick, a Stifel Nicolaus analyst. ▶

DATA: COMPILED BY BLOOMBERG

Briefs

By Kyle Stock

Changing Suitors

In the bargain-suit business, the hunted has become the hunter. Less than two weeks after rebuffing a bid from *Jos. A. Bank*, *Men's Wearhouse* has turned around and offered to buy its rival at $55 a share. Although Men's Wearhouse is roughly twice the size of its target by sales and number of stores, Jos. A. Bank has more cash on hand and has been much more profitable in recent years.

Drivers for **Uber**'s mobile-based car-booking service are about to get a bargain on new cars. The fledgling company has struck deals for cheaper rates on vehicles from General Motors and Toyota.

In Switzerland, home to five of Europe's 20 best-paid CEOs, voters overwhelmingly rejected a proposal to limit executive pay to 12 times that of junior employees. Opponents of the pay cap argued that it would tarnish the country's probusiness reputation. *Rogers Communications* agreed to pay $4.9 billion for rights to National Hockey League games for the next 12 years. The deal marks the first time the NHL has granted Canadian rights to a single company. Rogers, a media conglomerate that is Canada's largest wireless carrier, will air the games on tablets and mobile phones, and has also made agreements to let other broadcasters carry some games. *Boeing*'s nascent 787 model has hit yet more turbulence as U.S. regulators ordered airline pilots to steer some of the planes clear of thunderstorms. So-called Dreamliners equipped with General Electric engines have shown signs of icing up and losing power in bad weather. GE plans to fix the problem with software modifications. Asian shoppers and higher prices continue to put a shine on *Tiffany*. Profit at the jeweler surged 50 percent in the recent quarter, far more than analysts expected. Sales in Asia increased 27 percent, and the company's gross margin swelled.

4.8%

Estimated decline in the number of turkeys raised in the U.S. this year. High corn prices discouraged farmers from fattening up birds.

"It's better than Scotch."

Peter Lewis, marijuana advocate and chairman of insurer Progressive, who died on Nov. 23 at age 80

◀ That's McMillon's official bio. Then there's his cultural pedigree. "He's probably one of the few most senior executives who knew Sam Walton. That's a huge thing for Wal-Mart," says Joe Feldman, senior managing director of researcher Telsey Advisory Group. The Walton family owns slightly more than half of Wal-Mart's stock, and Walton's eldest son, Rob, is chairman.

In the U.S., Wal-Mart's lower-income customers are struggling amid persistent unemployment and higher payroll taxes. Many seem to have fled to dollar stores in search of even lower everyday prices. Other shoppers are frustrated, because Wal-Mart doesn't always have enough workers to keep its shelves well-stocked. And **Amazon.com** has lured away customers with its low prices and quick shipping. In November, Wal-Mart reported its third quarter of declining sales at U.S. stores open for more than a year—a key measure of a retailer's well-being. And though Wal-Mart began offering Black Friday deals a week early, it also said it expects same-store sales during the holiday season to be "relatively flat."

Under McMillon, Wal-Mart's international business—29 percent of the company's sales last fiscal year—hasn't been faring too well, either. In China, Wal-Mart faces competition from increasingly savvy local companies even as more shoppers migrate online. The giant retailer plans in the next three years to close as many as 30 poorly performing stores in the mainland and open about 100 in smaller cities.

Wal-Mart this year broke with its venture partner in India, delaying its ambitious plans to build hundreds of supercenters there. And the retailer is cooperating with a federal investigation into allegations that employees in Mexico used bribes to secure building permits—allegations that predate McMillon's tenure.

McMillon just got the job he's been groomed for. Now everyone is waiting to see if all that experience pays off.
—*Susan Berfield*

The bottom line Wal-Mart has seen sales at U.S. stores open for at least a year fall for three straight quarters.

Edited by James E. Ellis
Businessweek.com/companies-and-industries

MARVIN FONG/THE PLAIN DEALER/LANDOV

December 2 — December 8, 2013

Whole Woman's Health has had to stop abortions at some of its Texas clinics

The Vanishing Abortion Clinic

▶ A Republican push to regulate clinics more heavily is accelerating shutdowns

▶ "People who have influence work from within to enact change"

Amy Hagstrom Miller fired 34 people in November. "It's hard to look people in the eye and say they don't have a job anymore, not because of anything they or we did incorrectly or because we weren't caring for women in a fabulous way," she says. "It's illogical." Miller, founder and chief executive officer of **Whole Woman's Health**, based in Austin, had to stop or sharply curtail abortions at four of her six Texas clinics because a new state law requires doctors performing the procedure to have admitting privileges at local hospitals. To get an abortion, the mostly poor women who relied on Miller's establishment in McAllen, on the state's border with Mexico, will now have to drive 150 miles to Corpus Christi or to the local flea market, where illegal, do-it-yourself drugs start at $15 a pill.

At least a dozen clinics in Texas have closed their doors or stopped offering the procedure in the past month after a federal appeals court and the U.S. Supreme Court let the new statute take effect. The Texas law is emblematic of a shift in the tactics of abortion opponents: State-level laws targeting women and providers have become a more effective tool than the past noisy clinic blockades and violence against doctors. Since 2011, legislatures in 30 mostly Republican-controlled states have passed 203 abortion restrictions, about as many as in all of the prior decade. At least 73 clinics have closed or stopped performing abortions. New laws are responsible for roughly ▶

PHOTOGRAPH BY JARED MOOSSY FOR BLOOMBERG BUSINESSWEEK

Miller

◀ half of the closures, while declining demand, industry consolidation, and crackdowns on unfit providers have also contributed to the drop.

Laws aimed at the clinics, such as mandates to widen hallways and install high-tech surgical scrub sinks, are proving more powerful than those aimed at patients, such as waiting periods or parental notification requirements. "People who don't have power protest on the street," says Cheryl Sullenger, senior policy adviser for Operation Rescue, an anti-abortion group based in Wichita. "People who have influence work from within to enact change."

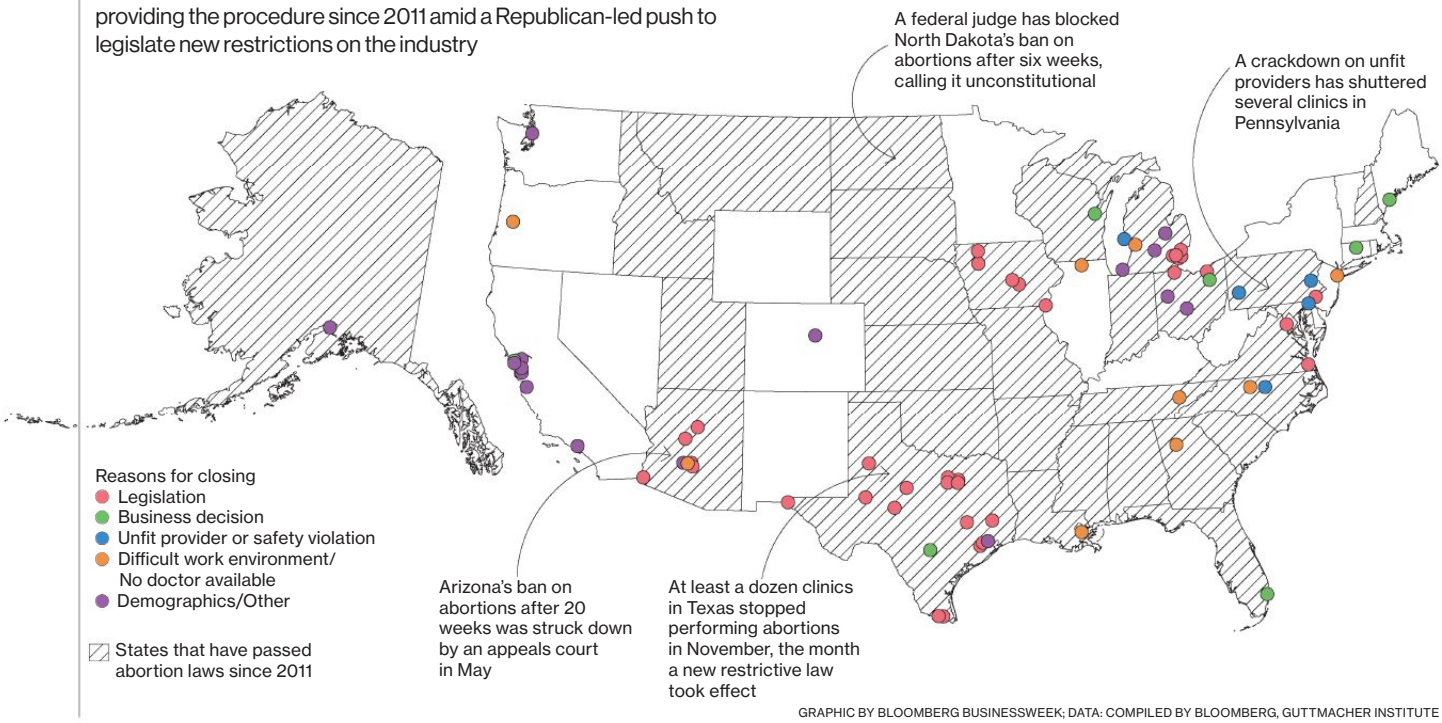
In 1992 the U.S. Supreme Court ruled states could pass restrictions that don't present an "undue burden" to women seeking abortions, made legal in all 50 states by the 1973 *Roe v. Wade* decision. Courts are now clogged with challenges to recent state laws testing what "undue burden" means. The number of clinic closings would probably be higher were it not for legal fights that have prevented some laws from taking effect.

Nearly half the 6.7 million pregnancies in the U.S. each year are unintended, and almost half of those end in abortion. Rates of both unintended pregnancy and abortion are higher among minorities and the poor. The abortion rate hit 19.4 per 1,000 women in 2005, the lowest since *Roe v. Wade*, and has remained steady since. The ranks of clinics have been thinning since the late 1980s, when the number of large nonhospital providers—those that performed 400 or more abortions per year—peaked at 705, according to the Guttmacher Institute, a New York-based reproductive health research organization. By 2008, the most recent year for which data are available, the number had fallen to 591.

Both sides in the debate have a stake in the proposition that restricting access to clinics is holding abortion rates down. Social scientists say that's not the whole story. Increasing

Landscape of Closures

Nationwide, at least 73 abortion clinics have shut down or stopped providing the procedure since 2011 amid a Republican-led push to legislate new restrictions on the industry



GRAPHIC BY BLOOMBERG BUSINESSWEEK; DATA: COMPILED BY BLOOMBERG, GUTTMACHER INSTITUTE

cultural acceptance of single motherhood, the decline in pregnancies that accompanied the recession, and more prevalent use of contraceptives, which are more effective than they have ever been, are also factors. A 2012 paper from the National Bureau of Economic Research found that if 31 states outlawed abortion tomorrow, the majority of women would still travel to states where it remained legal. But the impact on those unwilling or unable to travel could produce a 15 percent decrease in abortions nationally and as much as a 4.2 percent rise in the birthrate.

Miller scored a small victory at the end of November when her doctors in the Fort Worth area won hospital admitting rights, allowing her to resume abortion services. (No such prospects exist in McAllen, where Miller says one hospital even refused to provide an application.) Some big battles still lie ahead, though. A provision of the Texas law that takes effect in September requires abortion clinics to become hospital-like outpatient surgical centers—complete with wider hallways, janitors' closets, and backup generators. That will force Miller to find new quarters for five of her clinics or make costly upgrades. "I'm just sort of stunned," she says. "I don't have the convenience of having time to grieve."
—*Esmé E. Deprez*

The bottom line By moving the fight over abortion rights from the streets to legislative chambers, Republicans are getting results.

Diplomacy

Congress Could Derail A Deal With Iran

- Hawks in the Senate are in no mood to compromise
- There is an "urgent need for Congress to increase sanctions"

When U.S. Secretary of State John Kerry joined the nuclear negotiations at the InterContinental Geneva on Nov. 23, he employed the oldest negotiating trick in the book, casting Congress as the bad cop to the Obama administration's good cop. Kerry told Iranian Foreign Minister Mohammad Javad Zarif that if they failed to reach an agreement that day, the Obama administration would be unable to prevent Congress from approving additional sanctions. Less than 24 hours later, Kerry and Zarif walked into the hotel lobby to announce that world powers had struck a deal with Iran to temporarily freeze its nuclear program.

In the face of criticism from American allies in the Middle East and their sympathizers in Congress, administration officials have insisted that the Geneva agreement is just the first step toward a more far-reaching disarmament deal. But such a pact will require that the White House promise not only to forestall new sanctions but also to dramatically ease those in place. And that depends on cooperation from Congress, where Iran hawks outnumber the doves. On Nov. 25, Senate Majority Leader Harry Reid (D-Nev.) said the Senate would review the deal "and see if we need stronger sanctions" after members return from the Thanksgiving break.

The method for removing a given set of sanctions depends on how those were imposed in the first place. If they're the product of an executive order, as are many existing sanctions against Iran, removing them requires only that the White House decide to stop enforcing them. That's how the administration will make good on its promise to Iran to restore access to $7 billion in foreign assets, part of the interim agreement.

Removing sanctions imposed by Congress is much tougher. Despite the gridlock of the past several years, bipartisan majorities have managed to cooperate on several rounds of sanctions. In 2010, Congress passed the Comprehensive Iran Sanctions, Accountability and Divestment Act, which targeted the country's purchases of gasoline. The following year, it attached an amendment to the National Defense Authorization Act (against the Obama administration's advice) that imposed sanctions on any foreign banks conducting business with the Central Bank of Iran. Rescinding those banking sanctions, a source of currency weakness and rampant inflation in Iran, will undoubtedly be among Tehran's top priorities in a final agreement.

Sooner or later the administration will have to confront the many members of Congress whose goals for the nuclear negotiations diverge sharply from its own. Although the interim agreement essentially concedes that Iran will maintain an enrichment program in any future compromise, many legislators have declared that Iran should not be allowed any nuclear capabilities.

"How do you define an Iranian moderate?" Senator Mark Kirk (R-Ill.), who co-sponsored the most recent round of sanctions to pass Congress, asked recently. "That's an Iranian who's out of bullets and money." After the Geneva deal was announced, Senator Marco Rubio (R-Fla.) declared: "There is now an even more urgent need for Congress to increase sanctions until Iran completely abandons its enrichment and reprocessing capabilities." A few Democratic senators have also pronounced themselves against the interim accord: New York's Charles Schumer called it "disappointing" in a written statement, and New Jersey's Bob Menendez said it gave too much away.

That may all turn out to be grandstanding. But the talks could be undermined if Congress seeks to pass legislation setting conditions on future negotiations and on the eventual removal of sanctions. A bipartisan congressional group is pushing a bill that would automatically impose sanctions against Iran if it fails to agree to a comprehensive deal during the six months covered by the interim agreement. The bill seeks to define in advance the boundaries of an acceptable comprehensive agreement.

"How do you define an Iranian moderate? That's an Iranian who's out of bullets and money."
—Senator Mark Kirk (R-Ill.)

It wouldn't be the first time Congress has tried to limit the Obama administration's scope for action. Earlier this year, Kirk drafted legislation that would have severed the link between sanctions and the nuclear program by keeping them in place until "the Government of Iran has released all political prisoners, is transitioning to a free and democratically elected government, and is protecting the rights and freedoms of all citizens of Iran, including women and minorities."

The White House's biggest foreign policy priority right now is selling its Iran policy at home. Dennis Ross, Obama's former adviser on Iran, says that if the administration does achieve a comprehensive deal with Iran, it will immediately have to make the case ▶

FROM LEFT: PHOTOGRAPH BY JARED MOOSSY FOR BLOOMBERG BUSINESSWEEK; WIN MCNAMEE/GETTY IMAGES

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Bloomberg Businessweek

◀ that there is no other diplomatic alternative. "Those on the Hill who disagree would then be forced to make the case for war," Ross says. "I want to see who would say at that point, 'No, that's not good enough.' " —*Cameron Abadi*

The bottom line The White House doesn't have the power to lift all sanctions on Iran and will need cooperation from Congress.

Internet

In Britain, a New Front in The War on Child Porn

▶ Rage at a pedophile TV star spurs the prime minister's war on smut

▶ "Going after private companies isn't necessarily the way to go here"

Revelations that late BBC TV host Jimmy Savile sexually abused hundreds of children have prompted soul searching across Britain over how his star power trumped years of suspicion. With constituents enraged, Prime Minister David Cameron has made restricting access to pornography, and especially stamping out images of children, a signature issue.

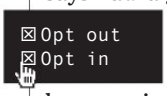
Cameron in April asked public Wi-Fi networks to filter explicit content in public settings such as coffee shops, train stations, and libraries. The six biggest providers have complied. Then in July the father of four threatened to require companies offering home Internet service to install filters that automatically block pornography; subscribers would need to "opt in" to view such material. Once again, the industry agreed; by early 2014, the filters will be on virtually all Internet accounts in Britain. Adults wanting to view explicit content will "have to have a discussion" with their spouse or partner, Cameron told BBC Radio on Nov. 18.

At a London conference that day, **Google** and **Microsoft** announced controls that limit child porn searches, initiatives Cameron threatened to enforce through legislation if not enacted voluntarily. The companies have introduced algorithms that block illegal content and have halted auto-complete on potentially abusive search terms, so typing "underage g..." doesn't suggest the word "girl." Google is implementing technology that brands child porn videos with a unique ID code, which will help authorities remove any copies of such material that are later reposted to the Web.

The government effort comes after reports that Savile, host of the much-loved TV show *Top of the Pops* for 20 years, abused children on BBC property, in hospitals, and elsewhere. Public anger escalated after two men convicted of murdering young girls in separate crimes were found to be purveyors of child porn online. Such cases, as well as Cameron's initiatives, have boosted public awareness of the problem. Calls to a child abuse hot line run by the Internet Watch Foundation, an industry group that fights illegal porn, have climbed 40 percent in the past year.

Cameron's strategy would be hard to replicate in other countries. In France and Germany, where nudity isn't unusual on late-night television and in advertising, such broad restrictions might be considered overreaching. In the U.S., freedom of speech concerns would likely scuttle any broad effort to restrict access to such material. "Looking for online content is a very sensitive area, even though child porn is illegal," says Carolyn Atwell-Davis, vice president for government affairs at the National Center for Missing & Exploited Children in Alexandria, Va.

The Index on Censorship, a London group promoting freedom of expression worldwide, says it's studying Cameron's measures. While restricting child pornography—which Britain also legally bans—is an admirable goal, says Padraig Reidy, a senior writer at the index, mandatory porn filters are "slightly worrying," adding, "It should be an active choice to opt out of adult content, and the government isn't making it so."



Even child safety advocates have come out against Cameron's tactics. Pedophiles don't search for victims on **Yahoo!**, Google, or Bing, but lurk in social networks frequented by kids and in chat rooms where they can be anonymous, says Jim Gamble, the former head of the U.K.'s Child Exploitation and Online Protection Centre. "Going after private companies isn't necessarily the way to go here," he says.

A more appropriate focus, Gamble says, would be peer-to-peer networks where child porn is traded in anonymity. Much of that traffic is hosted on the Tor network, created by the U.S. government a decade ago to boost Internet freedom in authoritarian countries. ▶

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American Corporate Partners (ACP) is a non-profit organization that assists veterans in their transition from the armed services to the civilian workforce.

ACP

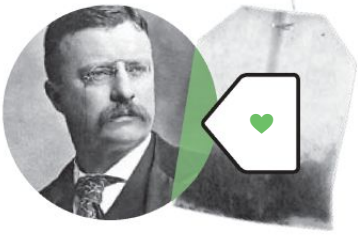
◀ Meanwhile, the filters Internet access providers voluntarily deploy sometimes block nonporn websites, says Andrew Kernahan, public affairs manager at the country's Internet Service Providers' Association. "We've been pushing the government to provide clarity around the legal issues on this," he says.

Despite the government's stepped-up tactics, some groups are engaged in vigilante activity. Parents in Leicestershire banded together under the name Letzgo Hunting to lure online pedophiles to meetings by posing as young girls. The group posted films of the encounters online and passed details on to authorities. Local police say six men were arrested, though none have been charged while officers gather more evidence. The group disbanded after a 23-year-old man jailed for child sex abuse killed himself when confronted by Letzgo Hunting. Police asked the group to leave such inquiries to officers, says spokesman Brendan McGrath, "and not to start an amateur investigation." —*Kristen Schweizer*

The bottom line The British government has used the threat of regulation to spur Internet providers to install pornography filters.

Energy

Red and Blue and Green All Over



▶ Tea Partyers and conservationists come together on solar energy

▶ "Some people have called this an unholy alliance"

Heres's a riddle to vex the Washington political class: When do Tea Party Republicans stand together with Sierra Club environmentalists?

The answer lies in their support for solar energy. The Green Tea Coalition, a Georgia-based group, is reviving a Republican Party link with the Sierra Club that dates back more than a century to President Theodore Roosevelt. Their goal is to reignite support for environmental conservation and fight traditional utilities' market power by pushing alternative energy sources, especially solar power. "Some people have called this an unholy alliance," says Debbie Dooley, a co-founder of both the coalition and the Atlanta Tea Party Patriots. "We agree on the need to develop clean energy, but not much else."

In recent years, Dooley organized protests of what she calls **Georgia Power**'s stranglehold on its customers. She was especially rankled in 2009 after the company, the state's largest utility, added a monthly surcharge to customer bills to finance the development of two nuclear reactors south of Augusta. In 2012, Dooley was approached by the local chapter of the Sierra Club about joining forces to lobby Georgia's Public Service Commission to require Georgia Power to buy more solar power.

At the coalition's Aug. 6 inaugural meeting, about 100 small-government advocates mingled with Sierra Club members at a Quaker meeting house in Decatur. Attendance was almost evenly split between conservatives and liberals, Dooley says.

Politics aside, everyone was celebrating a recent win: In July the utility regulators passed a bill requiring Georgia Power to buy 525 megawatts of solar power capacity by 2016; about a fifth of that must come from residential and commercial rooftops, as opposed to solar power farms built by large utilities. The groups more recently worked to persuade state regulators to reject Georgia Power's proposal to charge customers with solar panels an additional $5.56 per kilowatt for use of the grid. Facing increasing opposition, the utility has withdrawn its request.

"There's no competition here," Dooley says. "Solar is our only way to force" the utilities to compete. On that, the Sierra Club's position aligns with the coalition, says Colleen Kiernan, director of the club's Georgia chapter. "With the conservative side, it's a desire to provide a fair market for everyone and eliminate subsidies, and we agree to that," she says.

"The free-market approach works well in Republican circles, so I can understand how these [groups] come together," says Frank Maisano, an energy specialist at the Washington law firm Bracewell & Giuliani. "It becomes an economic argument."

In North Carolina, Representative Ruth Samuelson, a Republican from Mecklenburg, helped fight off attempts earlier this year to gut the state's renewable energy mandate. The 2007 law—similar to ones in 29 other states—requires North Carolina's utilities to produce more of their power (12.5 percent by 2021) from renewable energy such as wind and solar. Republican opponents had introduced a bill that would have cut the requirement in half.

Worldwide Energy Prices
Per megawatt hour

Solar
$143

Nuclear
$101

Natural gas
$70

But renewable energy advocates faced a recent setback in Arizona. On Nov. 13, the state's utilities regulator agreed in a 3-2 vote that **Arizona Public Service** can collect $4.90 a month from customers with solar panels. (Solar developers reached a compromise on the proposed fee, reducing it from $100 a month.) Arizona Public argued that a rule requiring it to buy solar power from customers with rooftop panels unfairly shifts some of its costs to people without panels; the commission agreed with the argument. Barry Goldwater Jr., son of the late senator and presidential candidate, campaigned against the utility on the issue. Utilities "don't like the competition," he says. "I'm a conservative Republican, and I think people should have a choice."

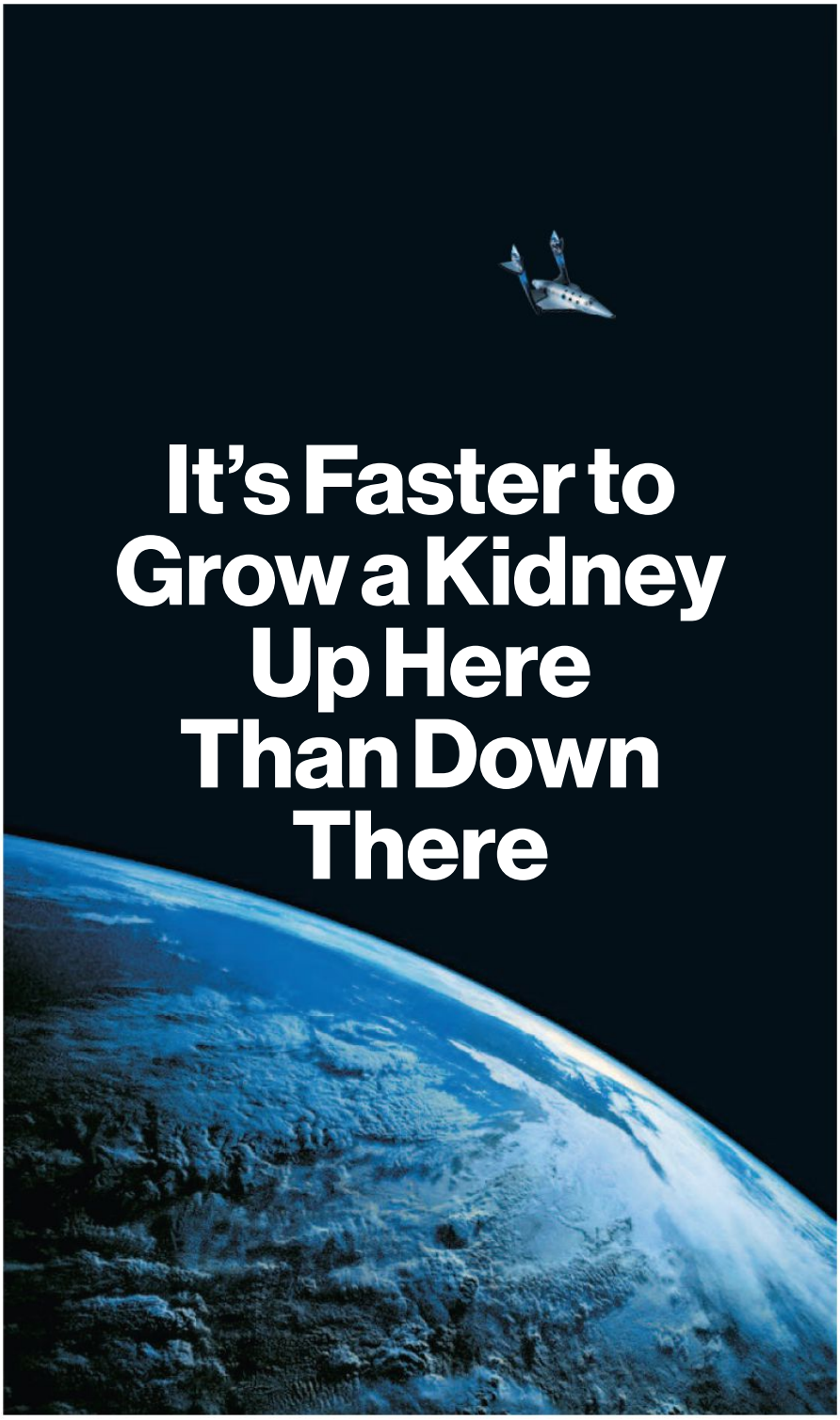
Many Republicans remain opposed to solar energy because of the high costs, according to Americans for Prosperity, a group funded by the billionaire Koch brothers that often allies with the Tea Party. "We've had disagreements over solar," says Virginia Galloway, director of Americans for Prosperity's Georgia chapter. Coal and gas both generate electricity at a lower cost than solar, she says. Making utilities buy solar will raise costs that will be passed on to consumers, she says. "We oppose any mandates that would raise utility rates," Galloway says.

The coalition's Dooley says she won't give up anytime soon. "I want a cleaner world for my grandson and his grandchildren," she says. "I'll join whoever I need to in this fight."
—*Christopher Martin*

The bottom line Some Tea Party members are breaking ranks with fellow conservatives and pushing for clean energy.

B Edited by Cristina Lindblad & Dimitra Kessenides
Businessweek.com/politics-and-policy

December 2 — December 8, 2013



It's Faster to Grow a Kidney Up Here Than Down There

▶ As countdowns near, spaceflight companies turn to R&D clients

▶ "We will roll out of the garage.... This is gas and go"

Commercial space travel is almost here. For real this time. Sometime in 2014, **Virgin Galactic** will be able to fly 100 kilometers into the sky and put you in near-zero gravity for a few minutes. The price tag: $250,000. Already Angelina Jolie, Ashton Kutcher, Katy Perry, Justin Bieber, and Richard Branson, the company's eccentric billionaire founder, have lined up with 600 other people to get on flights. Booking a flight on rival **Xcor Aerospace** will cost roughly $100,000, the company says. **Blue Origin**, the space company launched by Amazon.com founder Jeff Bezos, says it's close behind but hasn't put out a price list just yet.

Musicians, actors, and wealthy corporate executives won't keep these companies flying forever. Virgin estimates it will run through its star-studded list in 12 to 18 months. So most of the space companies expect to turn to a less glamorous source of business to keep them going: companies and researchers in search of a little time at near-zero gravity to conduct experiments.

The near-weightless state known as microgravity has uncanny and, for researchers, desirable effects on a wide range of technologies. Companies such as **Procter & Gamble** and **Merck** have performed experiments in space for years to better understand how their toothpaste ingredients bind together or their engineered antibodies attack disease in isolation, without the complicating effects of gravity. **Mitsubishi Heavy Industries** has tested its medical devices in low G and wants to conduct suborbital drug research on animals. Startup **Made in Space** intends to test whether its 3D printers can work in near orbit. Space also makes stem cells grow superfast: "Give me 30 to 35 days, and I'll build you a kidney," says genetic engineer Richard Godwin, the chief executive officer of stem-cell startup **Zero Gravity Solutions**. "How expensive is that? Who cares?"

Ideally, many of these experiments would be performed in the International Space Station, where they could undergo longer-term observations, but trips that far into orbit are costly and infrequent. The new spaceflights will offer quicker chances for ▶

EARTH: STEVE BLOOM IMAGES/ALAMY; SHIP: COURTESY OF VIRGIN GALACTIC

◀ experimentation and allow scientists to interact with their equipment while it's up there. "Now space scientists can go into the field and get some measurements and get some hard data and not just rely on models," Khaki Rodway, Xcor's director of payload services and operations, said at a Silicon Valley space conference in October.

"Unlike tourists, researchers will fly their experiments multiple times," says James Muncy, the founder of independent space policy consultancy PoliSpace. The companies are also competing for former clients of NASA, which before its space shuttle program was mothballed in 2011, regularly ferried experiments into space and sometimes to the International Space Station. Virgin has contracted with NASA to run some of the scientific missions that interest the agency, such as the Made in Space printing project.

Xcor, based in Mojave, Calif., plans to begin commercial flights of its *Lynx* spaceship in late 2014. Virgin Galactic's *SpaceShipTwo* will fly from the spaceport it's building at its headquarters in Las Cruces, N.M. Both vehicles look a little like a cross between the space shuttle and a jet. Fourteen-year-old Xcor has signed deals with Mitsubishi Heavy; a group called Citizens in Space, which has bought 10 flights earmarked for regular folks; and **Unilever**, which plans to send 23 people into space to promote its line of Axe body sprays and deodorants. Virgin says it's just waiting on the results of a few last test flights in December and some final regulatory hurdles to begin its commercial flights.

Regularly scheduled flights for customers doing research and development would be a major leap beyond what government programs had offered the private sector in the past, says Sean Casey, the managing director of the Silicon Valley Space Center, which advises space startups. "Researchers have been turned off by NASA's traditional time scale," he says. "With Xcor, you can spend $1 million to $2 million and do 10 flights each with about six minutes of microgravity and make sure your experiments are working." Blue Origin business development manager Erika Wagner said during the recent space conference that the company's goal is spaceflight at a moment's notice. "We will roll out of the garage," she said. "This is gas and go."

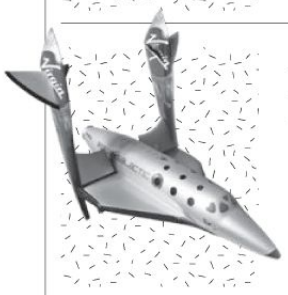
Godwin of Zero Gravity Solutions, which got room on NASA shuttles when the program was still operating, says the ability to buy a spot on regular spaceflights will help accelerate research. Zero Gravity, in Boca Raton, Fla., has been trying to crack the genetic code of a tropical plant called jatropha, a promising biofuel limited on earth by its inability to survive cool temperatures. Looking at data collected during a 2010 spaceflight on the NASA *Endeavor*, Godwin's researchers found that jatropha cells under exposure to low gravity began to express previously unknown cold-tolerance genes. They're still trying to figure out how to activate the genes back at home. "When you turn off gravity, a plant doesn't know what's going on, and it ignites all of its survival mechanisms," Godwin says. "Here is a plant that produces 500 percent more yield as a biofuel than corn or switch grass and could be a new cash crop. You might be able to grow this stuff in Texas and have a new variety of the plant that is patentable and licensable."

Price may remain a catch for some space customers. Virgin says flying a simple, nonhazardous single cargo bag or storage locker will cost around $50,000, but clients who want one of the company's spacecrafts to themselves for a flight will have to pay north of $1.2 million. "Centuries ago people put a load on a camel's back and walked from China to Istanbul to make a profit," Godwin says. "It was low volume and high value, and this is the same thing. I call it the Silk Road from space." —*Ashlee Vance*

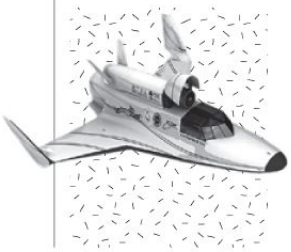
The bottom line Space companies will charge $100,000 a seat or more and expect to attract businesses interested in microgravity research.

Space Specs

Blue Origin
Ship *New Shepard*
Altitude 330,000+ feet
Payload A rocket booster sends a capsule carrying astronauts and research into space. The capsule's descent is slowed by parachute.



Virgin Galactic
Ship *SpaceShipTwo*
Altitude 360,000 feet
Payload Carries six passengers and two pilots beyond the earth's atmosphere. From there it can glide back to earth.



Xcor Aerospace
Ship *Lynx*
Altitude 330,000 feet
Payload Uses a rocket propulsion system to take off and land like a plane. Expected to carry people and research on up to four suborbital flights a day.

Engineering

GE Turns to 3D Printers For Plane Parts

▶ The company is leading a push toward assembly-line printing

▶ "There doesn't exist a supply chain out there ... for this kind of work"

General Electric, on the hunt for ways to build more than 85,000 fuel nozzles for its new Leap jet engines, is making a big investment in 3D printing. Usually the nozzles are assembled from 20 different parts. Also known as additive manufacturing, 3D printing can create the units in one metal piece, through a successive layering of materials. The process is more efficient and can be used to create designs that can't be made using traditional techniques, GE says. The finished product is stronger and lighter than those made on the assembly line and can withstand the extreme temperatures (up to 2,400F) inside an engine. There's just one problem: Today's industrial 3D printers don't have enough capacity to handle GE's production needs, which require faster, higher-quality output at a lower cost.

"With today's technology, it would take too many machines," as many as 60 to 70, to efficiently make the nozzles, says Greg Morris, business development leader for additive manufacturing at GE Aviation. Morris joined the aerospace company last year, as part of GE's acquisition of his 3D company, Morris Technologies. "We can start ramping up with the current generation of technology, but within two to three years we're going to have to be onto the next

CLOCKWISE FROM BOTTOM LEFT: COURTESY OF BLUE ORIGIN; COURTESY OF VIRGIN GALACTIC; COURTESY OF XCOR AEROSPACE; COURTESY OF GE AVIATION (2)

The GE90 is one of the world's most powerful jet engines. GE plans to produce 100,000 3D-printed components for the next generation GE9X and Leap models.

generation to meet our cost targets," he says. So GE is waiting for development of new printers with three to four times the capacity.

As part of a $3.5 billion investment in its aerospace supply chain, GE says it will spend tens of millions of dollars to invest in new technology and, over the next five years, triple the size of its 70-person 3D-printing staff and expand its factory floor fourfold. (The 85,000 nozzles are for engine orders that will enter full production in late 2015.)

Each Leap engine will contain 19 metal 3D-printed fuel nozzles. The part is lighter and more durable than traditional parts.

The company's embrace of 3D printing throws the weight of the world's largest jet-engine maker behind a process invented in the 1980s to fabricate scale models. As the technology has advanced, 3D printing has evolved. Today, **Boeing** uses the process to make plastic air-conditioning ducts for its 787 Dreamliner jet, and **Nike** has a football cleat made on 3D printers. "[GE's] investment changes everything, and it's also unprecedented," says Terry Wohlers, president of 3D printing consulting company Wohlers Associates. The company's annual report tracking 3D technology estimates that the industry is poised to almost triple, to about $6 billion in sales, by 2017.

Sales of 3D printers and related services rose 29 percent in 2012, to $2.2 billion, according to Wohlers. They're on track to keep rising as GE, **Siemens**, and **Rolls-Royce** among others invest in industrial-grade systems capable of producing metal parts. Demand from the aerospace industry alone is driving huge growth, Credit Suisse Group said in a Sept. 17 note. That's creating opportunities for companies such as **3D Systems**, the largest maker of 3D printers in the U.S. GE is testing equipment from the Rock Hill (S.C.)-based company, as well as from **Concept Laser**.

"We have an excellent relationship with GE at the highest levels, and we've been collaborating with them for several years now on a variety of additive manufacturing applications," says 3D Systems Chief Executive Officer Avi Reichental.

The stock price of 3D Systems has more than doubled this year through mid-November, while that of another major 3D printing player, **Stratasys**, has jumped 59 percent, beating the 27 percent advance for the Standard & Poor's 400 MidCap Index, to which they both belong.

"[General Electric's] investment changes everything, and it's also unprecedented." —*Terry Wohlers*

Expanding 3D printing will give GE clout with device manufacturers, an opportunity to guide the growth of the industry. "There doesn't exist a supply chain out there right now for this kind of work," Morris says. "GE has to be involved in developing it." —*Tim Catts*

The bottom line GE is making a game-changing investment in 3D printing, helping to bring the technology to more assembly lines.

Mobile

Discount iPhones Come to India

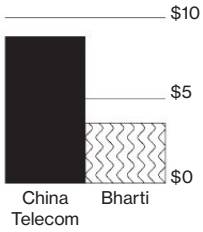
- A wireless carrier subsidizes phones to boost spending on data
- "We are hungry for growth, and this could be the tipping point"

Signing up for a monthly wireless contract to get a subsidized iPhone is common in the U.S., but in India, **Apple** fans are accustomed to paying the phone's full price. In November, **Reliance Communications** (RCom), India's third-largest mobile operator by market value, became the first to hand iPhone 5Cs to customers willing to commit to 2,599 rupees ($41) a month for 24 months. Gunjan Hasan, who got one at an RCom shop in Mumbai, says ▶

◀ she'd been putting off buying a phone because of the upfront costs. "When you have a family and other expenses, you really need to think before paying up to 50,000 rupees [about $800] or so for just a phone," says Hasan, 36, who works at KSA Development Venture, a teacher-development company in New Delhi.

The subsidies are part of Chief Executive Officer Gurdeep Singh's plan to reduce RCom's dependence on low-margin users. India is the second-largest mobile market after China. In the fiscal year that ended in March, its active subscribers hit 788 million, up 37 percent in two years, according to the Cellular Operators Association of India. Most of those users, however, have cheap voice-only plans; India market leader **Bharti Airtel** averages $3.10 per subscriber each month, compared with $8.80 at comparably sized **China Telecom**. Subsidies may nudge shoppers toward pricier data plans, Singh says: "We are hungry for growth, and this could be the tipping point."

Monthly Average Revenue Per User Q2 2013



If he's right, RCom could help solve an ongoing headache for telecom operators in the world's fastest-growing smartphone market. With the country's mobile users accustomed to paying less than a penny a minute for voice calls, India's operators make far less per customer than their international peers. Averaging only $1.60 a month per user, compared with $69 for U.S. companies, Indian operators have slashed data fees by as much as 90 percent, betting cheaper rates will help fuel a rise in mobile gaming and social networking. RCom's average revenue per user jumped 26 percent, to 120 rupees ($1.92), during the three months ended in September. To increase averages further, the company said in a Nov. 5 statement that it had disconnected 10 million "unprofitable, low-end subscribers."

Most Indian operators are counting on devices cheaper than the iPhone. High prices have kept Apple a distant No. 8 in the local market, well behind first-place **Samsung**. Almost 80 percent of Samsung's smartphone sales in India come from models priced below $380. Local brands such as **Micromax** offer many low-cost smartphones, too. India's smartphone shipments will grow from 16.3 million in 2012 to 41.4 million this year, according to market researcher IDC, which predicts the number will hit 128 million by 2015.

Most operators need to persuade more Indians to use phones for more than voice calls before they can woo them with Apple products, says Ankita Somani, an analyst in Mumbai with Angel Broking. "First they have to increase data usage in the country," which is about 10 percent of overall revenue, she says, predicting that slice will grow at double-digit rates.

Ten years ago, RCom tried subsidizing Samsung and **LG** handsets but ended the program after customers stopped making payments and walked off with the phones. Now the company requires users to agree to automatic credit card payments. It's teamed with banks that run credit checks, including **Citibank** and **Standard Chartered**. "Credit rating and history go a long way in determining the success of this plan," Singh says.

Not many Indians use plastic, though. The country has only 18.5 million credit cards, or about one for every 50 mobile phones, according to Bloomberg Industries analyst Praveen Menon. And Indian customers aren't used to a long lock-in period with a service provider, says Harit Shah, an analyst in Mumbai with Nirmal Bang Equities. "Six months, maybe," he says, "but not two years."

—Bruce Einhorn and Bhuma Shrivastava

The bottom line An Indian mobile operator is using U.S.-style incentives to lure customers into pricier, more profitable plans.

Quoted

"Modern technologies can deliver mobile services in the air safely and reliably."

New Federal Communications Commission Chairman **Tom Wheeler** in a Nov. 21 statement. After an outcry from people who oppose phone calls on planes, he said that it's up to airlines to act on his technical advice.

Apps

A Plague That's Carried On Mobile Devices

▶ Plague Inc.'s contagion app thrills gamers—and the CDC

▶ "Games like this reach people who don't think about... science"

The disease didn't look like a killer. The symptoms were coughs and sneezes, and its spread attracted little notice. Then someone with the virus got on a plane, launching its journey around the globe. Sneezes gave way to fatal hemorrhages; thousands of infected turned into millions. The virus mutated and developed drug resistance. Soon it wiped out the human race. For players of the mobile game Plague Inc., that counts as a win.

The object of the game, available for 99¢ on iPhone, iPad, and Android, is to create an infectious disease that kills as many people as possible. Players exploit countries' vulnerabilities—climate, population density, poverty—to help the disease spread before a cure is discovered. James Vaughan, the game's creator, designed it around actual risks such as antibiotic resistance.

With more than 15 million downloads since its release last year, Vaughan's creation has captured the attention of gamers and public health officials alike. The latter see Plague Inc. as a tool to raise awareness of real-world pandemic risks at a time when research is under

MOBILE DATA: COMPILED BY BLOOMBERG; INNOVATORS: COURTESY OF TECHNICAL ILLUSIONS

pressure. "Right now there's a dire funding crunch for science in the U.S.," says W. Ian Lipkin, director of Columbia University's Center for Infection and Immunity. The U.S. National Institutes of Health was required to cut 5 percent, or $1.55 billion, from its fiscal 2013 operating budget. "Games like this reach people who don't think about the importance of science," Lipkin says.

In March the U.S. Centers for Disease Control and Prevention invited Vaughan to speak to researchers in Atlanta and agreed to let its name appear in the game's mock news alerts. For example, a text bubble may pop up saying that the CDC has identified the first case of a disease in humans. "We think everyone can learn from this," says Dave Daigle, a CDC spokesman. "Public health is one of those things very few of us know about unless something goes wrong."

The agency has tried before to reach younger people via social media. It built its own iPad game this year, called Solve the Outbreak, where "disease detectives" win by finding the cause of infections based on real outbreaks that the CDC has investigated. In 2011 the agency posted to its Public Health Matters blog a tongue-in-cheek primer on how to cope in the event of a zombie apocalypse. Daigle says kids unenthusiastic about prepping for a hurricane or tornado were happy to remind their parents to stock up on water, food, medicine, and other supplies to survive an onslaught of the undead.

Plague Inc. has the same appeal, says Vaughan, 26, who isn't an epidemiologist and didn't build the game with education in mind. While a consultant for Accenture in London, he sought a creative side project. He spent less than $5,000 developing the game over the course of a year, collaborating with contractors for the programming, art, and sound. Now "I get e-mails and tweets and Facebook messages from people teaching 11-year-olds all the way up to people doing Ph.D.s in infectious disease," he says. "Parents are sending me messages saying, 'Little Timmy was just asking where Bolivia is and he wants to know what climate it's got. He's never shown any interest in geography before.'" —*Meg Tirrell*

The bottom line Plague Inc. is a hit with gamers and public health officials, who see it as a tool to raise awareness about pandemics.

Edited by Jeff Muskus
Businessweek.com/technology

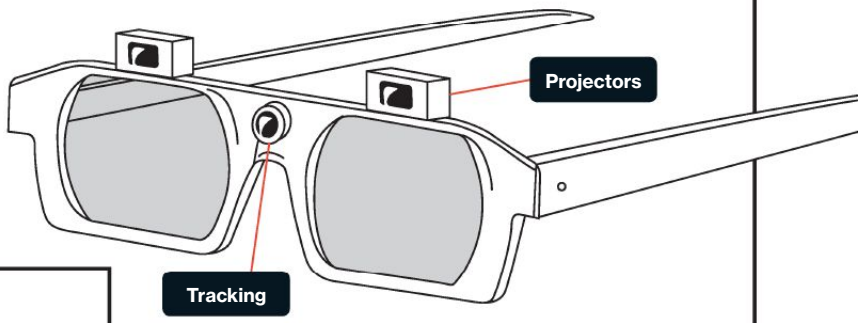
"It's going to deliver on the dream of the holodeck." —*Bre Pettis, chief executive officer of 3D printing company MakerBot*

Innovation

Hologram Glasses

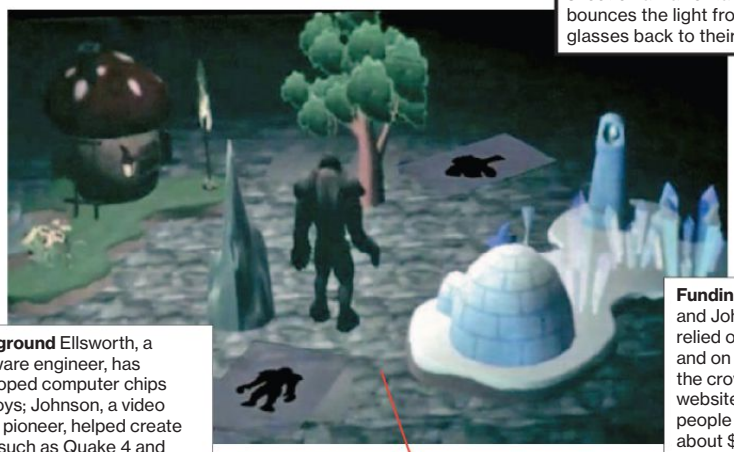
Form and function
Technical Illusions has developed castAR, a pair of high-tech glasses that project 3D hologramlike images, and a "magic wand" that can be used to interact with the holographic projections to enliven gaming and teaching.

Innovators Jeri Ellsworth and Rick Johnson
Ages 39 and 42
Titles Co-founders of Technical Illusions, a startup in Woodinville, Wash.



1. **High-tech frames** Two tiny projectors mounted on the frames of the glasses cast game images (a chess piece or a monster), while a head-movement tracking system adjusts the holographic scene to make it appear realistic.

2. **Light fantastic** For users to see 3D effects, they must place a retro-reflective sheet on a wall or table that bounces the light from the glasses back to their eyes.



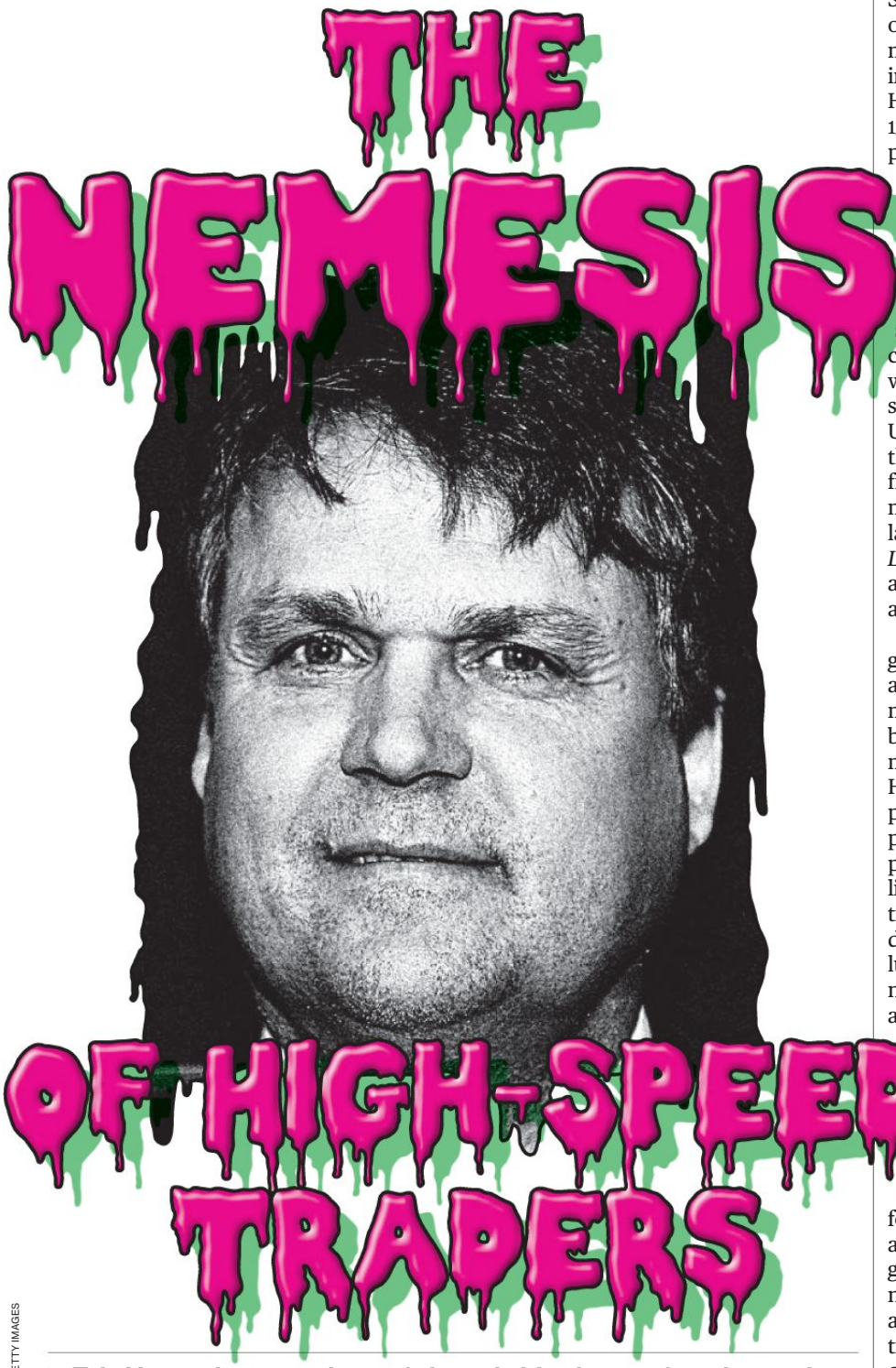
Background Ellsworth, a hardware engineer, has developed computer chips and toys; Johnson, a video game pioneer, helped create titles such as Quake 4 and Soldier of Fortune. Both were fired from video game maker Valve in February and launched Technical Illusions to commercialize the castAR technology.

Funding Ellsworth and Johnson have relied on savings and on Kickstarter, the crowdfunding website. About 3,900 people pledged about $1 million, more than double the co-founders' $400,000 target.

Next Steps

Ellsworth and Johnson aim to start manufacturing their hologram glasses this summer. The castAR starter kit, which includes the specs and the retro-reflective surface, will sell for $189. The wand to manipulate the images will cost an additional $60. They anticipate the glasses will be available for retail purchase by the fall. —*Nick Leiber*

THE NEMESIS OF HIGH-SPEED TRADERS



BRAD BARKET/GETTY IMAGES

▶ Eric Hunsader sees signs of abuse in his charts of market action

▶ "If you can't prove your point, then disprove mine"

Eric Scott Hunsader, the scourge of Wall Street's high-frequency traders, operates out of an office above the Bliss Salon—manicure/pedicure $45—on Elm Street in the Chicago suburb of Winnetka. Hunsader is the founder of **Nanex**, a 13-year-old firm that operates as a "ticker plant," taking price streams from U.S. exchanges and distributing the data to clients through software that allows them to analyze and chart it and write their own trading programs.

Spending long hours staring at four computer monitors, he looks for signs of illicit trading hidden in psychedelic images of triangles dancing with dots. Each dot and triangle represents a trade or a quote to buy and sell U.S. stocks by the millisecond. To him the images provide evidence that high-frequency trading firms are exploiting market rules to turn a profit in a lawless environment. "You ever see *Lord of the Flies* or read that book?" he asks. "When you don't have a parent around, things fall apart."

Since regulators opened trading to greater competition six years ago, the almost $22 trillion U.S. market has fragmented to the point where orders bounce among 13 exchanges and more than 40 alternative platforms. In Hunsader's view, high-frequency traders pose a threat to other market participants because they react so quickly to price movements. He also says the millions of orders they place—and sometimes immediately cancel—drive up data-processing costs and can lead to lurches in the price of individual stocks, not to mention outright disasters such as the May 2010 "flash crash" when the Dow Jones industrial average fell almost 1,000 points in minutes.

To illustrate computerized trading to the public, Hunsader has turned data into animated videos. One posted on YouTube shows a 50-millisecond period in which quotes for Nokia dashed around the market at a rate of 22,000 per second. He programmed a computer to play piano notes corresponding to different bids and offers for a popular exchange-traded fund, resulting in a manic staccato composition. He says such projects are meant to highlight the absurdity of modern computerized trading.

People at HFT firms accuse ▶

A frame from a video showing about a third of a second's trading in Nokia on Oct. 9

◀ Hunsader of misunderstanding what he sees in market data. Manoj Narang, chief executive officer of **Tradeworx** in Red Bank, N.J., compares Nanex to the "truthers" who doubt the official explanation of the Sept. 11 terrorist attacks. "The conclusions that they form generally have a paranoid or conspiracist sort of bent to them," he says. Chris Concannon, a partner at **Virtu Financial** and a former Securities and Exchange Commission attorney, joked in a recent speech that Nanex's slogan should be "making markets better with inaccurate information."

Nanex's interpretations are helping to drive the public debate about the fairness of the modern stock market. Virtu and Nanex have traded insults since Hunsader published a Sept. 20 report titled *Einstein and The Great Fed Robbery*. The report cited market data it said showed a trading firm or firms somehow got advance word about the Fed's Sept. 18 decision not to reduce its $85 billion in monthly bond purchases, then used the milliseconds-long head start to place bets totaling more than $1 billion. Following the report, the Fed began a review and ultimately tightened the way it releases its statements. Virtu issued a report saying Nanex's study was "severely flawed." Hunsader replied that Virtu needs to buy a "new calculator." Concannon didn't respond to requests for comment.

"Everybody who's gone this route" of taking on the trading establishment "has had to be a little bit theatrical, and Wall Street doesn't like it," says Haim Bodek, founder of Decimus Capital Markets, which develops computer programs to help institutions trade with HFT firms. "The irony here is that he really is addressing these deep flaws."

Calling patterns crop circles, "caught the eye of Main Street. ... The curse was that the Wall Street glitterati, or elites, would always associate us with conspiracy theories"

Nanex's offices consist of a room dominated by Hunsader's wall of monitors, another filled with stacks of servers, a common area with a mini-fridge full of soda, and not much else. Hunsader, 51, says he's released about 3,000 pieces of trading research and never stood down from a finding. How do you publish that many reports, he asks, "and not ever have to retract them? If you can't prove your point, then disprove mine. But don't go around saying we think you're making leaps without backing it up."

The flash crash inspired Hunsader to look more closely at the data he was distributing. He and Nanex programmer Jeff Donovan, a Southern California surfer and ticker-plant programmer who also develops three-dimensional graphics software, drilled through the quotes. Patterns they saw as evidence of market manipulation emerged in charts for stock orders. They called them crop circles, a reference to the mysterious patterns sometimes reported in grain fields, and published the research on the firm's website. Calling them crop circles "was a blessing and a curse," Hunsader says. "It was a blessing because it caught the eye of Main Street, and it got us into the *Atlantic*, which got us into the *New York Times*. But the curse was that the Wall Street glitterati, or elites, would always associate us with conspiracy theories."

A high-frequency tweeter with more than 11,000 followers, Hunsader conducts his crusade on the Internet and through interviews with journalists, documentary filmmakers, and others looking for someone to explain today's computerized market. Many of his Twitter posts link to his charts highlighting unusual patterns in stock quotes and often blame computer algorithms used by HFT firms. "Obscene manipulation in $AAPL stock. Where's @SEC_News on this & 1000's of other examples?" he tweeted on Oct. 5, referring to the symbol for Apple and a Twitter feed run by the SEC. An SEC spokesman declined to comment on Nanex's assertions, as did representatives of the **New York Stock Exchange**, **Nasdaq OMX Group**, and **Bats Global Markets**, which is combining with **Direct Edge Holdings**. Bloomberg LP, parent of *Bloomberg Businessweek*, operates an alternative equities platform called Tradebook and is a provider of market data and analytics.

Among those who have come to Winnetka to consult with Hunsader is James Angel, a finance professor at Georgetown University who studies markets. "I don't think his analysis is always correct," Angel says. "He doesn't know who's trading, who's putting in the various quotes." Nevertheless, he says, Hunsader's work is important: "Even though on average our markets are a whole lot better than they were 10 or 20 years ago, the reality is, hey, there's still some blemishes around the edges that can and should be addressed. And he draws attention to them." —*Michael P. Regan*

The bottom line Nanex's founder is on a mission to expose what he sees as market manipulation by high-frequency traders.

Commodities

China Is Ready to Pass India in the Gold Race

▶ Falling prices send aunties on jewelry-buying sprees

▶ "You look around and see very few places to put your money"

Yang Cuiyan, a 41-year-old housekeeper from Anhui province, is one reason China is poised to topple India as the world's top consumer of gold. Standing outside Beijing's busiest jewelry store, wearing a thick coat against the autumn chill, she clasps a gold necklace that cost her 10,000 yuan ($1,640), or five months' wages. "I can put it on when I go back home to show everyone that I'm doing well."

Yang is one of the legions of middle-aged Chinese women, respectfully referred to as aunties, who bought coins and jewelry this year. Gold purchases in the world's second-largest economy will surge 29 percent in 2013, to a record 1,000 metric tons, according to the median of 13 estimates from analysts, traders, and gold producers in China surveyed by Bloomberg News. China's purchases of gold climbed 30 percent, to 996.3 tons, in the 12 months through September, while sales in India rose 24 percent, to 977.6 tons, according to the London-based World Gold Council. India was No. 1 in 2012. Each country buys more gold than the U.S., Europe, and the Middle East combined.

Gold's burnished appeal in China stems in part from a lack of alternative investments. While the MSCI All-Country World Index of equities rose 18 percent this year through Nov. 22, the Shanghai Composite Index slumped 3.2 percent. Policymakers clamped down on property investments in March to cool the housing market, ordering the central bank

Buying on the Dip

Price per ounce of gold on Nov. 22, 35 percent below 2011's record high

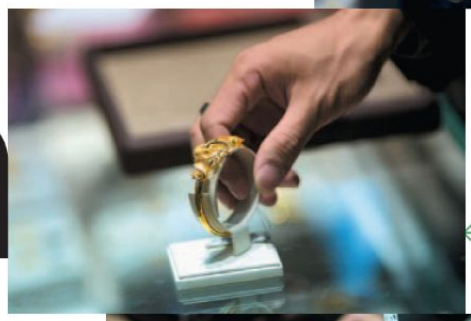
$1,243

Rise in rural China's per capita income in the first nine months of 2013 from the same period last year

+12.5%

China's rank worldwide for the number of people with $1 million or more in investable assets

4th



Projected growth in gold purchases in China for 2013

+29%

Projected tons of gold bar, jewelry, and coin sales in China for 2013

1,000

LAM YIK FEI/BLOOMBERG(5)

to raise down-payment requirements for second mortgages in cities with excessive price gains. "In China, you look around and see very few places to put your money," says Duan Shihua, a partner at Shanghai Leading Investment Management. "With the share market down and the government nudging people away from real estate, gold will remain a favored choice."

The increased appetite for gold also reflects rising wealth. China's rural per capita income in the first nine months of the year jumped 12.5 percent from a year earlier, while urban per capita disposable income rose 9.5 percent, data from the national bureau of statistics show. The nation ranks fourth worldwide for the number of people with $1 million or more in investable assets, with 643,000 in that bracket last year, up 14 percent, according to a report by consulting firm Capgemini and Royal Bank of Canada. The U.S. ranks first, followed by Japan and Germany.

In April, when the price of gold fell 14 percent in two days, Chinese media showed images of aunties clearing shelves in gold shops. "I don't know anything about the stock market, and I don't have enough money to buy property, so I figured gold is the safest choice," says Yang, who made the 650-mile journey to Beijing from her rural home to visit relatives and shop. "I want to keep up with my relatives and friends back home. We all like to compete to see whose necklace is thicker." —*Bloomberg News*

The bottom line China's gold purchases rose 30 percent in the 12 months ended Sept. 30, to 996.3 tons, topping India's 977.6 tons.

Bonds

Subprime Loans Are Boosting Car Sales

- Yield-starved investors provide funds for buyers with weak credit
- "They have to pay the car payment before they pay anything else"

A woman came into Alan Helfman's showroom in Houston in October looking to buy a car for her daily commute. Even though her credit score was below 500, in the bottom eighth percentile, she drove away ▶

◀ with a new Dodge Dart. A year ago, "I would've told her don't even bother coming in," says Helfman, who owns River Oaks Chrysler Jeep Dodge Ram, where sales rose about 20 percent this year. "But she had a good job, so I told her to bring a phone bill, a light bill, your last couple of paycheck stubs, and bring me some down payment."

"Perhaps more than any other factor, easing credit has been the key to the U.S. auto recovery"

As the fifth anniversary of the Federal Reserve's policy of keeping interest rates near zero approaches, the market for subprime borrowing is again becoming frothy, this time in the car business instead of housing. U.S. auto sales, on pace for the best year since 2007, are increasingly being fueled by borrowers with spotty credit. They accounted for more than 27 percent of loans for new vehicles in the first half of the year, the highest proportion since Experian Automotive began tracking the data in 2007. That compares with 25 percent last year and 18 percent in 2009, as lenders pulled back during the recession. "Perhaps more than any other factor, easing credit has been the key to the U.S. auto recovery," Adam Jonas, an analyst with Morgan Stanley, wrote in an October note to investors.

The money for subprime loans comes from yield-starved investors who buy bonds backed by them. Issuance of such bonds, which pay higher rates than U.S. government debt, soared to $17.2 billion this year, more than double the amount sold during the same period in 2010, but still below the peak of about $20 billion in 2005, according to Harris Trifon, an analyst at Deutsche Bank.

The interest rates on subprime auto loans can climb to 19 percent, according to Standard & Poor's. "Right now, you have to have fairly bad credit to be paying above 3 percent," says Jessica Caldwell, an analyst with auto research firm Edmunds.com. **Chrysler Group** has been a beneficiary of the subprime boom. Fifty-eight percent of loans taken out to purchase its Dodge brand vehicles in October were above an annual percentage rate of 4.2 percent, the industry average, according to Edmunds. The average loan for a Dodge charged an APR of 7.4 percent, and 23 percent of the loans had APRs of more than 10 percent, making Dodge the brand with the highest percentage of loans at more than 10 percent, followed closely by Chrysler and **Mitsubishi**. Dodge's U.S. sales rose 17 percent this year through October compared with a year earlier, propelling Chrysler Group to 43 straight months of rising sales.

About 13 issuers have raised money in the asset-backed bond market to make subprime auto loans this year, according to Citigroup. Among them are **GM Financial**, the lender known as AmeriCredit before it was acquired by General Motors in 2010, and new entrants such as **Exeter Finance**, owned by Blackstone Group. Exeter has issued $900 million of bonds linked to subprime auto loans this year, data compiled by Bloomberg show. Exeter has higher loss rates compared with other lenders, S&P said in a Sept. 17 report. A spokeswoman for Exeter declined to comment.

Shoddy home loans packaged into bonds by Wall Street banks fueled the financial crisis. Subprime auto loans are a good investment, Helfman says: "A person that has to get from point A to point B, they're not going to jeopardize their job. They have to pay the car payment before they pay anything else." His Dodge Dart customer with the bad credit had to pay a higher-than-average interest rate on her loan. "It wasn't pretty, but it wasn't crazy," he says. She was "so happy she couldn't see straight." —*Sarah Mulholland and Tim Higgins*

The bottom line Borrowers with spotty credit accounted for 27 percent of auto loans in the first half of 2013, up from 18 percent in 2009.

Equities

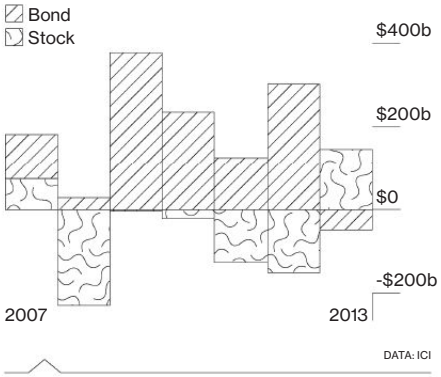
Record Highs Lure Investors Back to Stocks

▶ Cash pours into equity mutual funds after five years of withdrawals

▶ "Jumping from one frying pan into another"

Investors are rediscovering their taste for equities. Stock funds took in $148 billion in the year's first 10 months, after five years when money flowed out, according to Investment Company Institute data. The shift marks a reversal

Mutual Fund Flows



from the four years through 2012, when investors put $1 trillion into bond funds, and the financial crisis drove many to abandon stocks and miss out as the Standard & Poor's 500-stock index almost tripled from its March 2009 low.

The Barclays U.S. Aggregate Bond Index–a common fund benchmark–declined 1.4 percent this year through Nov. 19 and is heading for its first annual loss since 1999. Some professionals see bigger trouble ahead for stocks. "We will have the third in the series of serious market busts since 1999," wrote Jeremy Grantham, chief investment strategist at money manager GMO, in a November letter to clients. BlackRock Chief Executive Officer Laurence Fink says stocks may decline as much as 15 percent because of political risks in China, Japan, France, and the U.S. People moving their money from bonds into stocks "are jumping from one frying pan to another," says Eric Cinnamond, manager of the $694 million Aston/River Road Independent Value Fund.

Bonds have fallen in value since May, when Federal Reserve Chairman Ben Bernanke raised the possibility of scaling back the Fed's $85 billion monthly bond-buying program. The yield on the 10-year Treasury note rose to 2.79 percent as of Nov. 20, from 1.93 percent on May 21, the day before Bernanke first mentioned the idea. Bond prices fall as rates rise. **Pacific Investment Management Co.**, the biggest operator of bond funds, had withdrawals of $39 billion in the third quarter. "People are rotating into stocks because they opened up their statements and saw losses in their bond funds for the first time in God knows how long," says Michael Mullaney, chief investment officer for Fiduciary Trust.

Individual investors have grown

increasingly optimistic about stocks as benchmarks set new highs. The S&P 500 closed above 1,800 for the first time on Nov. 21, and the Dow Jones industrial average broke the 16,000 mark on the same day. Bullishness in the American Association of Individual Investors' weekly survey has averaged 43 percent this quarter, up from 29 percent in August and a long-term average of 39 percent.

The stampede into stock funds could be a sign the rally is nearing an end, says Jonathan Pond, an independent financial adviser in Newton, Mass. "The timing of retail investors tends to be terrible." That isn't always a reliable indicator. Annual mutual fund flows turned from negative to positive twice before in the past 30 years, according to ICI data: in 1989, preceding market gains in eight of the next 10 years, and in 2003, when the S&P 500 rose until October 2007.

In the past, investors returned more quickly to stocks after market declines. When the S&P 500 index plunged almost 50 percent from March 2000 to October 2002 following the collapse of the technology bubble, individual investors shook off the damage and added $140 billion to stock funds in 2003. The 38 percent drop for stocks in 2008, the worst year for the U.S. benchmark since World War II, had a deeper impact on investor psychology because the losses were so widespread, according to Burton Greenwald, a mutual fund consultant in Philadelphia. "The public was beaten down," he says. "It took a long time for confidence to return."

Dismal fixed-income returns, and the potential for worse, are leading people to overcome their fear. "People seem to realize that if they want their money to grow they have to be willing to take more risk," says Theresa Wan, a financial planner in Dumont, N.J. One of her clients, retired doctor Michael Resnick of Suffern, N.Y., in July agreed with her suggestion to increase his allocation to stock funds to 35 percent of his portfolio from 30 percent. Resnick, 77, says he was wary because he has a low tolerance for absorbing losses. "But expectations for bonds are very low, maybe 2 percent or less," he says. "I'm sleeping all right." —*Charles Stein*

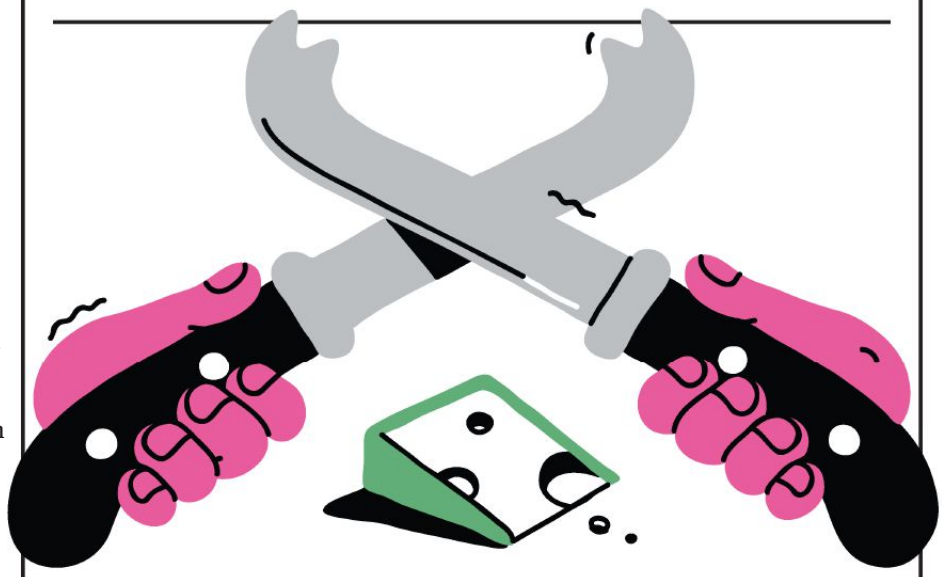
The bottom line Investors have put $148 billion into stock funds this year, after pouring $1 trillion into bond funds over the past four.

Edited by Eric Gelman
Businessweek.com/markets-and-finance

BID/ASK ILLUSTRATIONS BY OSCAR BOLTON GREEN

Bid/Ask

By Evan Applegate



$472m

A dairy bidding war Down Under drags into its third month. Bega Cheese, Murray Goulburn, and Saputo are vying for Australian milk processor Warrnambool Cheese & Butter Factory. The latest bid was made by Canada's Saputo, which is after a Pacific foothold to capitalize on Chinese demand. Bega and Murray Goulburn, both partial owners of Warrnambool, may raise their offers to keep out their foreign rival.

$2b

Deutsche Telekom sells its digital-classifieds business. The sale of Scout24 to private equity firm Hellman & Friedman will free up cash for mobile network upgrades.

$1.4b

WTGoodman wants Brazilian warehouses. The Australian REIT offered to buy 34 industrial buildings from BR Properties, which would use the money to repay debt.

$913m

China's Giant Interactive receives an offer to go private. The game company's chairman and a group of investors would pay a 21 percent premium over its share price.

$659m

EQT Holdings buys a unit of Aker Solutions. To focus on deepwater drilling, the oil company sold its well services division to the Swedish private equity fund.

$543m

DuPont sells off a glass-coatings division. Japan's Kuraray bought the Glass Laminating Solutions/Vinyls unit to expand its vinyl acetate business.

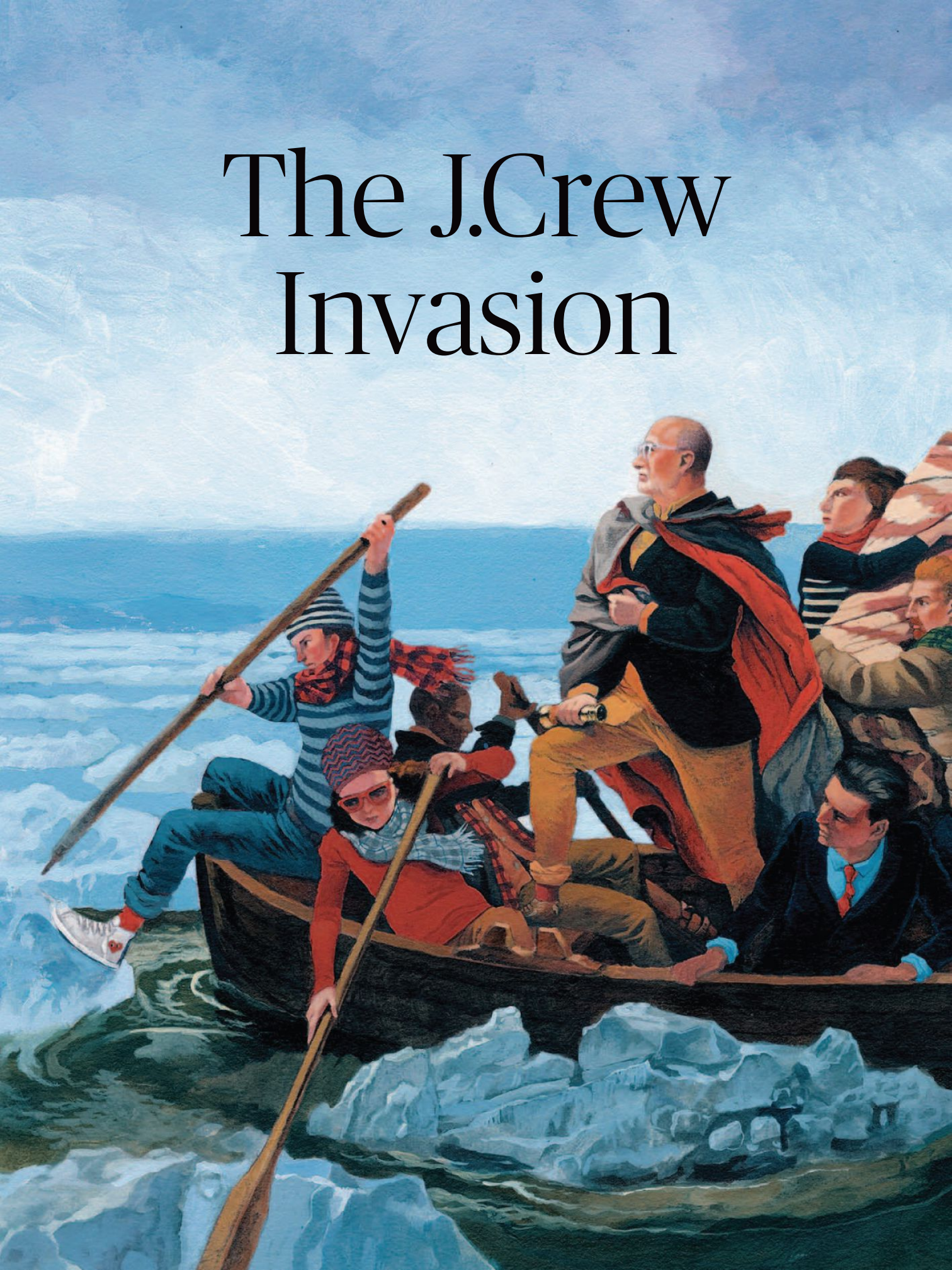
$500m

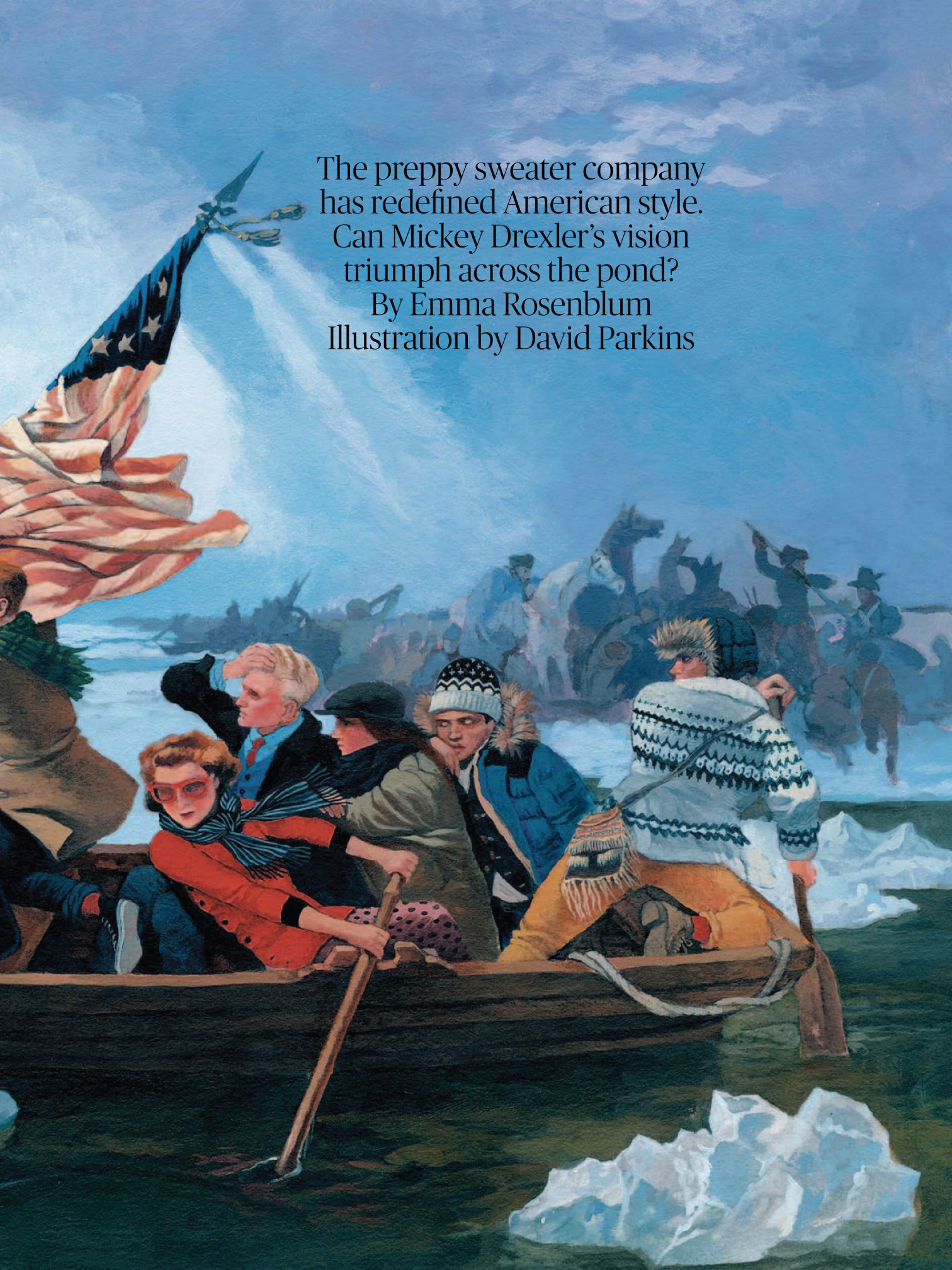
Intel sets a price for OnCue. The chipmaker wants to sell its online pay-TV service. Potential buyers could include Samsung, Verizon, and Liberty Global.

$350m

Apple acquires PrimeSense. The Israeli startup, whose technology powers Microsoft's Kinect, makes hardware that allows cameras to perceive depth and movement.

The J.Crew Invasion





The preppy sweater company has redefined American style. Can Mickey Drexler's vision triumph across the pond?

By Emma Rosenblum

Illustration by David Parkins

Dozens of shivering British fashion bloggers, TV personalities, and socialites snake down London's Regent Street, waiting patiently to get into the Nov. 6 opening night party for the J.Crew flagship store. Inside, bearded men like James Middleton, brother of Kate and Pippa, browse skinny ties and shrunken blazers. Women in full skirts and crop tops paw through tables of pastel cashmere. Everyone's hair is chicly disheveled, as are their teeth. On the stairs up to the second level of the 17,000-square-foot space, the biggest of the three J.Crew stores that opened in London in November, two partyers pause. "Oh! There's Mickey and Jenna," one whispers reverentially, pointing at J.Crew Chief Executive Officer Millard "Mickey" Drexler and Creative Director and President Jenna Lyons. He's playing town mayor in a navy blazer and a white button-down. She's in sparkly green pumps and her signature oversize black glasses. There's a photo booth and Champagne cocktails, and it's all very fabulous and also kind of funny, because it's just J.Crew, after all.

Minus a few British touches, such as mannequins topped with Grenadier Guard-style caps, the Regent Street store could be in Ohio or Nevada or New York. It's artfully filled with the latest designs from Lyons's team, the same ones sold in stores across the U.S.—women's skinny jeans and worn-in chambray shirts, men's vaguely vintage plaid button-downs and slim-cut chinos. Lyons says there was talk of tweaking the collection to be more British "for maybe five seconds," but "we have a point of view. We felt good about exporting what we were currently doing." That includes everything from hair elastics to hand-knit Fair Isle sweaters to $1,800 embellished jackets. The vibe is casually stylish, cool yet cheerful. Perfectly American. A British man in tweed stares at a baseball cap in awe.

Back in the store the next day, Drexler, sitting on a couch in the women's shoe area, is thrilled to talk about the transformation of his company from sweater catalog to the kind of international brand that draws A-listers on a chilly London night. "The party was below-the-radar cool," says Drexler. "They all looked good. Oh my God, if we could look like that!"

Drexler, 69, does look like that—with his gray scruff and translucent plastic glasses he resembles the preppy patriarch in a J.Crew ad, though his raspy accent is more Bronx than Martha's Vineyard. Drexler is constantly doing his own market research and pauses to greet some VIP shoppers. "How do you like the new store?" he asks. (Everyone loves everything, which seems to disappoint him.) "The interesting thing about apparel and clothes is that it's emotional," he continues. "People's emotions can change quickly. And the advantage we have in coming to London now is that it's not J.Crew how it used to be. It's J.Crew. It's brand new. Oh my God!"

The J.Crew that Drexler's referring to isn't that new; it's also very much a Jenna Lyons Production. Drexler took over as CEO in 2003 and plucked Lyons from relative obscurity to run all of design (she'd been at the company since 1990), promoting her to creative director in 2007. Under Lyons, who's 45, J.Crew has become an unlikely fashion force. Her style—a quirky mix of classic pieces, vivid colors, and louder, often sparkly accents—has been copied everywhere from the Gap to the pages of *Vogue*. Editor Anna Wintour is a fan, as is Michelle Obama, and since 2012, J.Crew has presented its collection at New York's Fashion Week. With prices hovering above fast-fashion chains such as Zara and H&M but below designer lines such as Alexander Wang and Thom Browne, J.Crew has found a lucrative niche as an aspirational destination for younger shoppers and the go-to store for wealthy customers seeking wardrobe staples. "I don't want to risk being arrogant, but I think a lot of what we've done has connected emotionally with America," says Drexler.

Growth has been steady; there are now 446 stores within the J.Crew family of brands in the U.S. and Canada, and last year revenue was up 20.1 percent, to $2.2 billion, according to the company. J.Crew is finally in the black. After losing $10.5 million as recently as the second quarter of 2011, its net income over the same period in 2012 topped $22 million. Even so, Drexler says, it's trying not to rush things. The words that Drexler and the president of the J.Crew brand, Libby Wadle (who heads merchandising and buying), use to describe the company's international strategy are "thoughtful" and "careful."

J.Crew rolled out shipping for online purchases in more than 100 countries last year, but the U.K. stores are its first physical outlets overseas under Drexler. He's planning two stores in Hong Kong next spring. In addition to the Regent Street flagship, there's a women's boutique in the upscale shopping area of Brompton Cross, selling the higher-priced J.Crew Collection, and a men's shop on Lambs Conduit Street that specializes in suiting. "We're not flooding the markets. We're not out to become a mass brand," says Wadle, 40, who worked with Drexler at Gap and has been at J.Crew since 2004. "And so we're putting a lot of pressure on the stores we are doing to succeed."

J.Crew is still small compared with the Gap's more than 3,000 stores—but its rise points to something significant. While fashion is inherently elitist, Lyons has made it less so. "Style is for everyone," she says. "We don't talk down to our customers." The ethos of J.Crew is design plus value; the cashmere is made in Italian mills, but costs less than at Bloomingdale's. Nothing falls apart. (If it does, the salespeople will happily replace it.) The post-2008 demand for value coincided with a resurgence in buying made-in-the-USA products and supporting local manufacturing. J.Crew smartly began beefing up its In Good Company offerings, which include American heritage brands such as Sperry Top-Sider, Red Wing Shoes, Alden Shoes, and Woolrich.

Although most of J.Crew's products are manufactured overseas, the company has come to own the Americana movement

> "The advantage we have in coming to London now is that it's not J.Crew how it used to be. It's J.Crew. It's brand new. Oh my God!"

A brief history of J.Crew, from twin sets to skinny ties

	1983	1988	1997	2003	2006
	First **catalog** hits American mailboxes	First retail store opens in South Street Seaport	Sold to TPG for $560 million	**Drexler** takes over as CEO	The company goes public
Number of stores		1	50	154	203

Drexler and Lyons at the Nov. 6 Regent Street opening night party in London

in men's fashion—rugged button-downs, broken-in-yet-slim-fitting jeans, upscale field jackets (think chic WPA workers). Older brands such as Brooks Brothers and Ralph Lauren have profited from this trend, newer lines like Band of Outsiders have also cashed in, and larger retailers like Club Monaco are moving in that direction—hence its new $450 Varsity Jacket. And Americana has gone global. In Asia, especially, there's huge demand for the "authentic" heritage brands that J.Crew has curated—Japanese buyers are bidding as much as $1,000 for Red Wing boots on EBay, and Alden has opened a successful standalone store in Shanghai, decorated with American flags. While there's no single "American look"—the country is too big, the concept too fuzzy—Drexler & Co. are betting that J.Crew is the closest thing to an exportable national style.

J.Crew is headquartered in a converted loft in downtown Manhattan near Cooper Square. On a warm November morning the streets are filled with New York University students in jeans and sweaters, girls wearing chunky necklaces and guys in old-school New Balance sneakers. Lyons's influence is everywhere. Sitting at a large table in her office, which is white and airy and piled with sketches, she talks about her role at the company. "At the end of the day, all I really want is for people to be excited about clothes," she says. She's wearing gray slacks and a navy Comme des Garçons sweater (another of J.Crew's In Good Company collaborations), an outfit that reflects her high-low aesthetic. Lyons is J.Crew the way Diane von Furstenberg is DVF; her own image is so intertwined with the clothes she creates that it's hard to separate the two. Yet she says she's not necessarily designing for herself. "You want to love what you make," she says. "I don't wear shorts, but we design lots of shorts. I can have a really robust dialogue about shorts!"

Of course, J.Crew has always sold shorts, but not the $425 leather kind that Lyons is talking about. The first J.Crew catalog arrived in American homes in 1983, filled with glossy photos of rosy-cheeked yuppies in ruffled blouses and pea coats. ("Crew" was chosen for its association with the Ivy League sport.) An offshoot of Popular Merchandise Inc., a privately held direct-selling catalog company, the brand targeted the *Official Preppy Handbook* crowd that wanted Ralph Lauren's vision of a better life but at a lower price. J.Crew took off—in 1990, founder Arthur Cinader told the *New York Times* that the company had been growing at 25 percent to 30 percent a year—and by 1988, the year before J.Crew opened its first store in New York's South Street Seaport, annual sales had reached $100 million.

By the mid-'90s, America knew its heather pine cardigans from its lilac. Crinkly brown J.Crew packages dotted suburbia's welcome mats, and college students crowded quads in barn jackets and rollneck sweaters. But by 1997, as a result of increased postage costs and management turmoil, J.Crew was foundering. The Cinaders sold a 60 percent stake to investment firm Texas Pacific Group (TPG) for $560 million and gave up day-to-day control. The company went through three CEOs in three years.

Drexler, meanwhile, was turning the Gap into the largest apparel chain in the world. Under Drexler, Gap acquired Banana Republic, launched Old Navy, and made khakis hip. He took the company from $400 million in revenue to more than $14 billion but by 2002 had made a series of strategic errors, most notably trying to make Gap more fashion-forward (the low-rider jeans were not a hit). That led to losses for 29 consecutive months and his dismissal from the company.

That same year, J.Crew posted a loss of more than $40 million. The brand had become uncool, too reminiscent of *Friends*. When the J.Crew board approached Drexler to take over—"a great name with a better fashion image than Gap," as he said—he couldn't resist. Drexler took J.Crew public in 2006, then in 2010 oversaw the sale of the company back to TPG and Leonard Green & Partners for almost $3 billion. The deal was controversial: There were reports that Drexler had been courting buyers without the board's knowledge and that he ignored bidders other than TPG. He won't talk about it except to say that, "fashion, by its nature, is not a straight-up business, and most shareholders in the public market have a very short view." In November, J.Crew issued bonds worth $500 million to pay a dividend to its owners, leading to talk of a possible initial public offering or sale within the next two years. Drexler won't comment but said in an earlier conversation, "Being private is much more fun."

Since 2010, Drexler has increasingly empowered Lyons as the company's visionary. "When we're thinking about an item, with Mickey it's never just, 'is it the right price, and how many units should we buy?' It's 'do we love it, is it beautiful, is it the thing we want?'" says Lyons. J.Crew's headquarters houses both the design and business sides of the company, and the areas look pretty indistinguishable. Racks of J.Crew clothes are everywhere, and Drexler's voice pipes over a loudspeaker for everyone to lovingly roll their eyes at. The 4,900 employees, mostly women, channel Lyons—fresh-faced, well-accessorized J.Crew soldiers. In 2006 it bought the name of defunct clothing line Madewell to use for a standalone denim brand aimed at young women that now has 64 stores. That same year it restarted Crewcuts, J.Crew's children's brand, which features $88 bejeweled dresses for girls and $65 boys' hoodies.

A few years ago, the top executives started thinking about London, but "there was never a moment of, like, 'It's time to go on a big international expansion!'" says Wadle. She says J.Crew is still growing in the U.S. but is focusing more on specialty stores—and that the brand felt particularly relevant, so the London move made sense. "We certainly weren't a pioneer coming here," says Drexler. "We did our own brand research, and then it became an easy decision." Wadle agrees, with reservations: "Am I worried? I'm not worried," adding wryly, "I'm anxious, of course."

"Historically, overseas expansion in fashion has been tricky," says Howard Davidowitz, chairman of

CLOCKWISE FROM TOP: RICHARD YOUNG/REX USA; COURTESY J.CREW (2); GAP/BLOOMBERG NEWS; AP PHOTO

Opens the first **Madewell** store

Starts In Good Company partnerships

2007

227

Hires **Muytjens** as head of menswear

2008

260

Opens the **Liquor Store** in Tribeca

Obama poses in *Vogue* wearing J.Crew

2009

300

retail consulting firm Davidowitz & Associates. "Go ask Abercrombie & Fitch," he says. Abercrombie, which made a big push into Europe starting in 2007, opening seven flagships and 62 Hollister stores, has struggled abroad. Last year comparable store sales internationally were down 8 percent, and the company announced plans to close all of its stand-alone Gilly Hicks stores, both abroad and in the U.S. "The worst thing you can do is open a bunch of stores to big fanfare and then have to retrench," says Allen Adamson, managing director of brand consultant Landor Associates.

J.Crew is part of a pack of retailers that expects to succeed in London. Mass American brands such as Victoria's Secret and Banana Republic have recently increased their presence in the city, and high-end labels like 3.1 Phillip Lim, Rag & Bone, and Opening Ceremony have opened stores there in the past year. "London is a good place to start an international rollout," says Adamson. "It's very cosmopolitan and open to brands from other parts of the world succeeding. Unlike Paris, which is very hard."

The Regent Street megastore followed J.Crew's more guerrilla-style entry, the men's shop on Lambs Conduit. It's a wisp of a spot, about the size of the large closet of a very wealthy hipster. It resembles the Liquor Store, the Partners & Spade-designed J.Crew outpost in New York's Tribeca that opened in 2008, the same year Lyons tapped designer Frank Muytjens as head of menswear. Muytjens brought a distressed yet tailored sensibility to the men's line, inspired by vintage American workwear. (Muytjens is from Amsterdam, but he spent the early part of his career at the very American Polo.) He fixed the pants fit—no more pleats, nothing oversize—and also introduced higher-end fabrics. A men's magazine darling, Muytjens managed to do for J.Crew's menswear what Lyons did for women: make it accessibly, authentically cool.

In the back section of the Lambs Conduit store, decorated with Jasper Johns prints and Brian Eno posters, is a wall of Ludlow suits. At about $800, it's J.Crew's answer to mid-priced, stylish suiting. A common sight in Brooklyn, Los Angeles, or East Austin, Tex., is a framed wedding photo in which the entire bridal party is outfitted in Ludlow suits and J.Crew bridesmaid dresses.

"This is not a store for college kids anymore. That woman over there—look," Drexler says, pointing at a middle-aged shopper in the shoe section of the Regent Street flagship. "She's buying three pairs of £375 leather ankle boots. They're made in Italy, and designed by us. We take it from our costs directly, so there isn't a double markup. These would be twice as much at a department store," he says. The gray boots, with their sleek shape and pointed toe, do look a lot like a Manolo Blahnik version that sells at Barneys New York for $1,055. But to buy the same J.Crew shoes in America, customers pay only $375. Many items in the Regent store and on the U.K. website are priced the same in pounds as in U.S. dollars. With the exchange rate at $1.60 to the pound, cute ballet flats cost 40 percent more in the U.K.

The Regent Street megastore, one of three J.Crew outlets that opened in London in November

Drexler has gotten some flack for the jacked-up British prices: "Shoppers shocked as Michelle Obama's favourite brand J.Crew lands in UK ... at double the price!" read a Nov. 8 headline in the *Daily Mail*. "Prices are different from country to country. I've been coming to Europe for decades, and it's always been that way," says Drexler. The bad press doesn't bother him. "Opening international stores enormously helps your domestic business. Because then customers will buy even more when they come to America, because it's cheaper," he says.

Drexler may sound breezy, but Lyons and Wadle are more forthcoming about the challenges of J.Crew's British invasion. "Everything's different over there, from the labeling to compliance to legal issues," says Lyons, who manages all aspects of marketing and store design. "Stuff you wouldn't think of. The lighting wattage you're allowed in London is lower, which we didn't know, and so we spent the night before the opening changing all the light bulbs. We were like, 'It's dark over there, it's dark over there!' " she says. There were also staffing issues. J.Crew prides itself on "store experience," as Wadle puts it, and finding the right salespeople has been harder than expected. Says Lyons: "When someone's in the dressing room saying, 'This isn't really working,' where we excel is having the salesperson say, 'We have these three other things, or this option online.' " To help, the team has imported staff from America to train British employees.

J.Crew is deep into its leasing negotiations for the two planned Hong Kong stores. The brand has some experience in the city—last year, it began a collaboration with upscale department store Lane Crawford, displaying J.Crew merchandise in a store-within-a-store format. Drexler says that venture "did really well, though I can't tell you the numbers, 'cause then you'd have to report them." His executives, however, seem more measured about J.Crew's move into Asia.

"The U.K. really connects well with America," says Wadle, who was promoted to her current position in April. "It's much more of a mall culture in Hong Kong," she says, "and the biggest difference is the size of store. They're smaller, and rents are much higher." The merchandising team is working on editing down J.Crew's collection for the reduced square footage while still maintaining the brand identity. They're also researching Asian sizing. "You go in with the impression that everything would have to be smaller, but we're seeing that that's not necessarily the case," says Wadle. Lyons was surprised by how many size medium sweaters were selling at Lane Crawford. "I don't know if that's expats or people wearing them slouchy. I have no idea," she says.

Asian customers have historically gravitated toward logos and the it-costs-more-so-it-must-be-better mentality, as Drexler puts it, and luxury brands like Prada, Coach, and Burberry have profited accordingly. So far, based on online sales, Lyons isn't worried about J.Crew's understated vision succeeding in Hong Kong, but "China proper? That will be a different conversation," she concedes. Ⓑ

CLOCKWISE FROM TOP: COURTESY J.CREW (3); WENDELL TEODORO/WIREIMAGE

Sold back to TPG and Leonard Green for $3 billion

Teams up with CFDA/Vogue Fashion Fund to create **capsule collections** with winners

Lyons promoted to president

2010

321

First presentation at New York's **Fashion Week**

2012

362

Wadle promoted to brand president

Three stores open in London

2013

446

George McReynolds sued Merrill Lynch for racial discrimination and won an historic settlement. Then he went back to work

The Man Who Took On Merrill

By Karen Weise
Photograph by Jono Rotman

"I'll give you as much time as you want," George McReynolds drawls, leaning back in his chair in his Nashville office. That, he says, has been his philosophy during the 30 years he's worked as a financial adviser at Merrill Lynch. At 69, he's a slow-and-steady kind of guy: He's lived in the same home for almost four decades; he never takes his tan Chevy Malibu over the speed limit.

But McReynolds couldn't wait forever to be treated equally by his employer. Over the years at Merrill—he started there in 1983—McReynolds had gotten used to inequities small and large. With only a few fellow black brokers in the Nashville office, he felt isolated. Often excluded from work social events, he took to eating lunch at his desk; if he was out, he says, the receptionist sometimes told callers he didn't work there. He also noticed that the other African American financial advisers at Merrill were rarely top producers—meaning they generated less business than their white colleagues—though they seemed to work as hard as everybody else.

In 2001 his manager asked him to team up with two younger white brokers, pooling their accounts and splitting the profits. The bulk of the combined accounts came from McReynolds. Right away the three had problems. "We didn't agree on how business should be done," he says. After two years the team broke up, and the office manager gave a majority of the accounts to the younger brokers. McReynolds says he lost $40 million in client assets and had to give up his office. His new desk was in a carrel outside the ladies' restroom. "In this business, assets equal income," McReynolds says. "It cut my income in half."

The incident made him consider suing Merrill, but he worried he'd never prevail in court. (Merrill says numerous factors could determine how the accounts were divvied up after so long.) Then, in the spring of 2004, an arbitration panel found Merrill had systemically discriminated against female brokers and awarded $2.2 million to a single employee. The ruling was part of a spate of cases women brought in the 1990s against the financial industry, including the infamous Boom-Boom Room suit against Smith Barney. At the time, women were a third of managers and executives in finance. African Americans made up 4 percent. In 2004, Merrill had almost 10,000 full brokers, not including trainees; fewer than 150 were black.

The women's victory gave McReynolds hope. Over several months that year, he and Maroc "Rocky" Howard, a former Army captain in Merrill's Dallas office, talked about filing a lawsuit. The friends, who'd met a decade earlier, knew they faced steep odds.

During the next eight years, their case meandered through the judicial system, its journey marked by personal and professional misfortune, countless legal setbacks, unexpected breakthroughs—and finally redemption, when, last August, Merrill Lynch and McReynolds announced a settlement. In terms of cash, the $160 million won for 1,400 black brokers was a record for a racial bias case.

McReynolds's case, a class suit alleging unintentional yet systemic bias, is "extremely rare," says Michael Zimmer, a law professor at Loyola University Chicago. He estimates that of the roughly 15,000 discrimination lawsuits filed each year, fewer than 100 make similarly broad claims. Most are brought by individuals contesting specific incidents. The suits are so unusual in part because they're hard to win. Workplace bias has become more subtle, Zimmer says, and thus is harder to prove, and the Supreme Court has tightened the law around class actions. And such suits are big and expensive, "because the employers fight back very hard," he says.

"They already messed up my career," McReynolds says now. "I just felt they couldn't hurt me any more." In taking Merrill to court, McReynolds put before judges a core and complex question about why the ranks of African Americans were few and their production low: Was society racist—were clients to blame for not giving their business to blacks more often—or was Merrill?

"They already messed up my career. I just felt they couldn't hurt me any more"

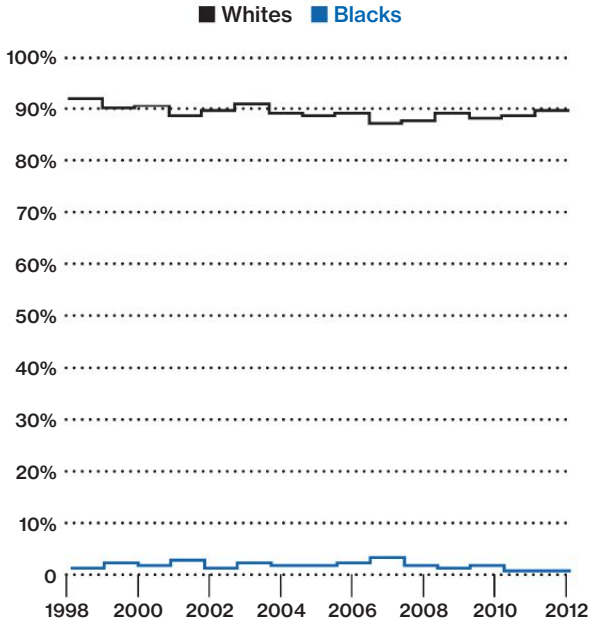
McReynolds was born in Louisville to a mother who taught third grade and a father who worked as a janitor at a bourbon distillery. After the Supreme Court's 1954 ruling in *Brown v. Board of Education*, McReynolds's elementary school became one of the first in the state to desegregate. Before he entered his integrated fifth-grade classroom for the first time, his father warned him to keep his head down and stay out of trouble. His father, he says, was like him: quiet, not one to rock the boat.

When he was a teenager, McReynolds watched a movie on his family's television that showed stockbrokers working the phones. Making deals looked like a fun job. That thought stayed with him while he worked on the Project Gemini satellite program for McDonnell Aircraft, earned an electrical engineering degree at Tennessee State University, then entered the management program at Sears. On the side, McReynolds started playing the market. He made a bit of money, and his broker suggested he join the profession. The small number of African Americans in the industry deterred him. "You know what I look like," McReynolds countered. The broker put him in touch with a black broker at Edward Jones, where McReynolds got a job in 1980, cold-calling prospects listed in the city directory. After three years, Merrill hired him.

Merrill was founded almost a century ago as Americans began longing for a piece of the action on Wall Street. They started investing in stocks in earnest after the turn of the 20th century, and by the Great Depression about a quarter of households owned equities, according to Julia Ott, an assistant professor in the history of capitalism at The New School. At the time, Merrill Lynch was a large and growing retail brokerage,

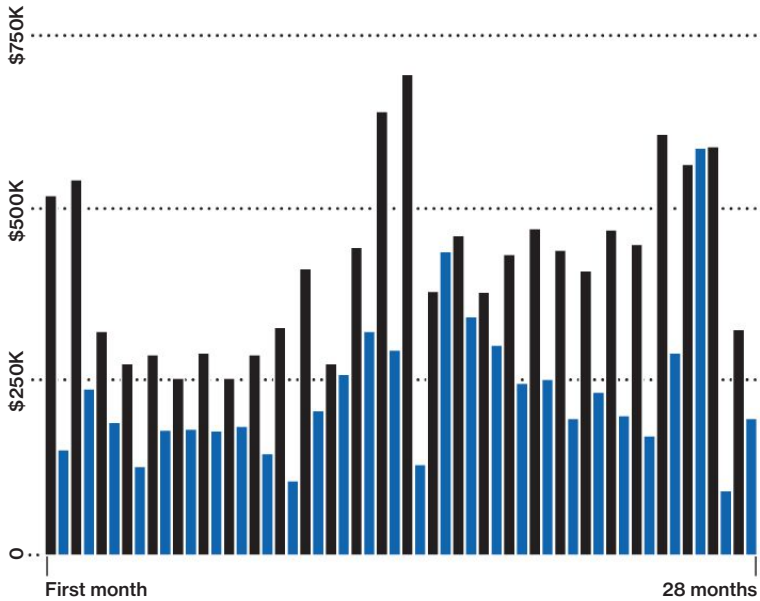
Black Brokers Are Rare...

Sales workers employed at U.S. securities brokerages



...and Even as Trainees, They're Left Behind

Average account assets Merrill transferred to trainees in each of their first 28 months, according to the plaintiffs' experts, which Merrill disputes



LINE CHART: GRAPHIC BY BLOOMBERG BUSINESSWEEK. DATA: EEOC

with about 50 offices scattered across the country. After World War II, investment returned to pre-Depression levels and stayed steady until the late '70s. The industry itself remained mostly white and male.

In 1974 the Equal Employment Opportunity Commission sued Merrill, then the biggest brokerage, over race and sex discrimination. The firm, which admitted no fault, settled and entered a consent decree promising to increase the hiring of black brokers from a little more than 1 percent of the workforce to 6.5 percent. Merrill still hadn't met this goal when the pact expired in 1995.

By the beginning of this century, more than half of Americans owned stocks. While the demographics of investors have broadened, the brokerages have been slow to change. In 1994, McReynolds flew to Chicago for an informal meeting organized by experienced black brokers at Merrill. About 50 attended. "For most of us, it was like, 'Wow, there were other blacks in the firm, and they're just like me,' " says Howard, who met McReynolds at the get-together.

They gathered in Chicago annually for the next several years to compare notes. The challenges they faced, Howard says, weren't overt. "There's no group or individual saying, 'Let's screw the black guys today,' " he says. While white brokers often partnered up, African Americans were rarely asked to join teams. And they consistently felt shortchanged when managers divvied up new accounts. All these problems seemed compounded by the fact that the bigger a broker's book, the more support—and assets—he'd get from Merrill.

Merrill started several programs over the years to help black brokers. The firm ran focus groups and took over the informal annual meetings. Some sessions Merrill organized were helpful, explaining new products and giving tips for attracting clients. But others, along the lines of "how to manage your manager," seemed tone-deaf to Howard. "You would have less success than what Obama is having in Congress trying to manage someone who didn't want you there in the first place," he says. The brokers would later assert in their suit that Merrill's efforts were superficial and didn't address the real issues they believed were holding them back—such as who gets what resources and accounts. Merrill says it focused on helping brokers bring in clients because production played an important part in its calculations for divvying up accounts.

Year after year, the number of black brokers at the firm barely budged. One black employee did particularly well: In 2000, Merrill asked Stanley O'Neal, who came up through the investment banking arm, to run the brokerages. He became chief executive officer two years later. O'Neal, as Merrill would later point out in court filings, is the grandson of a slave and grew up during the 1950s in Alabama, where his family had no indoor plumbing and lunch counters were segregated.

In 2005, Howard and McReynolds hired Chicago-based Stowell & Friedman, the firm that had represented the women against Merrill in the '90s. Stowell & Friedman took the racial-discrimination case on contingency and footed the upfront costs. Ultimately, 15 other brokers joined the suit. The plaintiffs asked the court to recognize a class of black brokers and trainees who worked at the firm from 2001 to 2006. As with most class actions, the biggest hurdle would be getting the judge to agree they had enough in common to be certified as a class. After that happens, financial expediency and exhaustion drive almost all cases toward settlements.

Merrill reacted swiftly. While it denied the claims made by McReynolds and his team, it did announce changes at the brokerages. The firm created new minority recruitment incentives, added an Office of Diversity to the duties of the unit's operating chief, and went on a hiring spree that, for a period, more than doubled the number of black financial advisers. (Not many of the new hires stuck around; the attrition rate of black brokers remains high.) O'Neal met with the plaintiffs in New York, and McReynolds got his office back. Among co-workers, though, McReynolds found the response "chilly." At the Christmas party, only a black sales assistant and a black

couple who'd retired would talk to him. "After seeing the way Merrill Lynch treated me and other African Americans, two of my children told me they would never work for a place like Merrill Lynch," McReynolds wrote in court documents. "A third child who has an MBA was told she was not qualified, even though a colleague's son without a college degree was hired."

Through it all, McReynolds kept serving his clients, hoping to see the case through. Every morning he stepped onto the elevator in the downtown office tower and pressed the button for the 17th floor, a button embellished with a drawing of Merrill's raging bull.

Merrill did not dispute that African Americans made up fewer than 2 percent of its financial advisers and were less likely than white brokers to be top producers. But it disagreed about why. The firm spent more than $12 million on eight experts who argued that society was prejudiced, not Merrill. Their data aimed to show that black brokers don't have the same access to wealth as their white counterparts, that they have weaker social networks of wealthy potential clients, and that customers are likelier to invest with brokers who are similar to themselves. Merrill said this made white brokers more likely to be higher producers, which in turn made them more desirable teammates to other brokers, who picked their own partners. And because the firm rewarded top producers with more account distributions, this also explained any differences in how new accounts were distributed.

More than a dozen Merrill executives, including O'Neal, testified that the organization was doing the best it could in a business that depended on getting access to the wealthy in America, who are largely white and inclined to socialize with people like themselves. "I think it is a fact of existence that reaching across cultural boundaries and racial boundaries ... can be a challenge in this country," O'Neal testified in a 2006 deposition, sitting across a conference table from McReynolds and at least a half-dozen other plaintiffs. He went on: "The concentration of wealth in most parts of this country ... is mostly in the hands of whites, which means, by definition almost, most African American financial advisers have to reach across racial ... boundaries to establish those relationships in order to be successful, to build a broad book of business. I think this is one of the seminal challenges of being an African American financial adviser." That, he argued, "to some degree, maybe a significant degree," accounted for why white brokers produced more.

"It was hurtful," says Marshell Miller, a plaintiff. "Although he's African American, you felt he didn't really have a clue what we were going through." Frankie Ross, another plaintiff, says O'Neal seemed to be in denial. Like the others, Ross reiterates that many, if not most, of their clients, people who have entrusted them with their savings and their retirements, are white.

Miller, Howard, Ross, and McReynolds (left to right) at the 7th Circuit courthouse in Chicago in January 2012

The plaintiffs' two experts, who charged a combined $1.6 million, argued that Merrill's policies didn't just replicate societal realities—they made them worse. They found that black brokers were far less likely to be asked to join teams than white brokers, which in turn limited the size of their books. The experts calculated that this alone accounted for as much as 28 percent of the wage gap.

They also found that, beginning in the first month of the training program for new hires, the company gave more and larger accounts from new customers or retiring brokers to the white trainees. (Merrill disputed their methodology.) That disparity was compounded by a seemingly meritocratic Merrill policy that rewarded higher producers by giving them even more accounts. "Even if all you did was give [white brokers] an advantage in Month One, blacks would always fall behind," says Linda Friedman, a lead attorney for the plaintiffs.

For McReynolds, the experts' findings were a revelation, an affirmation that he wasn't crazy. "We were working uphill, while a lot of people were on level ground," he says. Ross says the numbers the attorneys uncovered were startling. "All of the things we suspected were not only true, but there was even more," he says.

Still, Howard didn't discuss the case with his family and friends. "You are almost embarrassed that you were suffering," he says. "You were in a position where you could make by most people's definition a really good salary"—most experienced brokers, including McReynolds, usually make more than $100,000 a year—but at work, "you were being told you were a total failure." The four men who'd taken the helm of the case—McReynolds, Howard, Ross, and Miller—turned to each other, the only people who knew what they were going through. They'd formed a brotherhood, Howard says.

Amid the drawn-out discovery phase of the case, the group was rocked twice. First, in October 2007, O'Neal was ousted as Merrill collapsed under the weight of flawed subprime securities in a downward spiral that would eventually lead to Bank of America buying the firm. Three days after Christmas that year, McReynolds had a heart attack and a quadruple bypass. Complications caused his heart to stop for 17 minutes, and he remained in intensive care for three months.

McReynolds's toes, riddled with clots, were amputated. He had to stop flying to court hearings, because his special shoes made security screening a hassle. His wife, Elaine, insisted on driving the eight hours to Chicago with him for the hearings, where, over and over, they kept losing procedural battles. In August 2010, Federal District Judge Robert Gettleman dealt a major blow to McReynolds, ruling that the brokers didn't have enough in common to be called a class. The decision essentially invalidated the suit and left the plaintiffs with few options other than appealing. To Friedman, who like almost every lawyer in her firm is white, it was inconceivable that the suit might fail. The plaintiffs, on the other hand, were less surprised. They sent flowers and prayers to console her. "Any person who is breathing knows that typically whites see justice differently than African Americans," she says.

Then came a ruling that changed their luck. In the summer of 2011, in a 5-4 decision in the case of *Wal-Mart v. Dukes*, the Supreme Court ruled against female workers who had sued Wal-Mart Stores for bias. The court said that Wal-Mart's decision to give local managers the power to hire and promote workers did not constitute a nationwide policy that discriminated against women. By absolving the retailer of responsibility for local managers, the ruling was widely seen as a serious setback for future discrimination suits. But for Friedman, it had a silver lining: The justices spelled out the type of formal

policies, set at the corporate level, that could give employees the common experiences necessary to be considered a class.

The McReynolds team now argued that Merrill had nationwide policies for how brokers teamed up and how the bank doled out accounts. They lost in district court, but with a twist: In denying their class once again, Judge Gettleman made an unusual remark, encouraging Friedman to appeal his own ruling because the Wal-Mart decision had changed the legal landscape. "You've made a good argument," the judge told her in court, "and I think it deserves to be put to rest one way or the other."

The 7th Circuit Court of Appeals agreed to hear the case, and in the middle of January 2012, George and Elaine McReynolds made the snowy drive back up to Chicago. There, the brotherhood sat side by side in the wood-paneled courtroom as Friedman argued their case. During the first half of the time she had to present, the judges didn't seem to be buying her arguments. Then, Friedman drew on a trick she'd learned over years of working on civil rights cases. White people, even judges, sometimes seemed to understand gender discrimination better than racial bias, so she likened Merrill's teaming policy to when police departments first allowed women into the force. If departments allowed veteran officers to pick their own partners, the force would never have been integrated, she reasoned. This, Friedman argued, is what was happening to black brokers at Merrill. Judge Richard Posner, one of the leading conservative jurists in the country, pounced on the analogy, posing a series of additional questions. "Is it like a fraternity? They're not picked?" he asked.

"When Judge Posner related it to a fraternity, we felt somebody finally got what we were trying to say," McReynolds says. "It wasn't clear that he would rule our way, but at least he understood our perspective."

About a month after the hearing, Posner and the two other judges ruled in McReynolds's favor, ordering the district judge to certify the class. Posner wasn't saying that Merrill did discriminate—that's something that would be argued in trial—but that the brokers did face companywide policies. Citing the example of female police officers, Posner wrote that the teaming policy could set off a "vicious cycle" where black brokers aren't chosen for teams, so they earn less, so they don't get as many accounts given to them, which in turn makes them less likely to be put on teams in the future. Friedman says the decision was the first time a judge certified a racial class against a financial firm, where the certification was not itself part of a settlement.

A trial was scheduled for early 2014, but by the summer of 2013, Merrill agreed to settle. The firm denied any wrongdoing but said it would pay $160 million, the largest cash award ever in a racial-discrimination employment case. Stowell & Friedman has asked for 21 percent of the pool; the rest will be split up among the more than 1,400 black brokers employed from 2001 to September 2013. The class representatives, 17 named plaintiffs, will each get a $250,000 bonus for their involvement in the case. How much each plaintiff gets will be determined by an independent monitor, but given McReynolds's tenure, it's not hard to imagine that his take could approach $1 million.

Merrill also agreed to three years of policy changes. The firm won't distribute accounts to trainees in their first year and will place extra emphasis on the clients trainees bring in on their own. Merrill will hire two coaches to work with black brokers and two experts, one chosen by the plaintiffs and one by Merrill, to study the impact of team selection. Finally, all the settlement efforts will be overseen by a council of black brokers. "This is a very positive resolution of a lawsuit filed in 2005," Merrill Lynch spokesman Bill Halldin said in a statement. "These new initiatives, developed in partnership with African American financial advisers and their legal team, will enhance opportunities for financial advisers in the future." McReynolds will be on the committee in the first year. Similar changes implemented at Coca-Cola, after it settled a 2000 bias suit, helped make it a diversity leader. Among the soda maker's employees today is McReynolds's oldest daughter, Jennifer.

"Any person who is breathing knows that typically whites see justice differently than African Americans"

McReynolds was at home recovering from another surgery when news of the settlement broke. Elaine and his daughter Julie fielded a week of near-constant calls from the press. McReynolds received letters and calls from supporters, and one former black broker from Merrill made what Elaine calls "a pilgrimage to George" to thank him in person for bringing the suit.

The Supreme Court's ruling in *Wal-Mart v. Dukes* "no question was a setback" for class actions, says Cyrus Mehri, a plaintiffs' attorney who wasn't involved in this suit. Even with the McReynolds ruling, plaintiffs won't bring "a lot of cases" because they'd be such a long shot, he predicts. The McReynolds case has, though, "breathed life" into employment class actions in which the facts may point toward discriminatory corporate policies, he says. Stowell & Friedman, for one, is bringing a similar suit against Wells Fargo's brokerage, which declined to comment.

The men say they're ready to put the suit behind them. McReynolds expects to travel more and do some sailing, if his health holds up. But first the brotherhood will savor one last chance to be together on Dec. 6, when they expect Judge Gettleman to give the settlement final approval. Jennifer, with her husband and daughter, will meet the family at the courtroom. George, Elaine, and their two other kids will pile into the Chevy. Two decades after the brokers began informally meeting, and eight years after filing his case, McReynolds will make what he hopes is his last long drive to Chicago. Ⓑ

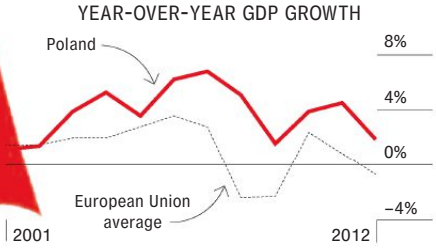
HOLY PO

HOW DID A POOR, GRAY FORMER COMMUNIST COUNTRY BECOME EUROPE'S MOST DYNAMIC ECONOMY? BY STEPHAN FARIS

The oldest coffee shop in Warsaw has been in operation nearly without interruption since the end of the 18th century. In the upstairs room, a young Frédéric Chopin played one of his last concerts before emigrating to Paris. During the Nazi occupation from 1939 to 1945, the cafe was strictly for Germans. When the city rose up at the end of the war, the building, like much of the old city around it, was completely destroyed–then reconstructed from photographs in the years following. The cafe was state-owned under communism and privatized in 1989 after the fall of the Iron Curtain, sold to a journalist and a jazz musician. "And now," says Polish businessman Adam Ringer, sitting in the cafe in early October, "it's been bought by an international company."

Ringer, 64, reopened the cafe earlier this year under the name Green Caffè Nero, a coffee chain co-owned by Ringer, another Polish partner, and the U.K.-based chain Caffe Nero. "Here you have the whole history of Poland," he says. "Look at that wall. Each brick is different. They were gathered from the ruins of prewar Warsaw." Although they're always aware of the past, Ringer and his countrymen are charging ahead. Revenue at most of his chain's locations is up 10 percent from the year before, and the company is in the midst of a rapid expansion. "People are much richer than they were, and you can easily feel it," he says.

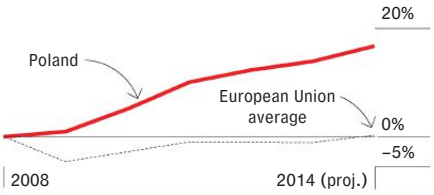
With much of Europe still struggling to recover from the impact of the 2008 financial crisis, Poland stands out as an unlikely island of economic success, a place where companies and individuals plan for growth rather than decline. In 2009, when the gross domestic product of the European Union contracted by 4.5 percent, Poland was the only country in the union to see its economy grow, by 1.6 percent. The EU economy as a whole remains smaller than it was at the beginning of 2009 and isn't



expected to recover its losses until the end of next year. In that same period, Poland is projected to enjoy a cumulative growth of more than 16 percent. "Poland didn't feel the crisis, really," says Ringer.

There are various reasons Poland, a country of 38.5 million with more than

CHANGE IN REAL GDP SINCE 2008



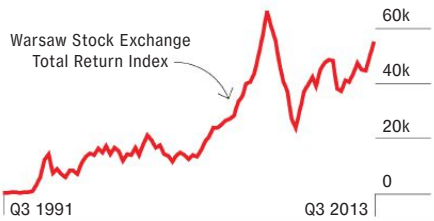
200 years of tragic history, suddenly finds itself in a position of envy. It has a large internal economy, a business-friendly political class, and the hypercharged potential of a developing country catching up with its western peers. It is playing an increasingly influential role in EU negotiations, often providing a voice of restraint during discussions on how to rebalance an off-kilter euro zone.

The secrets of Poland's resiliency trace back to the postcommunist era, when its leaders pushed through a set of painful but ultimately effective reforms. Two decades later, the country benefited from an infusion of foreign assistance at the precise moment other EU members were getting clobbered by the financial crisis. The story of the Polish miracle is a testament to the importance of prudent policymaking—but it's just as much about luck.

"I remember how it was 20 years ago," says Ringer. "Gray, dirty, with nervous people, always running." The street outside his cafe, until recently a tarmac thoroughfare, is now a narrow cobblestone lane flanked by wide sidewalks, where in the evening tourists mingle with students from the nearby university. A 20-minute walk away stands what was once the headquarters of Poland's Communist party, squatting over a small city block. From 1991 to 2000 it was home to the Warsaw Stock Exchange. Today a Ferrari dealership neighbors a Montblanc outlet.

Since the fall of the Iron Curtain, Poland has refashioned itself as a model of free-market economics. From 1989 to

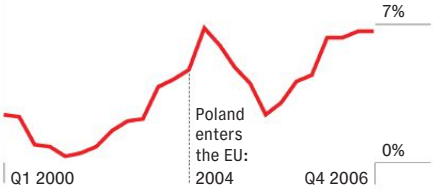
POLAND'S STOCK MARKET PERFORMANCE



2007 its economy grew 177 percent, outpacing its Central and Eastern European neighbors as it nearly tripled in size—the result of a series of aggressive measures taken by the government after the collapse of communism. Price controls were lifted, government wages were capped, trade was liberalized, and the Polish currency, the zloty, was made convertible. The policies left millions out of work but freed Poland to begin to recover from decades of mismanagement. The economy got a further boost with the country's entry into the EU in 2004.

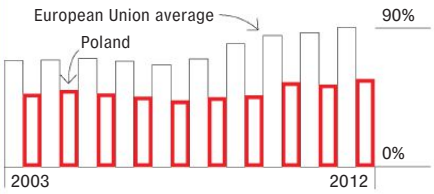
At the onset of the global financial crisis, Poland's burden of public debt was below 50 percent of GDP, low compared

POLAND'S YEAR-OVER-YEAR GDP GROWTH



with many European countries—in part the result of a clause in its 1997 constitution limiting government borrowing to 60 percent of GDP. Individual and corporate debt was relatively restrained, kept in check by strict financial regulation and a cultural aversion to borrowing. "Which

DEBT AS A PORTION OF GDP



countries suffered the biggest busts?" says Leszek Balcerowicz, an economist and former deputy prime minister who was the architect for the country's most important reforms. "Those that previously had the booms. One of the main reasons why we did not suffer a recession is because we didn't allow the boom to develop."

Private borrowing had begun to edge up in the two years before the crisis, but not so much that when the bottom dropped out of the global credit market, companies or individuals found themselves dangerously in the red. "We were late to the party," says Marcin Piatkowski, an economics professor at Warsaw's Kozminski University. "And it was over before we had time to get drunk."

Many of the characteristics of the Polish economy are shared by its Central and Eastern European neighbors, all of whom suffered deep if not catastrophic recessions in the early years of the crisis. Poland, though, had an additional advantage: It was the beneficiary of an almost accidental Keynesian stimulus that arrived just in time, boosting domestic consumption and saving the economy. "While other countries followed policies of austerity, government spending in Poland actually went up," says Gavin Rae, a professor at Kozminski University in Warsaw and author of *Poland's Return to Capitalism*. "At the point of the crisis, the foot was put on the pedal."

A series of tax cuts, including a drop in Poland's top rate from 40 percent to 32 percent, took effect just as the crisis's first shock waves were sweeping the world. Meanwhile, the EU budget for 2007-2013—which, among other things, distributes aid from richer countries to the union's poorer members—made Poland the biggest beneficiary of subsidies, showering the country with some €101.5 billion ($137 billion). Although it was not labeled a stimulus package, Poland's combination of increased spending and tax cuts was half again as large in per capita terms as the U.S.'s $800 billion American Recovery and Reinvestment Act of 2009.

Poland spent it quickly. The country had been elected along with Ukraine to host the 2012 European soccer championships, one of the biggest events in world sports. Polish officials from city councilmen to the president were eager to use the tournament as a national showcase, adding government spending to the incoming funds. The result was transformative. All across Poland, large cities and small towns underwent much-needed makeovers. In addition to new stadiums, everything from rail stations to city squares to airports were upgraded. Before the recent surge of infrastructure, Poles like to say, the country's only real highway was the one built by Adolf Hitler. Stretching from the western town of Wroclaw to the border with Germany, it was once known as the longest staircase in Europe for the sensation caused by driving over its disjointed concrete slabs.

For older Poles such as Ringer, who can remember the way things used to be, the contrast can be breathtaking. Even those too young to have lived under communism feel a palpable sense of acceleration. "It's hard to imagine how things were compared to what we have right now," says Grzegorz Inglot, executive adviser to the board of directors of Inglot, a major Polish cosmetics company. At 23, he was born the year after the fall of the Berlin Wall. "Poland is growing year by year," he says. "New investments, new roads, new buildings. It's just more of everything."

In the Continent's other capitals, shopping centers usually rise on the periphery, squeezed out of the centers by property prices and existing buildings. In Poland, wartime destruction and communist-era stagnation have left plenty of unused

GRAPHICS BY BLOOMBERG BUSINESSWEEK. DATA: EUROSTAT, DATA COMPILED BY BLOOMBERG

or underutilized lots ripe for redevelopment. Warsaw's iconic Palace of Culture and Science, a Stalinist skyscraper built by the Soviet Union in the 1950s, is flanked on both sides by shopping centers, offering brands ranging from Guess?, Hugo Boss, and H&M to Nike, Adidas, and Timberland–not to mention Burger King, Subway, KFC, and McDonald's. "We've had 20 years of transformation and growth, but we still have to catch up," says Leszek Baj, a business reporter at the daily newspaper *Gazeta Wyborcza*. Adds his colleague, Patrycja Maciejewicz: "We want to buy what everybody in Europe is buying."

Even as subsidies from the EU fueled its growth, Poland has benefited from remaining outside the common currency. From September 2008 to February 2009, the zloty lost about a third of its value relative to the euro, before stabilizing later that year at about 70 percent of its peak value. The resulting boost in global competitiveness for Polish companies quickly accomplished a rebalancing that the euro area's weaker economies are still

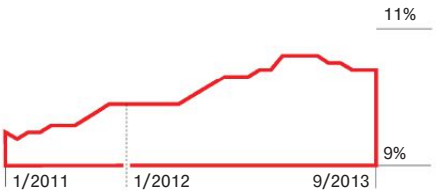
struggling to achieve. Measured in euros, the value of Polish exports dropped 15.5 percent from 2008 to 2009–but in zloty terms it grew 4.4 percent.

The drop in the zloty not only made Polish exports more competitive but also raised the relative cost of imports. The result was a boon for local companies, which increasingly are concentrating on quality. Standing in the Inglot flagship store in the upscale Galeria Mokotów mall in Warsaw, Greg Inglot says his company "felt a little slowdown, but it was nothing big. Our numbers were going up year to year." Inglot, which produces 95 percent of its cosmetics in Polish factories near the Ukraine border, has continued a rapid domestic expansion, opening 113 stores since 2009, most of them in new shopping malls. The company opened its first flagship store in the U.S. in 2009, in New York's Times Square. It now has 31 locations in the U.S. and outlets in 50 countries, including Belarus, Dubai, Guatemala, Malaysia, and the Philippines.

As Poles have gotten wealthier, their tastes have grown more sophisticated. Three years ago, when Jacek Rusiecki and his brother Michal opened their restaurant in the town of Jawor, not far from the border with the Czech Republic, the beer market was dominated by multinational breweries marketing mass-produced Polish brands. Theirs was the only establishment to introduce beers from the country's rapidly multiplying microbreweries. "Now they're all over the place," says Michal, 31. Poles of their generation are starting to demand the quality products sought by consumers across much of the rest of Europe. "Our parents remember a time when somebody high up [in the Communist Party] knew better than they did how the beer should taste," says Jacek, 28. Adds Michal, "We're coming back to explore the tastes that were here before the World Wars."

"The consumer has changed," says Małgorzata Starczewska-Krzysztoszek, chief economist at Lewiathan, Poland's private employer's confederation. "They want to have good quality for a good price." When Starczewska-Krzysztoszek surveyed small and medium enterprises in 2009, 60 percent of respondents said they were planning to compete on price and nothing else. "I was very worried," she says. "I tried to explain that we can't compete with China and India." In 2012, when she ran the numbers again, only 10.6 percent said they planned to compete on price. Nearly half said they were focused on quality.

Despite its expansion, Poland hasn't been totally shielded from the vicissitudes of the business cycle. A slight rise in unemployment in 2012, coming not long after the Euro Cup splurge, led to a sudden plunge in consumer spending. Many construction companies had

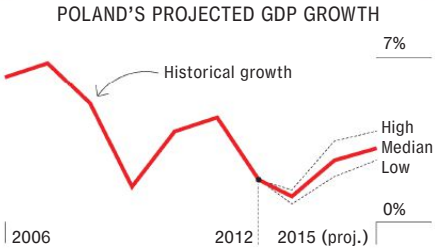


drastically underbid for Poland's infrastructure projects, leading the industry to slip into recession.

Cities found themselves with giant modern stadiums but no plans to fill them. The stadiums are largely unprofitable, pulling in too little through conferences, concerts, and the occasional game to pay for their maintenance, much less to pay down the loans that were taken to fund them. "The spending gave the economy a boost, but in the long term it wasn't necessarily a wise investment for the country," says Rae.

Poland also must address some long-deferred fiscal challenges. The government is pushing up against the constitutional debt limit and is desperate for funds. Many Poles say a recent change to the pension system, in which privately held funds are being transferred into the state system, is motivated by an effort to shore up the balance sheets. "They've done a lot of creative accounting to keep the deficit down," says Andrew Kureth, editor-in-chief of the *Warsaw Business Journal*, an English-language newsweekly. Unemployment remains stubbornly high at 10.3 percent; among the young, the figure is 26 percent. In September the country's trade unions organized one of the largest demonstrations since 1989, protesting working conditions. Prime Minister Donald Tusk recently reshuffled his cabinet, fired his finance minister, and pledged "an acceleration of economic growth."

Despite some inevitable problems, Poles have reason to remain optimistic. Growth next year is projected to be



2.5 percent, driven in part by a recovery in parts of the EU, especially Germany, the destination of more than 25 percent of Polish exports. The EU budget for 2014-2020 was the first in the union's history that saw cuts in total spending, but the money allocated to Poland rose nonetheless. Because of a mix of factors–including its size and proximity to Germany, the EU's biggest economy–Poland is eligible for €105.8 billion, making it once again the biggest beneficiary among member states. The funds are expected to start flowing by the end of 2014.

It isn't just money that's pouring in. In addition to Green Caffè Nero, Ringer runs a training center that helps doctors prepare for positions across Europe. When he started 13 years ago, the students were almost exclusively Poles. In recent years, as Polish doctors began to receive attractive wages at home, the school has suddenly found itself catering to Greeks, Spaniards, Portuguese, and Croatians. "Can you imagine a Greek doctor coming to Warsaw to learn Norwegian and then moving to Western Europe?" says Ringer. "That's the European Union right there." And Poland is one place where, for now, anything seems possible. Ⓑ

SCHOOL CONTACT INFORMATION

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ETC

SHE'S THE BOSS

How Alyssa Milano created a fan-gear fashion empire for women. By Joel Stein

Photographs by Ramona Rosales

Alyssa Milano isn't crazy about pink. "I was in Dodger Stadium, and I was freezing—it was the beginning of the season, before the poop smell sets in," says the star of TV's *Who's the Boss?* and *Charmed*, recalling a baseball game she attended eight years ago. "I went into the store to get something warm to wear. And I was offended." The only color available in women's clothing was pink. "Their answer for female sports apparel back then was 'pink it and shrink it.' It was either that or buy something from the kids' section. Which I did. I got a kid's hoodie." In Dodger blue.

Milano, 40, figured she could do better than the mini Pepto-Bismol tees. So in 2007 she paid a fashion illustrator to draw some less boxy, team-color-appropriate clothing. Her agent happened to be friends with someone at Major League Baseball's marketing division and got her a meeting with some execs. They liked her idea enough to set her up with former New York Giant Carl Banks, who runs the sports clothing collection for G-III Apparel Group, the $1.2 billion company that has licensing deals with Levi's, Guess?, Calvin Klein, and the major sports leagues. G-III Apparel agreed to manufacture and distribute her nascent line, Touch by Alyssa Milano, which had this motto: "Where the game meets the after party."

MORE WOMEN WATCH THE SUPER BOWL THAN THE OSCARS

"My idea was to make Touch fashionable enough for women to wear outside the arena," Milano says. The line, which was launched in 2008, now includes $85 quilted jackets in team colors, $45 jeans with logos on the back pockets, and $30 pendant necklaces with the logo in a crystal-lined silver heart. Milano chose the designs and modeled every piece on her website.

Still, her pitch meetings were a bust. She had trouble convincing team buyers that she even knew enough about sports to understand what she was selling. "It was a lot of work to validate my passion and knowledge. It's probably what every woman goes through when she's a sports fan. Except I was trying to validate it to Jim Rome," she says of being interviewed by the loudmouthed sports talk show host. Milano grew up in Brooklyn, where she bonded with her dad and brother over New York Giants and L.A. Dodgers games. (Her dad stayed loyal even when the Dodgers did not.) She's dated several professional athletes, such as hockey player Wayne McBean and pitchers Carl Pavano, Barry Zito, and Brad Penny. She's also had L.A. Kings season tickets since she was 15 and Dodgers season tickets for the past 10 years. Milano blogs for MLB.com; hosts segments on the TBS network called *Hot Corner*; and wrote a book in 2009 called *Safe at Home: Confessions of a Baseball Fanatic*. Her Australian shepherd is named Dodger Dog.

When Milano failed to score much retail space in stadiums, she started selling Touch merchandise through MLB.com and her own website in time for 2008 spring training. The collection sold out in five weeks, which surprised everyone, including G-III, which had no quick response plan to supplement stock. It lost time and profits while restarting production overseas. The clothing was cute, fit well, and had an American Eagle vibe. Most important, it filled a hole no one had realized existed. "We recognized that Milano was a go-getter. It wasn't like, 'Here's my name, you can make a hangtag and put it on there.' This was, 'I'm sitting in on the focus groups, and I'm sitting with the designers,' " says Tim Brosnan, MLB's executive vice president.

After her one year of exclusivity with baseball ended, Milano added deals with the NFL, NHL, NBA, and some colleges, and has since added Nascar, MLS, and minor

MILANO: PHOTOGRAPHS BY RAMONA ROSALES FOR BLOOMBERG BUSINESSWEEK; PROP STYLING: GEORGE SEGAL; WARDROBE: JULIE MATOS; MAKEUP: STELLA KAYE; HAIR: DAVID KEOUGH; PRODUCT PHOTOGRAPHS BY 731

RETHINKING PINK

A sampling of Milano's Touch collection

L.A. Dodgers triple play tank top; $37.95

Washington Capitals scripted three-quarter-sleeve T-shirt; $39.95

Baltimore Ravens chain-and-leather-strap bracelet; $23.95

Kyle Busch all-star tri-blend slim-fit T-shirt; $34.95

Miami Heat Signature jeans; $45

league baseball. Touch is now the only apparel company with licensing agreements for women's clothes with all the major American sports. "You could identify her as the driver for what now is an accepted part of the business. Retail buyers now come to the table expecting that you have a full female offering," Brosnan says. There's a Touch boutique in the Mets' Citi Field, and Bloomingdale's and Lord & Taylor carry the line.

Touch has grown every year, even during the recession, and Milano spends a few hours every day marketing the brand by showing up at playoff games and store signings. "I send a lot of stuff to players' wives," she adds. Milano still models nearly everything herself and even writes poems that she puts on ads and hangtags:

To rally for each other
To play fair
To run with abandon
To dance with life
Is to Touch

There weren't a lot of poems at stadiums before that.

As soon as Touch proved that women will wear jerseys in public—away from games—and around other women, the big sports apparel companies, including Nike and Reebok, came out with more fashionable lines of women's team wear. In 2010, Victoria's Secret introduced team-licensed clothing as part of its younger Pink line, including leggings, panties, and a shirt that says "Fantasy Player." More recently, CoverGirl packaged groups of nail color and gave instructions for making "fanicures." Marchesa sold a Swarovski crystal-bejeweled Jets top for $110 in 2012. And this fall, former pro wrestler and Baltimore Ravens cheerleader Stacey Keibler landed licenses with several teams to sell, through sportswear line Meesh & Mia, a $180 New England Patriots faux fur vest along with other items. "Milano gets all the credit in the world for being a trailblazer," says Leo Kane, the NFL's senior vice president for consumer products.

VICTORIA'S SECRET HAS TEAM-LICENSED PANTIES. MARCHESA MADE A BEJEWELED JETS TOP

Milano was prescient: Some 46 percent of self-identified MLB fans today are women, and 44 percent of NFL TV viewers are women, up from 34 percent in 2011. More women watch the Super Bowl than the Oscars—46 percent of the viewers for that game are women, up from 14 percent in 2002. In turn, the NFL reports that spending on women's apparel has risen 76 percent since 2010. Milano's line captures only a small percentage of that segment, but she still says Touch is one of her proudest accomplishments. "I could live off the money I'm making, but it's not as much as you might think. You're cutting the pie in many different ways because of the leagues," she says. "It's not Jessica Simpson clothing line kind of money."

As in regular stores, women do far more buying at stadiums than men, and so the leagues realized they were leaving a lot of money on the table. "Men are likely to wear last year's or, God forbid, something from 10 years ago. She will buy every year and buy for other people in her life," Kane says. The NFL started its own women's line in 2010 under Tracey Bleczinski, the vice president of consumer products (who recently left to head consumer products for the Ultimate Fighting Championship). The line includes maternity wear and is promoted with ads featuring Condoleezza Rice, Serena Williams, Melania Trump, and supermodel Karolina Kurkova. This season, the NFL put so-called style lounges, with dressing rooms, in 10 stadiums, and advertised its women's clothes in a 16-page *Marie Claire* insert called "The Savvy Girl's Guide to Football." NFL Commissioner Roger Goodell sat front row at designer Kimberly Ovitz's show during New York Fashion Week, because women's clothing is now something Goodell has to know about.

Marshal Cohen, the chief industry analyst at NPD Group, doesn't credit Milano with creating the category but says she "ignited it." Products that are made specifically for women, he says, now make up 17 percent of sports apparel, whereas eight years ago it was close to zero. "There are two big surprises in the world of fashion: Why they don't make more plus-size clothing, and they don't make sports-branded product for women," he says. "The sports apparel business is steeped in tradition. It was too far-fetched from where they were. It took a jolt of recognition and an experiment." In January, Milano will launch another venture, a comic book series called *Hacktivist*, about an Anonymous-like group. "I really like breaking into businesses where women aren't as predominant," she says. Ⓑ

NON-CHAMPAGNE CHAMPAGNES

This season, the most enticing bottles don't come from a certain region in France. By Evan S. Benn

2004 CA' DEL BOSCO FRANCIACORTA ANNAMARIA CLEMENTI ROSE, ITALY

The hills of Franciacorta in north-central Italy produce the juicy pinot nero grapes used to make this delicious sparkler. French law requires aging Champagnes for at least 30 months before releasing them for sale; this one spent 84 months bottle-aging. That extra time in contact with yeast adds depth, along with aromas and flavors of lime, raspberry, and fresh-cut grass.
PERFECT FOR: celebrating a new job. *$119.95*

2008 IRON HORSE CLASSIC VINTAGE BRUT, CALIFORNIA

This Sonoma County vineyard specializes in chardonnay and pinot noir, which are the traditional Champagne grapes. No surprise then that most of their sparkling wines are exceptional. With comforting notes of toasted bread and pie spices, the 2008 brut is one of the winery's best, and it's well-suited to the holiday comfort food season.
PERFECT FOR: sharing with friends at a dinner party. *$37.95*

THIERRY GERMAIN BULLES DE ROCHE SAUMUR BRUT NV, FRANCE

The Loire Valley's Vouvray region has been popular in wine circles for a few years now. But the nearby Saumur area, where winemaker Thierry Germain crafts his exceptional nonvintage blends, is still relatively unknown. In this bottle, chenin blanc grapes dominate, resulting in a fizz that's minerally, bone-dry, and highly acidic with a beautiful lemon color.
PERFECT FOR: impressing your wine snob co-workers. *$16.95*

PHOTOGRAPHS BY AARON DYER FOR BLOOMBERG BUSINESSWEEK

QUARTZ REEF METHODE TRADITIONNELLE ROSE BRUT, NEW ZEALAND

Winemaker Rudi Bauer creates this salmon-pink rosé from handpicked grapes grown in a single vineyard in south-central New Zealand, where he extracts the full flavor of the grape. Its first taste of cherry and rhubarb turns to an almost creamy finish, making it a no-brainer to pour with dessert.
PERFECT FOR: a Thanksgiving or New Year's Eve host gift. *$33.95*

SZIGETI GRUNER VELTLINER BRUT NV, AUSTRIA

Szigeti, a winery that sits on Austria's Hungarian border, ferments grüner veltliner grapes, which are standard for wines in the country but unheard of in the world of bubbly. This option balances peachlike sweetness with peppery spice, making it incredibly versatile with food. It's a thoughtful gift for a Champagne aficionado, but if you keep it for yourself, enjoy with ice-cold oysters.
PERFECT FOR: right now. *$20*

GO TO WWW.WINE-SEARCHER.COM TO FIND THESE BOTTLES AT SHOPS NEAR YOU.

BUZZWORDS

Five terms to make buying bubbly easier

BRUT
Extra brut, brut, and extra dry reflect in descending order the amount of residual sugar in sparkling wine. The middle option balances a dry finish with sweetness.

METHODE CHAMPENOISE
Certain wines that have undergone centuries-old production processes fall under this classification. Faster and cheaper methods create an inferior swill.

CREMANT
French for creamy, these wines have less carbonation and are often light and herbal. Seven regions in France and one in Luxembourg have designated producers.

A YEAR (ANY YEAR, REALLY)
Winemakers focus on the best years for vintage wines—made with grapes primarily from one harvest—so a date signifies higher status. Nonvintage wines (labeled NV) are typically less expensive.

CHEAP VINEYARD TO KNOW: GRUET
You can count on this U.S. producer for two reasons: 1) The bottles offer tremendous value. 2) The vineyard, based off the grid in New Mexico, distributes nine sparkling varieties to all 48 continental states.

HOW TO OPEN, POUR, DRINK, AND STORE

Stand it up
It's best to keep most wines in a cool, dark place on their sides to prevent corks from drying out. But sparkling wine should be left upright, because carbonation produces enough humidity to keep corks damp. A study commissioned by the French government found spoilage can occur in fizzy bottles kept on their sides, as their flared corks shrink from too much moisture and allow in oxygen.

Cool it down
A chill keeps bubbles small. Too warm, sparkling wine gets frothy. Too cold, aromas and flavors disappear. Two hours in the fridge is ideal.

Hiss, don't pop
The sommelier-approved way to serve sparkling wine is to secure the cork with one hand and slowly twist the bottle with your other hand, applying downward pressure as the cork rises. You should hear a little hiss, not a loud pop, as gas exits.

Sip, savor, repeat
Sparkling wine works alone as a celebratory aperitif, but the crisp carbonation and bright acidity make it an ideal match for fatty foods like cheese, roasted duck, or tempura-fried vegetables. With each sip, the bubbles will refresh your palate.

If you must show off
To saber, start with a cold bottle and remove the foil, wire cage, and paper label at the neck. Standing outdoors, hold the bottle near its base in the palm of your nondominant hand at a 45-degree angle, pointed away from people. Find the vertical seam on the glass and hold a long chef's knife (or sword) flat against it, with the dull edge aimed toward the top. Swiftly run the blade along the seam and strike the neck's ring, which will come off clean. Follow through.

Finish the bottle
Sorry, but you shouldn't save any for later: Food scientists have concluded the old spoon-in-the-neck trick to be bogus.

IT'S POSITIVE!

Clearblue is winning over the pregnancy-test market with the help of new technology and reality stars

By Jessica Grose

In October two celebrities posted pictures of their positive pregnancy tests on Twitter. Kendra Wilkinson—former Playboy bunny, now on WEtv's *Kendra on Top*—tweeted, "Round two. Here we go!! :)" on Oct. 31 with the hashtag #ClearblueConfirmed. She included a smiling selfie featuring a Clearblue Advanced Pregnancy Test with Weeks Estimator, which confirmed she was more than three weeks along. This was quickly retweeted 1,500 times, and more than 5,000 fans marked it a favorite. Nine days earlier, Melissa Rycroft, erstwhile *Bachelor* contestant, tweeted using the same hashtag about expecting her second child. The post was sandwiched between musings on Funyuns and hair conditioner.

Clearblue's Weeks Estimator, which hit stores in May, uses new technology that informs if you're one-to-two weeks, two-to-three weeks, or three-plus weeks pregnant. Standard kits test urine for the hCG hormone—if it's there, you're with child—but this innovation measures the concentration of that indicator. And while it may seem bizarre for Clearblue to advertise a new product by having D-list celebrities tweet pictures of pee sticks, it's actually smart marketing.

Swiss Precision Diagnostics (SPD), the maker of Clearblue, is capitalizing on an Internet trend: The Web is littered with hundreds of thousands of young women revealing pregnancy-test results in YouTube videos, Instagrams, and Facebook photos. Clearblue's brand manager, Kirsten Suarez, says the company reached out to Wilkinson and Rycroft to tweet their positive pregnancy tests after seeing many customers post the news on its Facebook page.

SPD, a venture between Procter & Gamble and Alere, has a 25 percent share of the $228 million pregnancy-testing industry. It competes with Insight Pharmaceuticals, which makes e.p.t tests, and Church & Dwight, which makes First Response. Clearblue pioneered the hCG concentration test, and it may woo Gen Y consumers, says IbisWorld researcher Jocelyn Phillips. "Millennials want things to be as high-tech as possible, and they're having kids later, so they have the disposable income," she says. These women might be willing to pay more—the digital test costs about $20 for two, compared with the standard test at $15 for two. (Insight Pharmaceuticals and Church & Dwight are likely working on similar advancements, she says.)

Analysts predict the industry will grow an annualized 1.5 percent in the next five years because of a postrecession baby boom, yet Phillips anticipates a pregnancy-test plateau. As more young women become eligible for health insurance through the Affordable Care Act, they can visit doctors for more accurate results. In the late 1970s, when home pregnancy tests hit the market, one of their biggest appeals was the privacy factor. In 2013 most women, regardless of marital status, aren't embarrassed to go to the obstetrician.

But Clearblue is betting on it being more fun for women to post pictures of their results online, from the comfort of their own bathroom. The visit to the doctor's office doesn't trump a few hundred favorites from friends. B

ASK A BILLIONAIRE

Dyson's first invention was the Rotork Sea Truck, a watercraft he sold while in art school

James Dyson
Managing director, Dyson
Net worth: $4.4 billion

HOW DO YOU DEAL WITH NEGATIVE FEEDBACK?

—@amalt

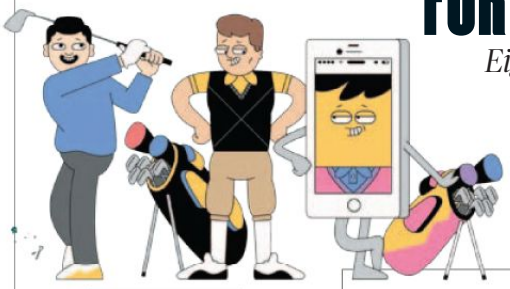
You learn from it. Often it starts a line of development: Well, yes, that person said they want a light vacuum, which is impossible, because motors are very heavy. So you say, "We might develop light electric motors—no one's ever done it before; we must do it." About 18 years ago, we set off on that journey. It took us 15 years before we launched a revolutionary small, light motor. Negative feedback is really interesting. I enjoy it in a masochistic way.

Submit your questions on Twitter with the hashtag #askabillionaire.

PREGNANCY TEST: JEFFERY HAMILTON/GETTY IMAGES; DYSON: PHOTOGRAPH BY KALPESH LATHIGRA FOR BLOOMBERG BUSINESSWEEK

THE BEST APPS FOR CLIENT ENTERTAINING

Eight ways to impress your guests
By Sam Grobart



The journey begins.

"Hey, we're business-people. Of course we golf."

PGA TOUR CADDIE

With more than 40,000 golf courses on file, this helps your foursome on just about any links in the world. Tour Caddie's features include yardage books, 3D flyovers of holes, and statistic tracking so you can evaluate your game. It uses GPS to calculate distance to the green, and if you track your shots, it will even make club recommendations. No tipping required.

"Eh, let's watch some real athletes."

SEAT SHERPA

This maps out hundreds of stadiums and sports arenas—helpful if your duties include getting tickets for a Final Four game. The app provides seating charts and allows users to upload photos and videos so you can check the view before you buy. You can store maps offline for easy retrieval.

"Famished. Who wants to eat?"

EATER

Why Eater and not, say, Yelp or Zagat? Those apps tell you about places people love—Eater tells you about the restaurants that people are going to love. There are two lists: The best restaurants in town—tried-and-true bastions of excellence—and the newest places everyone wants to check out next. Between the two, you'll find a spot that pleases conservative or daring tablemates.

FOURSQUARE

You may think Foursquare is just an app people use to stalk one another, but it's evolved into a location-specific gold mine. It has access to more than 250,000 menus and collects all comments from previous visitors, so you'll know that when you're at, say, New York's Minetta Tavern, the Black Label Burger is a must.

"Oops! We forgot to make a reservation."

OPENTABLE

You have OpenTable on your phone, right? No? Go do that. OpenTable shows up-to-the-minute availability at restaurants—more than 30,000 of them—in almost every major city in the U.S. and some smaller towns as well. Menu info and user reviews help set expectations.

"What do we feel like—red or white?"

WINERATINGS+

The waiter hands you the wine list. It's on you now. Cool your nerves with *Wine Spectator*'s app, WineRatings+. While your clients are chatting about today's boardroom drama, quickly search the magazine's database of almost 300,000 bottles to check ratings. A vintage chart gives the best years from a particular region. Or scan preselected lists such as Top 100 Wines or Blue Chip Collectibles.

"Get home safe, now." Handshakes, etc.

UBER

Yes, there are other car-service apps, but Uber is the only one that's reliable. When the check arrives, open the app and choose a car. Uber bills the ride to the credit card you have on file and e-mails a receipt. Because it ties you in to a network of drivers, you won't be waiting on hold with some car-service company while your guests are getting their coats.

"Nice to finally put a face to the name."

CARDMUNCH

"Here's my card." You heard that a dozen times. Snap a photo of each with CardMunch. The service, a part of LinkedIn, has actual humans transcribe them, which is much more accurate than apps using optical character recognition. You'll also get a LinkedIn profile when the data's returned to you, in anywhere from an hour to overnight. Keep everything in the app or copy to your phone book.

"Hello, couch."

ILLUSTRATIONS BY DAN WOODGER

TOUCH OF GRAY

Two pop acts try to stay relevant by targeting older fans

By Claire Suddath

Britney's back. Back again. On Nov. 29, the 31-year-old pop star released her eighth studio album, *Britney Jean*, a Dr. Luke and will.i.am production. This isn't a triumphant declaration that "Britney's here to stay!"—that was the job of her 2008 album, *Circus*—it's more like a comforting acknowledgment that she's still alive. Britney and Jean are her first and middle names.

Instead of touring to promote the album, Spears has opted for a two-year residency at the Planet Hollywood Resort & Casino in Las Vegas, where she'll perform a 90-minute retrospective of hits 48 times a year. Her first show is on Dec. 27, at which time her transition from virginal schoolgirl to bald paparazzi target to Celine Dion will be complete.

Vegas visitors can currently catch Rod Stewart, Olivia Newton-John, Carlos Santana, and Tim McGraw and Faith Hill, among others, but "as far as I know, this is the first pop star residency ever [of Spears's generation]," says Jason Gastwirth, senior vice president for marketing and entertainment at Caesars Entertainment, which owns Planet Hollywood. The gossip sites are claiming Spears will make $15 million a year for the gig. (In 2011, Caesars paid Dion $100 million for a three-year run.) The casino has outfitted its venue with a dance floor for the audience, which it expects to be men and women in their 30s, loyal Spears fans who grew up listening to her music. Work it, old people.

Pop has had a hold on the music charts since the late 1990s, when Spears, Christina Aguilera, and a glut of color-coordinated boy bands unseated grunge. According to industry trade magazine *Music & Copyright*, pop music accounted for 31 percent of global music sales in 2012—that works out to about $7.4 billion.

Yet profitable longevity is tricky for teen idols. Miley Cyrus released her breakout album, *Bangerz*, this year and found success and controversy by jumping into adulthood in one big swoop. Justin Timberlake, of course, is the gold standard. He broke from 'N Sync in 2002, but it took until his 2006 album, *FutureSex/LoveSounds*, along with several appearances on *Saturday Night Live*, for people over the legal drinking age to admit they liked him. The rest of the members of 'N Sync, well, they weren't so lucky. (Poor Lance Bass didn't even make it to space.) Spears has tried to win 'em over with consistency. Her sound hasn't changed much since her 1999 debut, *...Baby One More Time*. She hasn't suffered for it—*Circus* made its debut at No. 1, selling 505,000 copies its first week. Yet no one is a "new" Britney Spears fan.

With *Midnight Memories*, out on Nov. 25, boy band One Direction is taking a subtler approach to growing up, gently sliding down pop's spectrum, hoping no one makes a big fuss. The Simon Cowell-backed group, whose five members are all between 19 and 21, is clearly attempting to wean itself off the tweenybopper market in favor of fans closer to its own age—the album still contains references to first kisses and fights with parents, but it also has a number of simple love tunes aimed at more mature audiences. They're already coming around: A February StubHub! survey found that 46 percent of the group's fans were older than 35.

The songs on *Midnight Memories* are crisp and clean. Some make use of '80s guitar riffs; others, such as *Story of My Life* and *Strong*, adopt Mumford & Sons-esque banjos and hand claps. If *You & I* (chorus: "We can make it 'til the end / Nothing can come between you and I") doesn't appear on some sappy, flash mob proposal video soon, the Internet isn't doing its job.

BRITNEY IS AGING, AND EVEN ONE DIRECTION IS GROWING UP

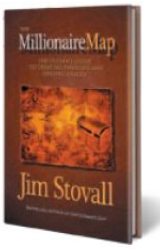
It's going to take some time, and probably more than one album, before One Direction sheds its *Tiger Beat* image. Directioners, as the group's teenage followers call themselves, are so blindly fanatic about their idols that they eschew any critical interpretation of the band's music. Earlier this year, when critics pointed out that the intro to *Midnight Memories*' first single, *Best Song Ever*, sounded like the guitar riff in the Who's *Baba O'Riley*, fans launched a Twitter attack on The Who, writing things like "WHO THE HELL IS THE WHO EVEN?" Eventually, Pete Townshend had to release a statement saying he wasn't going to sue One Direction and that he did like them. That's one way to win over an older listener. B

BUSINESS BOOK HAIKU

KEEP YOUR DAY JOB

Social media
Is kind of like
a fistfight?
Hashtag incorrect.

Sure, quit your
dull job!
You won't miss
the money spent
On this dumb
book. Swear.



Here's how
to get rich:
Become a haiku
writer!
Now where's my
book deal?

SPEARS: JASON KEMPIN/GETTY IMAGES; ONE DIRECTION: LARRY BUSACCA/GETTY IMAGES

ARMAND KHATRI

26, account executive, Federated Media Publishing, New York

What's Federated Media?
It's a digital advertising company. We connect bloggers with Fortune 100 brands for advertising opportunities. I work with Pepsi, Nestlé, General Mills, and Comcast.

What's your look?
Neat. I'm tall and thin, so I have my dress shirts tailored to fit perfectly.

What do you like most in clothes?
The whimsical elements that garner smiles.

Like your blazer lining?
Yes! I found it at a sample sale and absolutely love the very cool lining. I love small details in clothing that are not necessarily noticeable at first glance, like contrast stitching.

Does your style reflect your work personality?
When I'm reaching out to new clients, noticing small details can make all the difference in them feeling it's worth their time to respond to you.

I like your socks.
Dominic, one of my co-workers, started an Instagram hashtag called #sockgametuesday. It's become a big thing here. It's a photo of your Tuesday socks.

Did you go buy more?
Yeah. I already had quite a few, but you don't want to repost the same pairs every Tuesday. I particularly like this pair because they came in a two-pack, so I gave Dom one. We're brothers in socks.

What's the dress code?
We don't necessarily have one, and people usually have things going on after work. Not like those boring people who just go home. I'm not knocking that! Most nights I go home, too. I like my eight hours.

Interview by Arianne Cohen

PHOTOGRAPH BY CHRISTOPHER LEAMAN FOR BLOOMBERG BUSINESSWEEK

FRITS VAN PAASSCHEN

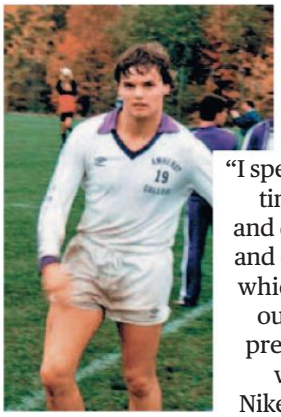
President and chief executive officer, Starwood Hotels & Resorts Worldwide

EDUCATION

- Mercer Island High School, Mercer Island, Wash., class of 1979
- Amherst College, Amherst, Mass., class of 1983
- Harvard Business School, class of 1988

"I actually can't remember doing much homework in high school. I'm sure it happened, but it wasn't much."

"These were the most important years of my life. I met my wife there. I also ran my best marathon."



"I spent most of my time running and drinking beer and oversleeping, which as it turns out was great preparation for working at Nike, Coors, and Starwood."

WORK EXPERIENCE

- **1976-83** Dishwasher, janitor, newspaper delivery boy
- **1983-85** Consultant, Boston Consulting Group
- **1989-95** Consultant, McKinsey
- **1995-97** Vice president of finance and planning for Disney consumer product, Walt Disney
- **1997-2004** Corporate vice president and general manager, Europe, Middle East, Africa, Nike
- **2004-07** President and CEO, Coors
- **2007-PRESENT** CEO, Starwood
- **2013** Runs his 13th marathon

"I thought I wanted to be a doctor until I read a *Harper's* article about young consultants doing all these cool things for companies. I had no idea that was even a job until then."

"My biggest coup was making $300 in a carpet shampooing business."

"Disney was such an American-focused company at that time. I kept telling them that there was an opportunity for growth around the world."

"We didn't worry about market research. We were trying to solve problems for athletes, not create products that maybe athletes would like to use."

"We were losing share volume. I remember one day someone said the only thing we know for sure is that people who drink light beer like to drink it cold. That's how we came up with the frost brew liner."

"I'd interviewed for the job before but didn't get it. I read in the newspaper that they were looking for a CEO. I said to my wife, 'I still want that job.'"

Opening the renovated Le Méridien Al Khobar in 2011

"I've been running ever since 1968, when I watched the Olympics on TV and decided I wanted to become a runner. I was 7 years old."

LIFE LESSONS

1. "Effort is more important than talent." **2.** "Being bilingual helps you appreciate that people might see things very differently than you." **3.** "Anyone who believes he's a self-made man has a very selective memory."

Top: Michael Buckner/Getty Images; vacuum: Eye-Stock/Alamy; Mickey: Ben Hider/Getty Images

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kia.com

Introducing our world-class luxury sedan, the K900.

They say tradition and heritage are what make a luxury sedan, but is that truly the case? Or is it the fact that it's meticulously crafted from the finest materials available? Or that it's equipped with the most advanced onboard technology and is the perfect combination of comfort, power and elegant design? While others may be convinced that history is what defines a luxury sedan, we invite you to come to your own conclusion. Experience the K900 for yourself at kia.com/K900.

2015 K900 expected Spring 2014. Initially only available in select markets with limited availability. 2015 K900 V8 prototype shown with optional features. Not all features are available on all trim levels.