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FINANCIAL TIMES

Tuesday May 10 2011

UK £2.00; Channel Islands £2.30; Republic of Ireland €2.50

Modern warfare

Bandwidth trumps artillery. Analysis, Page 11

Beware hyperbole about ownership models

Andrew Hill, Page 14

World Business Newspaper

News Briefing

LinkedIn targets $3.3bn valuation after IPO

LinkedIn is aiming for a valuation of up to $3.3bn (£2bn) when the professional social network site launches its initial public offering this month in a move that will realise great paper wealth for its founders and executives. **Page 17; Facebook ads lead, Page 21**

HSBC clarity on pay

HSBC moved towards clearer disclosure on staff bonuses as the bank revealed it had started accounting for deferred pay-outs as soon as they were awarded rather than spreading the impact over a number of years. **Page 17**

Lansley backed on bill

Andrew Lansley has insisted the coalition's NHS reforms are "not about me", amid talk that the health secretary's job and ... are in jeopardy. **Page 2; Editorial Comment, Page 12**

Security shake-up

Lady Neville-Jones has stepped down as security minister at ... "own request", triggering a shake-up that will hand more ... to Theresa May, the home secretary. **Page 4**

Trade chief chosen

...k Baird, a senior Foreign ...ce mandarin, has been ...en to head the UK trade ...otion arm as ministers ...e a more "entrepreneurial" ...gy to boost exports and ...ment. **Page 4**

...ition a year on

... curious feature of the ...on's first year how much ...on goodwill and the ...minister's empathy with ...puty. **Page 3**

...a-US talks begin

...resence of the Chinese ...ry for the first time at ...vel US-China dialogue ...reduce the dangerous ... of misunderstanding and ...lculation", said Hillary ...n, the secretary of state. **...; Letters, Page 12**

...ce deal influence

...t's key role in the peace ... between Hamas and Fatah ... Palestine shows how far ...region has changed. **...e 5; www.ft.com/mideast**

...n alarm on Syria

...e spread of unrest to Syria, ...an's closest Arab friend, is a ...eminder of the dangers of the ...ansformation in the region. **...age 5; Gideon Rachman, Page 13**

BNP Paribas exit

Michel Pébereau is retiring as chairman of BNP Paribas, the bank he transformed over two decades into one of the world's biggest and most profitable. **Page 17, Lex, Page 16**

Overtures to Wall St

Republican leaders in the House of Representatives are stepping up efforts to woo Wall Street and key campaign donors, with visits to New York to allay concerns that they might fail to raise the US debt limit. **Page 6**

Climate change row

A row between government ministers threatens to derail the UK's commitment to tackling climate change, officials and campaigners have warned, and in the US, up to $15,000 billion – more than the US debt – needs to be found over the next 20 years to develop wind, solar and other renewable energy sources to keep global greenhouse gas emissions at bay, a UN report warned. **Pages 4 & 6**

● Bank in £850m provision ● Second-largest UK compensation settlement

RBS loan insurance retreat

By Sharlene Goff and Elaine Moore

Royal Bank of Scotland has belatedly joined its rivals in conceding the cost of years of mis-selling loan insurance, revealing an £850m provision as part of the UK's second-largest customer compensation settlement.

The part-nationalised bank succumbed to mounting pressure on Monday to quantify its compensation bill after the industry dropped a six-month legal dispute over payment protection insurance, which covers loan repayments when borrowers fall ill or lose their jobs.

Barclays had said earlier in the day it would take a £1bn hit for PPI repayments, while HSBC, a smaller provider, set aside £270m.

These followed a larger-than-expected £3.2bn charge taken last week by Lloyds, the UK's biggest PPI provider. RBS had declined to follow Lloyds during its results announcement on May 6, saying it was too early to estimate likely PPI losses.

RBS's disclosure, announced after the markets closed, took total provisions by the four banks to £5.3bn, making PPI the second-biggest compensation payment recorded by the Financial Services Authority.

The banks' capitulation ends a long-running dispute over a product that was aggressively sold to huge numbers of borrowers who either did not know they were buying it or would not be able to claim compensation because, for example, they were self-employed.

Banks will have to write to millions of customers who they think may have been mis-sold PPI, even if they have not filed a complaint. The FSA believes this could unearth a further 2m cases warranting compensation.

The FSA expects banks to honour a large proportion of complaints and estimates that 70-90 per cent will be upheld.

Adam Scorer, head of external affairs at Consumer Focus, called the PPI fiasco "an embarrassment" for high street banks.

"PPI highlights that people find it difficult to understand everyday financial products," he said. "Banks need to offer more consumer-friendly accounts and services which do what they say on the tin."

Banks had opposed the application of new PPI selling rules to past policies, arguing that it set a damaging precedent for other products. Their challenge was undermined by the decision by Lloyds last week to break ranks and announce it would reimburse customers, leaving rivals little room to continue.

The British Bankers' Association said ending the legal process would provide "certainty for customers".

The move was welcomed by consumer organisations as an important victory for the borrowers who took out PPI alongside mortgages, credit cards and loans. They also predicted that it would trigger a culture shift in the industry. "PPI epitomised the worst of the banking sector," said James Daley at advocacy group Which? "This lays the ground for them to change."

As well as the 2m new claims still expected from customers who have been mis-sold PPI in the past, the FSA estimates banks will pay out on a further 750,000 future policies.

About 16m PPI policies have been taken out and banks have already made significant payouts. RBS said it had refunded £100m and made a provision for a further £100m.

The Financial Ombudsman Service, which has been receiving 5,000 PPI cases a week in recent months, has upheld 200,000 claims at a total cost of £550m to banks.

Customers in line for compensation should be refunded their total premiums plus interest – typically 8 per cent per year – and possible goodwill payments.

Lex, Page 16
Lombard, Page 18
www.ft.com/bankingpodcast

Making provisions

	Lloyds	Barclays	RBS	HSBC
Provision	£3.2bn	£1bn	£850m	£270m
Market share	35–40%	10–15%	10–15%	8%

Mis-sold

Personal pensions
Up to 1m people incorrectly advised in the late 80s and early 90s. Pay-out: £11bn

Mortgage endowments
Tens of thousands have received compensation payments. Pay-out: £2.7bn

Split-capital trusts
About 50,000 small investors lost £700m. A £144m compensation fund was set up in 2005

Default fears spur fresh credit rating cut for Greece

By Richard Milne and Tracy Alloway in London and Ralph Atkins in Frankfurt

Standard & Poor's has cut Greece's credit rating by two notches, warning that any voluntary debt restructuring would amount to a default.

The US rating agency said that any demands from the eurozone's biggest countries for Athens to extend the debt payment maturities on its bail-out loans from a year ago would probably lead to similar demands on private creditors. "Such private-sector burden sharing would likely constitute a distressed exchange . . . for which we assign a rating of selective default," S&P said.

The downgrade to B, six notches into junk territory, comes after European politicians acknowledged publicly that Greece's €110bn (£96bn) rescue package was insufficient.

On Monday the European Central Bank became the latest institution to throw its weight behind revamped assistance.

But the ECB, European Commission and some eurozone governments continue to oppose a debt restructuring. The ECB also does not see an extension of maturities – referred to as a debt re-profiling by some politicians – as feasible or effective.

Investors are confused by the terms used by eurozone policymakers to describe restructuring. Eurozone ministers at the weekend excluded restructuring. But some German and Greek officials have floated the idea of a "voluntary restructuring" involving an extension of maturities, called a "debt re-profiling" by some. Such a move would see bondholders paid back but at a later date, something S&P says would amount to a selective default.

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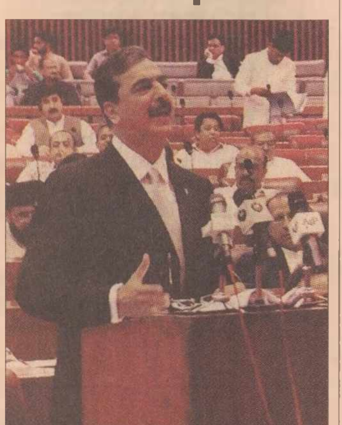
Bin Laden probe



Pakistan's civilian leadership has used last week's killing of Osama bin Laden by US forces to assert its authority over the military, which has ruled the country for most of its history. Premier Yusuf Raza Gilani (pictured) ordered army chiefs to explain to parliament the intelligence and military failures surrounding the US raid on bin Laden's hideout in Abbottabad, close to a military academy.

Report, Page 8

Twitter user account lays down challenge to super-injunctions

Limitations of British privacy laws exposed

By Tim Bradshaw, Digital Media Correspondent

Twitter, the social networking site, has challenged British gagging orders by directing traffic to one of its users who has been posting allegations about celebrities' private lives.

The UK media has been unable to name the offending account for fear of breaking a series of so-called super-injunctions brought by public figures. These court rulings have been ignored by the anonymous Twitter user.

The Twitter account detailed six cases of actors, television presenters, a chef and a footballer in an apparent effort to undermine the orders. Twitter's official press relations account linked to a string of 140-character posts containing the allegations and left them intact.

The messages have exposed the limitations of Britain's notoriously tough privacy laws and reopened the debate about how local laws can be enforced on a global internet.

At least 30 such injunctions are thought to have been granted by the High Court enabling the rich and famous to protect their private lives.

Twitter has vociferously supported free speech online, particularly in countries such as Iran and Egypt where governments have tried to repress internet dissidents. This year, the company resisted a US legal attempt to clamp down on accounts related to WikiLeaks, the whistleblowing website that leaked confidential US diplomatic cables.

It said on Monday: "We don't comment on individual accounts. In keeping with our policy, we review reports that acc[oun]ts violate Twitter's rules & ToS [terms of service]."

Those rules include commitments, to which all users of the site must agree, to protect people's "private and confidential information".

"You may not use our service for any unlawful purposes or for promotion of illegal activities," the rules state.

The account's number of followers at least doubled to more than 50,000 during the day, with the case dominating discussion on the site in the UK.

Twitter did not say whether it had received requests to remove tweets breaking the super-injunction from lawyers representing the parties named.

In January, Biz Stone, cofounder of Twitter, wrote on the company blog that "freedom of expression is essential".

Post fuels debate, Page 4

World Markets

STOCK MARKETS

	May 9	prev	%chg
S&P 500	1346.29	1340.2	+0.45
Nasdaq Comp	2843.25	2827.56	+0.55
Dow Jones Ind	12684.68	12638.74	+0.36
FTSEurofirst 300	1140.23	1144.91	-0.41
Euro Stoxx 50	2902.4	2952.9	-1.71
FTSE 100	5942.69	5976.77	-0.57
FTSE All-Share UK	3094.14	3109.63	-0.50
CAC 40	4007.26	4058.01	-1.25
Xetra Dax	7410.52	7492.25	-1.09
Nikkei	9794.38	9859.2	-0.66
Hang Seng	23336.0	23159.14	+0.76
FTSE All World $	228.83	229.73	-0.39

CURRENCIES

	May 9	prev		May 9	prev
$ per €	1.427	1.451	€ per $	0.701	0.689
$ per £	1.630	1.642	£ per $	0.614	0.609
£ per €	0.875	0.883	€ per £	1.143	1.132
¥ per $	80.7	80.6	¥ per €	115.2	116.9
¥ per £	131.6	132.4	£ index	79.7	79.5
$ index	77.4	76.7	€ index	96.68	97.83
SFr per €	1.251	1.268	SFr per £	1.429	1.436

COMMODITIES

	May 9	prev	chg
Oil WTI $ Jun	102.55	97.18	5.37
Oil Brent $ Jun	115.90	109.13	6.77
Gold $	1,506.50	1,491.00	15.50

INTEREST RATES

	price	yield	chg
US Gov 10 yr	104.02	3.14	-0.01
UK Gov 10 yr	103.07	3.36	-0.03
Ger Gov 10 yr	101.25	3.10	-0.04
Jpn Gov 10 yr	101.39	1.14	0.01
US Gov 30 yr	107.48	4.30	0.01
Ger Gov 2 yr	99.64	1.70	-0.02
	May 9	**prev**	**chg**
Fed Funds Eff	0.09	0.09	-
US 3m Bills	0.01	0.02	-0.01
Euro Libor 3m	1.38	1.37	0.01
UK 3m	0.72	0.72	-

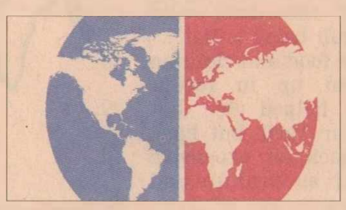
Prices are latest for edition

Inside today

State of the UK Economy

Part 3: growth plans driven by exports

Separate section



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Berlin plays down Greek debt rethink

Tensions rise over extra aid for Athens

Political debate rages in parliament

By Quentin Peel in Berlin

The German government has played down the prospect of debt rescheduling for Greece, insisting that the onus was on Athens to fulfil the conditions of its existing bail-out programme.

Officials in Berlin refused to spell out what actions they might consider in order to provide further relief to Athens – hit by a further credit downgrade on Monday by Standard & Poor's – until they see the conclusions of a progress report on the programme.

An increasingly stormy political debate is raging in parliament and the media on eurozone rescue plans.

Wolfgang Schäuble, finance minister, was last night due to address leading parliamentary spokesmen for the ruling Christian Democratic Union and Free Democratic party, its junior partner in power, as Greece's financial plight threatened to aggravate divisions over the future of the eurozone. Today he will address the full CDU parliamentary group in a bid to reassure backbenchers.

Opponents of further assistance to indebted nations have been vocal in demanding restructuring of Greek government borrowing before any further assistance can be given.

Senior parliamentarians from the CDU, the party of Chancellor Angela Merkel, and some influential economists nonetheless hold out the prospect of measures to improve the conditions for loans to Athens, in return for further Greek measures to reduce the country's massive debt burden.

The German government itself will not take any decisions on further measures until it sees the progress report on the present austerity programme from the International Monetary Fund, the European Commission and the European Central Bank, according to a spokesman in Berlin. Officials from all three institutions are in Athens preparing the report.

Martin Kotthaus, finance ministry spokesman, said there was "no discussion at the moment" about measures to improve Greece's conditions. He also said restructuring was "not on the agenda. All discussion [about it] is speculation".

Steffen Seibert, government spokesman, also rejected any suggestion that a Greek exit from the eurozone had been or was being discussed in any way. "You have heard the denials from all possible sides – especially from the Greeks," he said. "You should take these denials seriously."

German officials are at pains to stress the disadvantages of a debt restructuring because of its complexity, the danger of contagion within the monetary union and the likely consequences for the Greek economy and the wider European banking system.

The concern in government circles is that the backlash could grow if Greece is not seen to make greater efforts to keep to the debt-reduction measures in its austerity programme – and offer further concessions in exchange for any additional support.

Michael Meister, a deputy chairman of the CDU in the Bundestag, and financial spokesman, said on Monday that if Greece wanted to pay a reduced rate of interest on its loans from the eurozone it must take further action to reduce the risk of lending.

If Greece were to reduce the risk of lending, he said in an interview on German radio, "then its partners in the eurozone could consider whether to provide further interest rate reductions or consider the question of extending the term of their loans. So the question is: what can Greece do to reduce the risk?"

Germany enjoys surge in demand for goods

German exports have surged above their pre-crisis level to set a record after rising more than 7 per cent in March, according to official figures, **writes Ralph Atkins in Frankfurt.**

The rapid pace of export growth highlighted the strength of Europe's largest economy at the start of the year. Data on Friday would show that German gross domestic product grew 1 per cent or more in the first quarter compared with the previous three months, economists said.

German exports totalled €98.3bn in March, almost 16 per cent higher than the same month in 2010, according to the federal statistics office. That was the highest monthly total since the data started to be compiled in 1950, exceeding the €88.8bn in April 2008 – before the collapse of Lehman Brothers that year. After seasonal adjustment, exports in March were 7.3 per cent higher than in February.

The pace of export growth might not last long, however. Industrial orders fell 4 per cent in March, data showed last week.

€98.3bn

Total value of exports in March, a 16% rise

In full: www.ft.com/europe

Athens in line of fire over inability to hit targets

Rescue plans

European Union insists promised reforms must be implemented, write Kerin Hope and Peter Spiegel

Greece last week took the unusual step of appointing a high-profile public prosecutor, renowned for unmasking a deadly leftwing terrorist group 10 years ago, to lead a fresh crackdown on tax evasion.

The choice of Ioannis Diotis to head the revamped financial police force signals a tough new approach, according to the finance ministry, which has tasked the new tax police chief with raising at least €15bn ($21.5bn) each year from tax dodgers over four years.

But the move suggests to some analysts that hope has once again triumphed over experience.

The revamp of Athens' €110bn financial rescue package proposed at the weekend, barely a year after it was agreed, points to the country's stubborn problems with implementing the bail-out conditions set by the European Union and the International Monetary Fund.

Persistent monthly revenue shortfalls, together with delays to public spending cuts and a privatisation plan, have prevented Greece from achieving reform targets.

Now it is seeking fresh loans to tide it over until the implementation of a new programme, due to be approved this month by the EU and IMF, which aims to cut the budget deficit from 10.5 per cent to less than 3 per cent of gross domestic product by 2015 – two years later than originally planned.

George Papaconstantinou, finance minister, came under pressure on Friday at an unscheduled meeting of eurozone finance ministers to work harder at implementing his €50bn privatisation programme, drawn up in February, along with the tax evasion crackdown and structural reforms.

A senior European official involved in the meeting said: "The key issue was really to make clear to Papaconstantinou that Greece must deliver on privatisation and structural reforms . . . The Europeans want sufficient guarantees that the privatisation programme will succeed."

The finance ministry has outlined a list of disposals, including equity stakes in state-controlled utilities, concessions to operate regional ports and airports, and leases for development of state-owned land. A detailed timetable of sales will be included in the updated reform programme, together with revenue targets of €15bn by 2013 and the remainder by 2015.

But the privatisation plan faces legal and administrative obstacles, such as those that have derailed past attempts to lease state land for tourism, as well as strong opposition from public sector trade unions.

George Papandreou, the prime minister, pledged at the weekend that the state would retain control of 51 per cent of Public Power Corp, the electricity utility, following a strike threat by its union.

Public sector unions have also managed to slow reforms agreed with the EU and IMF on cutting costs and improving efficiency, with planned mergers and closures of several hundred state organisations on hold. Unions plan another general strike on Wednesday.

European officials believe a successful privatisation programme – which would bring in more than 20 per cent of GDP in new cash by 2015 – coupled with extra financial help could yet overcome fears over allocating Greece fresh funds.

Athens is seeking about €30bn to fund its debt in 2012 as the EU-IMF loan is wound down, and another €30bn-€35bn in 2013 if it is still unable to resume borrowing on international markets.

"The clock is ticking as to when Greece will run out of cash," said Sony Kapoor, managing director of Re-Define, an economic consultancy. "The EU will need to choose between two difficult and contentious options – more EU money or a restructuring of outstanding debt."

The senior European official warned a debt restructuring could be disastrous for Greek banks, which hold about €50bn in government bonds. "The ECB is vehemently against this and the Commission is also emphasising the risks of a chain reaction," the official said: "People don't see how messy and risky it can be. The domestic banking sector would melt down."

Protesters march against budget cuts in Athens on May 1. Unions plan another general strike on Wednesday AFP

When the money is coming

2010 Greek bail-out (€bn)

Total: €110bn

Source: FT research

More at www.ft.com

- **Lex video** Is Greece one step closer to a restructuring? **www.ft.com/lexvideo**
- **Graphic** Bank exposure and eurozone risk, updated with fourth quarter 2010 data **www.ft.com/bankexposure**
- **Markets** Greek rating cut **www.ft.com/alphaville**

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Italy warned on era of 'sluggish growth'

OECD report

By Rachel Sanderson in Milan

Italy will see only "rather sluggish" growth coming out of its worst recession in 60 years and requires structural reform and a strong fiscal framework to improve its outlook, according to the Organisation for Economic Co-operation and Development.

In a report published on Monday, the OECD said that while Italy's economy had emerged from the deep downturn triggered by the crisis and seemed set for a gradual recovery, the strength of growth was uncertain.

"Italian gross domestic product will not return to its pre-crisis level bef[ore] 2013-14," the OECD said. [It] would be wise to plan for no more than the rather sluggish growth seen in the decade before the crisis," when Italy grew by around 1 per cent on average.

The report urges Italy to raise productivity, cut its debt and stimulate labour supply to improve growth – as the OECD did in its last report two years ago.

Italy's recession was deeper than in much of the EU. The economy shrank by almost 6 per cent between the first quarter of 2008 and the final three months of 2011 – the fourth-biggest decline for a eurozone country – the OECD said.

Italy aims to reduce its budget shortfall to below 3 per cent of gross domestic product by 2012-13 from 4.6 per cent now. Public debt rose last year to nearly 120 per cent of GDP.

The report warned core components of the deficit reduction plan, such as a public sector wage freeze, cuts in transfers to the regions and reduced tax evasion, were "uncertain" and further cuts in spending and action on taxation could need to be considered.

Nonetheless, it said two decades of pension reforms had made a contribution to long-term sustainability.

Italy needed to complete liberalisation of its services and extend liberalisation to transport and local services, it added. Public administration also required greater reform and transparency.

In a press conference with Angel Gurría, OECD secretary-general, Giulio Tremonti, Italy's economy minister, said he considered that Italy had nonetheless "passed the exam". The difficulties Italy faced, such as reduction of the public deficit, were shared among Europe's biggest economies, he said.

Italy's government last week passed a plan to [cut] bureaucracy and offer [tax] breaks to companies that invest in research as it attempts to spur growth.

Parties battle over labour cost cuts

Portugal

By Peter Wise in Lisbon

A big cut in labour costs required as part of Portugal's €78bn bail-out package has become one of the most disputed issues in the country's election campaign.

[T]he centre-right Social [De]mocrats (PSD), the main opposition party, has embraced the measure to make companies more competitive by cutting their social security contributions as part of their manifesto for the June 5 vote.

But the Socialists of José Sócrates, caretaker prime minister, question how the reduction will be financed, estimating it would imply a 3 percentage point rise in the main value added tax rate to 26 per cent.

Although both parties have voiced support for the rescue package agreed last week with the European Union and the International Monetary Fund, the election dispute has exposed differences over how the three-year programme should be implemented.

The bail-out package envisages a "fiscal devaluation" – cutting corporate social security contributions by the equivalent of 3-4 per cent of gross domestic product over the next four years.

"This is a potential game changer," said Poul Thomsen, head of the IMF negotiating team. "It replicates a currency devaluation by significantly reducing the labour costs of enterprises in one go."

Eduardo Catroga, expected to become finance minister if the PSD won the election, said the party proposed to lower employers' contributions by 4 percentage points in four years to less than 19 per cent of workers' wages.

● Finland could back the EU bail-out for Portugal this week, in spite of last month's breakthrough by a populist eurosceptic party. Finnish officials told the FT they were hopeful that parliament's grand committee would authorise the deal as soon as Wednesday.

More reports at www.ft.com/europe

THE LEX COLUMN

Tuesday May 10 2011

UK banks and PPI

Choose your battles. António Horta-Osório queered the pitch for his high street rivals last week by providing £3.2bn to compensate customers for mis-sold payment protection insurance. And by withdrawing from an industry-led legal wrangle over PPI, Lloyds Banking Group's chief executive has forced competitors to eat humble pie. Barclays on Monday set aside £1bn for PPI cases; HSBC provided $440m. Royal Bank of Scotland has earmarked £850m.

Mr Horta-Osório's move will mark him out as a splittist in the cosy coterie of the British banking community. But Lloyds was the most aggressive seller of PPI, with a market share of about 40 per cent. Faced with a protracted battle with regulators and consumers as he attempts to put Lloyds back on the front foot, he chose the bigger battle of fixing the bank.

Where is this debacle headed? Provisions announced so far make the Financial Services Authority's initial £4.5bn estimate of the cost to the industry look unrealistic. If Lloyds' provision is a guide, the hit is closer to £8bn. Taking into account the £100m already provided, RBS almost matches Barclays £1bn. Nor might that be the end of it. Berenberg Bank recalls how "big bath" provisions became a regular feature of Lloyds' accounts after the UK pension mis-selling crisis.

The charges are small in the scheme of bank profits – Lloyds' whopper amounts to a fifth of last year's pre-provision profit. Even so, and although banks may play down PPI as a lesser skirmish than the regulatory battles ahead, such as Basel III reforms, forced asset sales and the Independent Commission on Banking, they should be clear that it was a test of shareholders' patience. That is one battle UK banks cannot afford to lose.

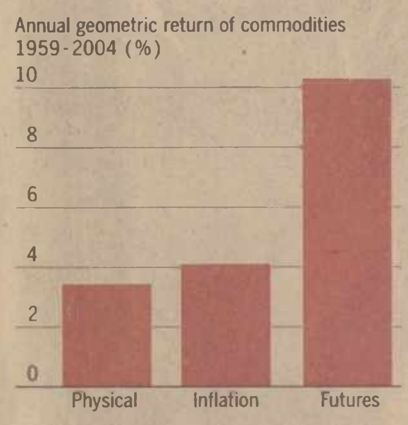
You've been contango'd

Commodity investing can be all things to all people – and that is its problem. Last week's incredible volatility in commodities markets is a reminder of what happens when even sound ideas are undermined by their very popularity.

History shows that a long-term investment in physical commodities is likely to deliver only a puny nominal return. But academics, many of them hired as consultants in the past decade by the likes of commodity index-providers Goldman Sachs and AIG, convinced portfolio managers that commodity futures are quite different. The argument was that they offered two additional legs of return: interest on collateral, and a positive "roll yield" – the profit that can be made from selling futures contracts at expiry and using the returns to buy the next contract if its term structure is backwardated or downward-sloping.

Even better, modern portfolio theory showed that the low correlation of commodities with bonds and stocks allowed investors to generate the same return with less risk. A widely cited paper by Gary Gorton and Geert Rouwenhorst showed annualised returns of 10.3 per cent from 1959 to 2004.

Pit bulls



Sources: Thomson Reuters Datastream; Yale ICF

Proponents claimed not to be making a directional bet on prices, but so many new investors poured into commodities that, by 2008, prices surged and both the roll yield and the benefits of diversification had vanished. Then prices collapsed.

But the commodities trade was reborn after the crisis with two different and not mutually exclusive rationales – a hedge against fiat currencies losing value, and a bet on emerging market growth. The fact that the first investing wave ended in hefty losses and that the current one suffered a significant hiccup last week does not mean that the theories behind them are wrong. They just got too crowded, too quickly.

The finance professors are now back in their ivory towers, slaving away at their drawing boards. Whatever they cook up next may be equally convincing. Just watch out if it becomes too convincing.

TV advertising

Something is wrong in the opaque world of advertising. Media buyers say companies are spending less on television ads in Europe than the industry expected, with Germany looking particularly weak. Some broadcasters have mentioned deteriorating ad revenue growth in March. Investors are paying attention: shares in free-to-air broadcasters such as Germany's ProSieben, France's TF1, Spain's Telecinco and the UK's ITV have fallen by between 15 and 35 per cent in the past three months.

This is not a canary in Europe's economic coal mine. Rather, it is a signal that the advertising market is finally reconnecting with the broader economy. Last year, ad spending in Europe grew about 5 per cent – more than double that of gross domestic product – as the market bungeed out of recession. Investors expected a similar feat in 2011, cheered by the general sense of market momentum.

The optimism did not make sense. In a normal year, ad spending tends to grow at a slightly slower rate than GDP. This year the International Monetary Fund expects Europe's GDP to grow by 2 per cent. And there are reasons to think this year will be worse than normal: consumer goods companies and retailers might well cut ad spending to protect their bottom lines as commodity prices rise. Meanwhile, television ads are nowhere near as cheap as they were a year ago.

Free-to-air broadcasters have had a great ride: ProSieben's share price, for example, rose from €1 to €25 in a year and a half. But investors are right to react quickly to murmurs of a changing market, even though the information is volatile and informal. Thanks to their high operational gearing, these companies are like the little girl with the curl: when they are good they are very, very good, and when they are bad they are horrid.

Greece

Monday was groundhog day in the eurozone. A year after the European Union and the International Monetary Fund unveiled a €110bn rescue package for Greece, the country is again at the top of the crisis agenda. The bail-out has not eased Greece's economic problems while exacerbating its indebtedness problem; the country's re-entry to the debt markets as a sovereign borrower early next year, envisaged in the bail-out plan, looks impossible. The eurozone had a choice at an emergency weekend meeting. It could expand the bail-out or allow Athens to restructure. It chose the first option. The second cannot be avoided for much longer.

A Greek restructuring is not only inevitable, it is essential. To avoid having to restructure, Athens would have to implement even more comprehensive structural and social reforms than those that have already caused civil unrest, as well as a frankly unrealistic pledge to privatise €50bn of state assets by 2015. Greece needs to execute these measures if it is to exit its crippling crisis eventually, but they should not be done in fire sale circumstances.

The issue for policymakers in Brussels, Frankfurt and Athens is one of timing. Deutsche Bank puts the likelihood of a credit event (default or restructuring) in Greece at 46 per cent within two years and 72 per cent within five, based on sovereign credit ratings, credit default swap spreads, and a 40 per cent recovery rate. (For Ireland, the likelihood is 24 per cent and 44 per cent, and for Portugal it is 22 per cent and 43 per cent.)

Athens needs to refinance at least €25bn next year; it will almost certainly need more funding to do so, which it would probably need even alongside a debt restructuring. But Greece is going to have to restructure. The eurozone needs to be prepared for when it does.

BNP Paribas

Michel Pébereau's retirement as chairman of BNP Paribas and his expected replacement by Baudouin Prot, chief executive, is a sign that the bank has found its post-crisis equilibrium.

It also suggests that France's biggest bank by assets has become more progressive. Until 2003 Mr Pébereau was both chairman and chief executive. Although Mr Prot's move into the top slot will raise eyebrows among investors who prefer their chairmen independent, others will welcome the continuity.

Messrs Pébereau and Prot have been a formidable double act. The former, well connected in government and corporate circles, let the latter concentrate on the business of running the bank. That combination has seen BNP Paribas's shares return 102 per cent – 40 percentage points more than the Euronext CAC financials index – over the past decade. The technocratic Mr Prot is less prone to hang out with the Elysée crowd. Seen another way, however, he and his likely successor, current deputy chief executive Jean-Laurent Bonnafé, will take over a well-balanced universal bank. In the first quarter,

BNP Paribas's retail banking and wealth and asset management areas accounted for 57 per cent of the pre-tax profit of its operating divisions, with investment banking making up the rest.

Mr Pébereau, whose career spanned a lively earlier period of consolidation in French banking (he led Crédit Commercial de France, and the pre-merger BNP), may regret that he never consummated a mooted merger with Société Générale.

In retrospect, that is just as well, given its arch rival's derivatives travails. BNP Paribas did, however, acquire Fortis's banking operations in Belgium and Luxembourg, which have helped transform the French group into Europe's most profitable bank. Given the increasingly tough and unpredictable environment in which European banks operate, that is not a bad legacy.

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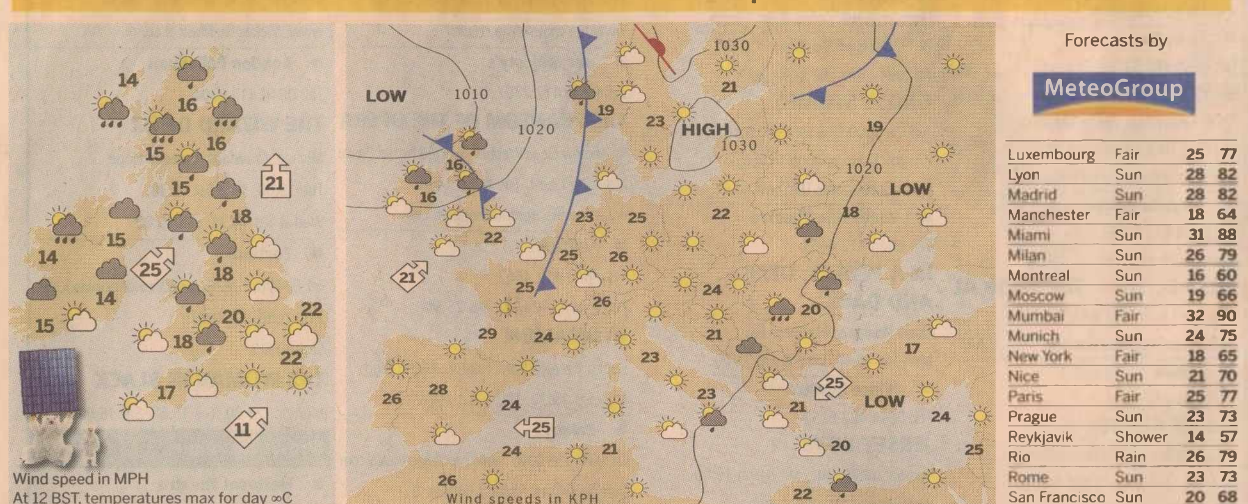
WEATHER



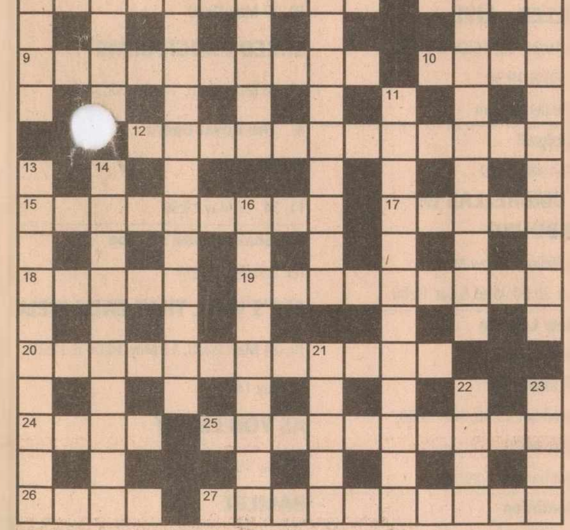
Forecasts by MeteoGroup

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

Abu Dhabi	Sun	40	104
Amsterdam	Fair	21	70
Athens	Sun	21	70
B'ham	Fair	20	68
Bangkok	Thunder	33	91
Barcelona	Sun	21	70
Beijing	Sun	26	79
Belfast	Cloudy	16	61
Belgrade	Sun	22	72
Berlin	Sun	26	79
Brussels	Fair	22	72
Budapest	Sun	24	75
Buenos Aires	Sun	21	70
Cardiff	Fair	18	64
Chicago	Shower	25	76
Cologne	Fair	25	77
Copenhagen	Sun	19	66
Delhi	Sun	42	108
Dubai	Sun	39	102
Dublin	Cloudy	16	61
Edinburgh	Shower	15	59
Frankfurt	Sun	26	79
Geneva	Sun	25	77
Glasgow	Shower	15	59
Hamburg	Sun	26	79
Helsinki	Sun	21	70
Hong Kong	Fair	30	86
Istanbul	Sun	15	59
Jersey	Sun	16	61
Lisbon	Sun	29	84
London	Fair	22	72
Los Angeles	Sun	20	68
Luxembourg	Fair	25	77
Lyon	Sun	28	82
Madrid	Sun	28	82
Manchester	Fair	18	64
Miami	Sun	31	88
Milan	Sun	26	79
Montreal	Sun	16	60
Moscow	Sun	19	66
Mumbai	Fair	32	90
Munich	Sun	24	75
New York	Fair	18	65
Nice	Sun	21	70
Paris	Fair	25	77
Prague	Sun	23	73
Reykjavik	Shower	14	57
Rio	Rain	26	79
Rome	Sun	23	73
San Francisco	Sun	20	68
Stockholm	Sun	23	73
Strasbourg	Fair	28	82
Sydney	Sun	17	63
Tokyo	Thunder	27	81
Toronto	Cloudy	14	57
Vancouver	Cloudy	15	60
Vienna	Sun	23	73
Warsaw	Sun	23	73
Washington	Sun	22	72
Zurich	Sun	26	79

CROSSWORD

No. 13,689 Set by HAMILTON



JOTTER PAD

ACROSS

1 Bet it gets cold in the water, so be nonchalant (4,2,4)
6 Oath taken by renegade (4)
9 Flatter with sophisticated conversation (6-4)
10 Thrill to a song and dance (4)
12 Unhappily, Bush relented to look for unfair advantage (4,3,5)
15 Graphic representation of logarithms omits fifty (9)
17 Philosopher not given to complaining (5)
18 Was an engineer first support for Rolling Stones drummer? (5)
19 Want to get in team colours to suit (9)
20 It can take you to the point of no return (3-3,6)
24 Search customers looking for *War and Peace*, say (4)
25 Somehow niece collared animal, 'e added with excitement (10)
26 Exasperate with endless stream of energy (4)
27 Printed page of directions to landlord (10)

DOWN

1 Flowers were said to be affected (4)
2 Prophet initiating a morning of study (4)
3 Uncomfortable position for atheist on the move? (2,3,3,4)
4 Called for detectives to take note (5)
5 The last person on earth to admit to his failings? (4,5)
7 Like Nato, go prepared to see and take part (3,1,4-2)
8 Mysterious group holding servicemen have something to hide (4,6)
11 Complete the race, but do it unacceptably badly (5,3,4)
13 Exhibitionist from the musical *Queen* (10)
14 Hearst limo engineered to keep at constant temperature (10)
16 Respected salesman with superior furniture (9)
21 Destroys blades that have lost their edge (5)
22 Something that bites back something that bites! (4)
23 He forecasts it will be dry, though changeable at the close (4)

Solution to Saturday's prize puzzle on Saturday May 21
Solution to yesterday's prize puzzle on Monday May 23
Crossword winners' names will be published in Weekend FT.

Markets & Investing

Bill Miller INSIGHT

Now is a good time to snap up healthcare and tech stocks

The most surprising thing about the market this year is not that the S&P 500 had its best first quarter since 1998. It is that only two of the S&P sectors outperformed the broader index in the first quarter: energy and industrials. The last time this happened was in the first quarter of 2000, as the tech bubble was peaking. While the US stock market was strong in the first quarter of 2011, it was also quite narrow, not usually a healthy sign, especially when the leaders have by and large led the market for the past 10 years.

Professor Daniel Kahneman, who won the Nobel in 2002 for his work in Prospect Theory, visited our research team recently. He chose to talk about new work in cognitive psychology, specifically work on how the subconscious affects behaviour.

He said that while we live in a conscious world, much of our behaviour is automatic and driven by the subconscious. Psychologists call the subconscious System 1 and conscious behaviour System 2. System 1 is more or less automatic and System 2 involves attention, time, logic and analysis.

There is a price at which demand destruction will begin, and which will then reverse the price of oil. It might even have started

The work he described has implications for how markets function. If one is a contrarian value investor, one's portfolio is a function of System 2. The time horizon is years. The market, though, is a real-time information processing mechanism and is almost entirely governed by System 1: a piece of news comes out and the market reacts almost instantaneously.

Last week's sharp drop in the price of oil demonstrates how long oil markets have been governed by System 1. With the exception of last week's sharp correction, it has been bullish for oil. If the dollar weakens, oil goes up, because oil is denominated in dollars and a weaker dollar leads to higher oil prices. If the US economy slows, that is bullish for oil, because it means the Fed will continue to pump liquidity into the economy and excess liquidity means higher oil prices. If the US economy strengthens, that is bullish, because it means more demand for oil. Emerging markets growth is bullish for oil, since it means more demand. Low per capita use of oil, such as in China, is bullish, since it is bound to go higher. High per capita use is bullish, because it means lots of demand.

The reaction of oil and other commodities to news flow is a largely automatic response to the market's dominant theme, the dollar debasement trade, which we refer to as DDT. Just as that chemical was highly effective in the short run but poisonous over time, so too with the economic version.

There is, however, a price at which demand destruction will begin, and which will then reverse the price of oil. No one knows what that price is, but it is a lot closer with Brent crude, up 50 per cent since early November. This trend may have even started last week.

Where is the value in the market today? In the assets people do not want, that have no momentum, and are cheap

According to data compiled by Barry Bannister, equity analyst with Stifel Nicolaus, commodity returns relative to stock returns are at 200-year highs on a rolling 10-year basis. One thing is clear about long-term commodity returns: they are cyclical.

The nature of commodity cycles is that when prices are at lows, people believe they will go lower, and when they are at highs, people believe they will go higher. For the cycle to end, prices have to have been high enough for long enough to convince everyone that this time is different.

Have prices reached a level that fully reflects the concerns about supply and that may begin to destroy demand? I don't know. What I do know is that there is a lot of price in these assets, a lot of momentum, a lot of belief, and not, in my opinion, a lot of value.

Where is the value in the market today? In the assets people do not want, that have no momentum, and that are cheap. Three broad sectors and two broad themes stand out. The S&P 500 sectors are; financials, technology, and healthcare which are in the bottom decile of their historical valuation ranges. This means they have been more expensive 90 per cent of the time over the past 60 years or so. The themes are US mega cap, and deep value, meaning low price to book value and high free cash flow yield.

We began the year quite bullish on US equities. The Federal Reserve was providing ample liquidity, core inflation was subdued, interest rates were low, earnings growing, corporate balance sheets strong and valuations undemanding at about a 20 per cent discount to our assessment of fair value.

The market has been absorbing a lot of DDT without yet succumbing to its noxious long-term effects. From this point on, a lower dollar with concomitant higher oil and commodity prices, is bearish not bullish. We expect the Fed to end QE2 this summer. The System 1 reflexive view that Fed policy means higher commodities and a lower dollar will lose one of its pillars.

We believe now is a good time to buy what's on sale, and a bad time to buy what's been marked up, just as it was in 2000.

Bill Miller is chief investment officer of Legg Mason Capital Management

Greek default swaps hit record high

'Peripheral' bond yields also jump

Portuguese banks increase borrowing

By Ralph Atkins in Frankfurt, Peter Wise in Lisbon and David Oakley in London

The cost of insuring against a Greek debt default soared to a record high on Monday as investors worried about the prospect of a forced restructuring.

Yields on bonds issued by some "peripheral" eurozone nations, including those of Greece, Ireland, Portugal and Spain, also jumped.

Five-year Greek credit default swaps saw their biggest daily rise since the peak of the country's debt crisis in May last year, surging by 122 basis points to 1,459bp, according to Bloomberg.

Greek 10-year bond yields jumped 22bp to 15.72 per cent. Irish 10-year yields saw a similar rise to 10.57 per cent, while Portuguese 10-year yields leapt 11bp to 9.66 per cent.

"Worries about a debt restructuring have sent the cost to insure Greek debt to record highs. There is a lot of nervousness around Greece and events of the weekend – despite officials' comments to the contrary – suggest a forced default may be more likely," said Don Smith, Icap economist.

It also emerged that Portuguese banks sharply increased their borrowing from the European Central Bank in April, highlighting their growing dependence on emergency liquidity.

According to central bank figures released on Monday, ECB funding to Portuguese lenders totalled €48bn at the end of April, an increase of almost 23 per cent on the previous month and the highest level since a €49.1bn peak last August.

The increase reflected the growing difficulty banks faced in raising liquidity as the government was forced to request a bail-out last month and Portugal's sovereign debt ratings suffered successive downgrades.

Portuguese lenders have been virtually frozen out of international capital markets for more than a year because of the debt crisis.

The ECB said on Monday it had made no eurozone government bond purchases for the sixth week in a row, confirming its bond-buying programme had been suspended, a year after launch, despite Greece threatening renewed turbulence.

The ECB announced in May last year it would start buying bonds in response to the then escalating eurozone debt crisis. Together with an agreement by European politicians for a €750bn eurozone rescue plan, the programme helped avert disaster for the continent's monetary union.

Some €76bn has been spent under the programme. But yields on bonds of peripheral countries worst-hit by the crisis have risen substantially over the past year.

The ECB insisted its programme was not US Federal Reserve-style "quantitative easing" to boost the economy but aimed at ensuring the proper functioning of markets. But it still ran into opposition in Germany, where Axel Weber, then Bundesbank president, voiced opposition, citing the risk to inflation of blurring fiscal and monetary policy.

The winding down of the scheme will have been greeted with relief by at least a few ECB council members, some of whom have not revealed their opposition. But Frank Engels, economist at Barclays Capital in Frankfurt, said: "From the point of view of markets, the ECB has not suffered any reputational loss. If anything, it has been criticised for not doing enough."

Currency club back to square one on Athens

News analysis

As the country's woes undermine the euro, **David Oakley** looks at the shape of a possible debt restructuring

Exactly one year since the €750bn international rescue package was launched to save the eurozone, the currency union has found itself back at square one as Greece's debt problems continue to undermine monetary union.

Yet, whereas the immediate danger 12 months ago was that Athens would run out of money, today's concerns are about the more subtle, technical issues of whether Greece could be allowed to default and, if so, what shape a restructuring should take.

It is a problem that has hung over the markets for months, because there is no easy solution. As one European policymaker says: "Nobody [apart from Germany] wants restructuring. But neither can anyone see an alternative."

The debate has reached a critical point in the past week as rising yields on Greek debt have cut the country's options. Its bailout package runs out of money next year, just as Greece was supposed to be making its return to the bond markets. This return looks extremely unlikely.

This realisation spurred European Union policymakers to finally admit they need to find more money for Athens. Greece needs an extra €30bn in 2012, on top of the existing €110bn loan programme, and a similar sum in 2013, according to Evolution Securities.

So far, however, policymakers, both at the European Central Bank and in the European Commission, insist default or restructuring is not an option while they consider more international loans. Financial markets think otherwise.

Gary Jenkins, head of fixed income at Evolution Securities, says: "It is going to be a challenge for the international community to claim Greek debt is on a sustainable path without restructuring."

For the markets, the debate has moved on to the timing of a restructuring and whether it should be voluntary or forced.

A forced default, which would lead to haircuts on the €262bn of outstanding Greek bonds, would hit the Greek banking system hard and would land the ECB with losses, some strategists warn.

Such a forced restructuring could hit sentiment not just in Greece but in the rest of the eurozone and lead to other defaults in the corporate and banking world, with those institutions holding Athens' debt put under particular strain.

For this reason, most investors say Athens needs more time, with most forecasting 2013 as the most likely date for any coerced default. This fits with the official line from the EU and the Greek government, both of which show no sign of wanting to go for an early restructuring.

A voluntary restructuring, on the other hand, could happen sooner and could involve less pain for investors, with many strategists saying there is a strong argument for extending the maturity of existing debt to limit the exposure of the rest of the region to Athens.

Such a scenario would not represent a credit event, if managed well, and should avoid significant disruption. That is, it would not trigger pay-outs on credit default swaps that could lead to problems for institutions liable for these pay-outs. But arguments against a voluntary restructuring are that it is unlikely to reduce Greece's public loans and would most likely kick the problem down the road, relying on Athens to find growth. For any debt extension to buy meaningful time, strategists say the debt would probably need to be extended by 15-20 years, a period many investors might resist.

One fund manager says: "Investors need an incentive to go for a voluntary restructuring. Being left with Greek debt for another 15 or so years is not that appealing."

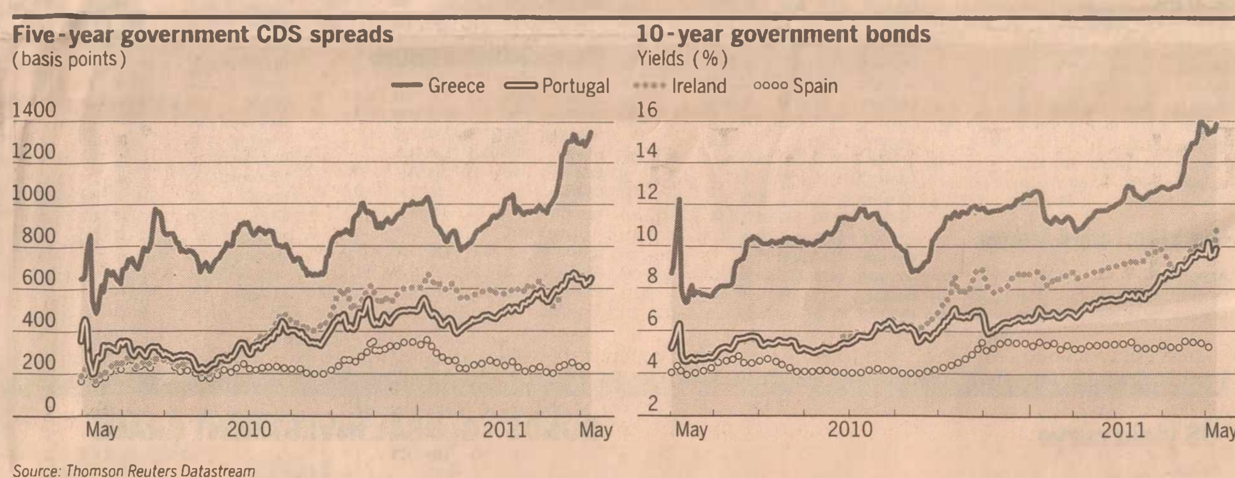
In past restructurings, coupon payments have been increased to compensate for the extension of maturities. But this would put more pressure on Greece.

While the debate over Greece continues, the dangers of contagion remain, with attention focused on Spain, the eurozone's fourth-largest economy, and whether it will be sucked into the crisis.

Ralf Preusser, head of European rates at BofA Merrill Lynch, says: "Greece is a problem for the eurozone because it can cause problems for the bigger countries that really matter. Greece will remain a problem until the restructuring debate is resolved."

Additional reporting by Richard Milne

Protesters in action during May Day protests. Rising yields on Greece's debt have reduced the country's options EPA



Source: Thomson Reuters Datastream

Oil and silver lead way in rebound from heavy losses

COMMODITIES

By Jack Farchy in London

Oil and silver led a strong rebound in commodities as investors piled back into the markets following last week's sharp falls.

ICE June Brent crude closed at $115.90, rising $6.77 from Friday in the second largest one-day gain in absolute terms.

Silver, which led last week's commodities sell-off with a 30 per cent drop, was up 12.4 per cent from its low on Friday at $37.35 a troy ounce.

But investors who were stung by Thursday's 4.9 per cent drop in commodities prices, the sharpest since the financial crisis, would be wary about recommitting immediately, said analysts, and were likely to be more selective in their bets.

David Wilson, metals analyst at Société Générale, said a combination of nerves over global growth and tightness in physical markets would pull sentiment in different directions.

"We're likely to see more corrections and rebounds," he said.

Many investors and analysts were surprised by the speed and scale of last week's correction.

Some of the top investors in commodity markets, such as Clive Capital, the largest commodity hedge fund, and Astenbeck Capital, run by star trader Andrew Hall, suffered heavy losses, according to investors.

However, many remain upbeat about the prospects for commodity markets.

In a letter to investors on Friday, Clive Capital said it remained bullish on fundamentals, particularly in energy markets.

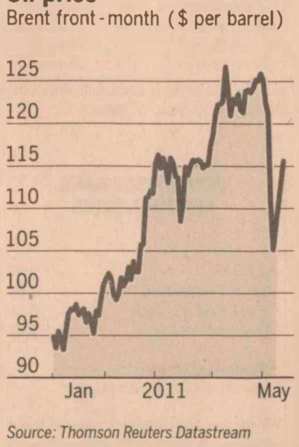
"Physical markets are quite strong," the hedge fund said.

Last week's punishing drop in commodity prices had no obvious trigger, and analysts said fundamentals for many markets remained strong.

Hussein Allidina, head of commodities research at Morgan Stanley, said: "Despite the exodus of extended speculative positioning, fundamentals continue to point to higher prices [for oil]."

Prices of commodities from oil to industrial metals tumbled but the structure of the futures markets for commodities continued to indicate strong fundamentals, said analysts.

For example, Brent crude for immediate delivery was trading at a premium of more than $2.50 to December-delivery Brent – a condition known as "backwardation" that is usually indicative of a tight market.



Source: Thomson Reuters Datastream

Commodity prices, Page 29
www.ft.com/commodities

US equity volumes tumble after Citigroup reverse split

By Telis Demos in New York

US equity markets saw the first of what is expected to be a sharp decline in daily trading volumes following a reverse split for Citigroup, by far the most heavily traded company stock.

For the session, 5.8bn shares traded hands on US exchanges, according to Bloomberg figures. It was the second slowest day of the year, behind only April 25, Easter Monday.

Citi shares opened the day with only one-tenth of the number of shares outstanding on Friday, after it completed a reverse split with a one-for-10 exchange of its 29bn shares, leaving 2.9bn outstanding.

That puts it more in line with Dow Industrial Average groups, which have an average of 2.6bn shares outstanding.

Only 49m Citigroup shares traded on Monday, compared with a 10-day average of 340m shares. On a split adjusted basis, it was an above-average day, however.

Its shares closed at $44.16 on Monday, a drop of 2.3 per cent on the day. Citi closed last week at $4.52 a share ahead of the split.

Citi shares have become a pillar of US trading volumes in recent years. It has been the top-traded stock on almost all days, primarily by retail traders and high-speed professional traders. Its collapse in price after the financial crisis accompanied a huge increase in the number of shares as it raised capital from the US government and other groups.

> The effect of the Citigroup split is expected to be sharp on US share trading volumes

On some trading days in the past three years Citi shares made up as much as 10 per cent of US volume. It was averaging 6.1 per cent of daily US volume in 2011, according to Rosenblatt Securities, an agency brokerage.

The effect of the split is expected to be sharp on US share trading volumes. Rosenblatt said that average daily US volumes could drop 5 per cent after the split.

The study by Rosenblatt estimated that Citi volumes would likely decline on average by 90 per cent. It also said US options volumes could be lower. Since 2009, Citi options were frequently 2 per cent of US monthly volume.

Patrick O'Shaughnessy, equity analyst at Raymond James, cautioned that trading seasonally begins to slow at this point as well. "We think the trading volume environment will weaken over the next few quarters," he said.

However, the shares may become more volatile, said Buff Pelz Dormeier, an independent market analyst. "The smaller float should allow the stock to move easier," he said.

The fall-off in volumes may not be as sharp initially, as institutions buy more of the shares. But retail investors may be turned off, seeing the split as a "public acknowledgement of contracting. This is typically the psychological effect of a reverse split."