BPM Report # 142

BUSINESS AND POLITICS IN THE MUSLIM WORLD

Weekly Report on General Economic and Business Developments in the World

Period: Oct 17 – 23, 2010

Submitted By: Muhammad Ibrahim

Presentation: October 27, 2010

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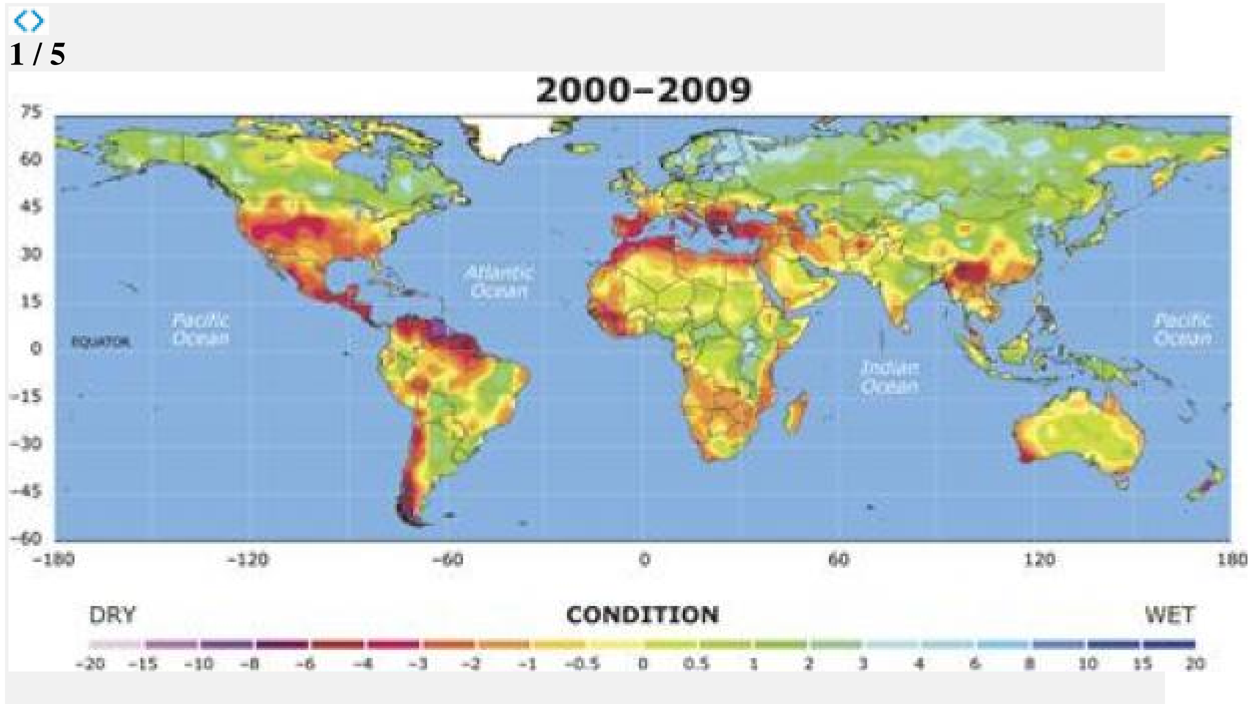
Drought could hit world's populous areas: study
Tuesday, Oct 19, 2010



WASHINGTON: Some of the world's most populous areas -- southern Europe, northern Africa, the western U.S. and much of Latin America -- could face severe, even unprecedented drought by 2100, researchers said Tuesday.
Increasing drought has long been forecast as a consequence of climate change, but a new study from the U.S. National Center for Atmospheric Research projects serious impact by the 2030s. Impacts by century's end could go beyond anything in the historical record, the study suggests.

To get an idea of how severe the drought might get, scientists use a measure called the Palmer Drought Severity Index, or PDSI. A positive score is wet, a negative score is dry and a score of zero is neither overly wet nor dry.

As an example, the most severe drought in recent history, in the Sahel region of western Africa in the 1970s, had a PDSI of -3 or -4.

By contrast, the new study indicates some areas with high populations could see drought in the -15 or -20 range by the end of the century.

"Historical PDSI for the last 60 years show a drying trend over southern Europe but nothing like those values at the end of this century," study author Aiguo Dai said in answer to e-mailed questions. "Decadal mean values of PDSI have not reached -15 to -20 levels in the past in any records over the world."

Areas likely to experience significant drying include:

-- the western two-thirds of the United States;

-- much of Latin America, especially large parts of Mexico and Brazil;

-- regions bordering the Mediterranean Sea;

-- large parts of southwest Asia;

-- southeast Asia, including China and neighboring countries, and

-- most of Africa and Australia.

While Earth is expected to get dryer overall, some areas will see a lowering of the drought risk. These include:

-- much of northern Europe;

-- Russia;

-- Canada;

-- Alaska, and

-- some areas of the Southern Hemisphere.

That doesn't necessarily mean that agriculture will migrate from the drought areas to these places in the high latitudes, Dai wrote.

"The high-latitude land areas will experience large changes in terms of warmer temperatures and more precipitation, and thus may indeed become more habitable than today," he wrote. "However, limited sunshine, short growing season, and very cold nighttime temperature will still prevent farming over most of these high-latitude regions."

The study's findings are based on computer models and the best current predictions of climate-warming greenhouse gas emissions. This could change depending on actual greenhouse emissions in the future as well as natural climate cycles such as El Nino, the center said in a statement.

http://www.reuters.com/article/idUSTRE69I3MD20101019

Bangladesh, India most at risk from climate change

Tuesday, Oct 19, 2010
OSLO: Bangladesh and India are the countries most vulnerable to climate change, according to an index on Wednesday that rates the Nordic region least at risk.
British consultancy Maplecroft said its rankings showed that several "big economies of the future" in Asia were among those facing the biggest risks from global warming in the next 30 years as were large parts of Africa.

It said poverty and large low-lying coastal regions prone to floods and cyclones were among factors making Bangladesh the most exposed country. India, in second place, was vulnerable because of pressures from a rising population of 1.1 billion.

Madagascar was in third place, followed by Nepal, Mozambique, the Philippines, Haiti, Afghanistan, Zimbabwe and Myanmar. Vietnam, in 13th place and flood-hit Pakistan in 16th were also in the most exposed group.

"Understanding climate vulnerability will help companies make their investments more resilient to unexpected change," wrote Matthew Bunce, principal analyst at Maplecroft, who noted that many Asian countries were attracting large investments.

Norway was bottom of the list of 171 nations, least vulnerable ahead of Finland, Iceland, Ireland, Sweden and Denmark -- all rich north European nations which may initially gain from factors such as longer crop growing seasons.

The ranking combined exposure to extremes such as droughts, cyclones and mudslides, sensitivity to damage tied to poverty, population, internal conflicts and dependence on agriculture, and the capacity of a country to adapt.

The U.N. panel of climate scientists says it is at least 90 percent likely that a build-up of greenhouse gases, mainly from human use of fossil fuels, is responsible for most warming in the past 50 years.

Among major economies, the United States ranked at 129, China 49 and Japan 87. Most European Union nations were low on the list, among less vulnerable countries.

Mexico, which will host annual U.N. climate talks from November 29-December 10 trying to agree building blocks for a U.N. climate deal, was the most vulnerable of rich nations in the Organization for Economic Cooperation and Development at 45.

Fiona Place, an environmental analyst at Maplecroft, told Reuters the ranking could help companies plan and identify markets where new environmental technologies are needed.

She also said it could help when the U.N. negotiations are focusing more on helping developing countries adapt to the impacts of global warming.

Some states were left off the list because of a lack of data, including North Korea, and small island states like the Maldives that are vulnerable to rising sea levels.

http://www.reuters.com/article/idUSTRE69I6LE20101019

U.S. ethanol makers seek renewal of tax breaks
Tuesday, Oct 19, 2010
WASHINGTON: Attacked as subsidy addicts, U.S. ethanol makers may need help from friends in high places, including the White House, to hold on to lucrative tax breaks set to expire at the end of the year. The industry says it is ready to discuss revisions in the incentives, worth $6 billion a year. An amalgam of food-makers, livestock producers, environmentalists and deficit hawks say there is no need for subsidies because bio-fuels are guaranteed by law a share of the motor fuel market.

"The ethanol industry is addicted to subsidies," said Steve Ellis of Taxpayers for Common Sense, a good-government group. "It's time for the decades-old ethanol party to end."

Corn-based ethanol is a Farm Belt favorite, valued as a home-grown fuel that reduces reliance on imported oil and creates jobs and income for rural areas. Rural lawmakers back ethanol as a success story.

The average ethanol plant employs 40-50 people and spends $130 million a year on supplies, wages and transport. With 204 plants nationwide, that amounts to thousands of jobs and billions of dollars in outlays.

The largest ethanol makers are privately owned POET, Archer Daniels Midland Co and Valero Energy Corp.

"Ethanol is an expanding market, unlike some of our traditional customers," said Jon Doggett of the National Corn Growers Association.

In Congress, backers include Democrat Collin Peterson, chairman of the House Agriculture Committee, and Charles Grassley, the Republican leader on the Senate Finance Committee, which oversees tax law.

The farm bloc has influence because rural districts often are a pathway to control of the House. Two-thirds of the most competitive House races are in rural districts this year.

"I think it would be very irresponsible to take away an incentive overnight," Jeff Broin, head of POET, told Reuters in an interview. "We're working hard with the White House (and) dozens of lawmakers to get a solution as soon as possible."

The last chance this year would be the brief congressional session set after the November 2 mid-term elections, when an omnibus tax bill could be a vehicle for ethanol incentives. However, an anti-spending mood has blocked revival of a $1 a gallon bio-diesel credit and could affect ethanol too.

'WORK IN PROGRESS'

Corn growers and ethanol trade groups back a one-year extension of the excise tax credit for ethanol, to be followed by revisions to lower the cost of supports.

The tax credit, now 45 cents a gallon, is the largest of the expiring incentives. Also expiring are the 54-cent tariff on ethanol imports and a 10-cent credit for small producers.

One industry suggestion is to convert the excise tax credit to a producer tax credit at a lower rate. Other changes could include opening the door for corn ethanol to qualify as an advanced bio-fuel, which could more than double its sales; a fund to help pay for so-called blender pumps; and loan guarantees for an ethanol pipeline.

"It is very much a work in progress, but we all agree extending the tax incentive is critical," said a spokesman for one of the groups, the Renewable Fuels Association.

Analyst Divya Reddy of Eurasia Group said in a research note that a one-year extension was more likely early next year than in the fall session. Reddy noted proposals to set the tax credit at 36 cents and create a 25-cent production credit.

Trade groups, already at odds over how to get higher ethanol blends onto the market, split in July when a long-term extension of the tax breaks stalled in Congress.

Growth Energy proposed a phase-out of tax credits if an "open market" for ethanol were created through federal support of blender pumps and production of millions of vehicles that can burn higher blends of the alternative fuel.

The Obama administration "believes in continued financial support for bio-fuels that can help us meet our energy security and environmental goals", White House energy advisor Heather Zichal wrote in an October 8 blog.

She said the White House and the industry were exploring options for reform of subsidies.

In July, a think tank at Iowa State University said ethanol output would fall 7 percent in 2011 if the tax credit and import tariff lapsed. Six percent of plant capacity is now idle, the result of economic slowdown and a 2008-09 shakeout.

Livestock producers, meatpackers and food-makers attacked ethanol after grain prices surged in 2006. Oil refiners joined food-makers and environmentalists to oppose E15, a 15 percent blend of ethanol approved last week for newer cars and trucks.

The National Petrochemical and Refiners Organization said U.S. environmental watchdogs had become "the Ethanol Promotion Agency".

Purdue University agricultural economist Wally Tyner said high grain prices drove up feed costs for livestock producers.

"With corn up more than $2 this summer and one-third of the crop going to ethanol, they will continue to fight ethanol," Tyner said. "Ethanol plants can still make money with high corn prices so long as ethanol keeps going up with corn."

http://www.reuters.com/article/idUSTRE69I3WR20101019

Officials hint Fed on the verge of more easing
Tuesday, Oct 19, 2010

WASHINGTON | A string of Federal Reserve officials on Tuesday indicated the central bank will soon offer further monetary stimulus to the economy, with one saying $100 billion a month in bond buys may be appropriate.
While some internal reticence to the unconventional policy was still evident, the consensus view at the Fed sees the economy as weak enough to warrant further support, most likely through increased purchases of Treasury debt.

The U.S. economy is expected to have grown just 1.9 percent in the third quarter, a level considered too low to bring down unemployment. The debt purchases would help lower long-term interest rates in the hope of boosting demand.

Atlanta Fed President Dennis Lockhart's willingness to cite a specific dollar figure for purchases, one largely in tandem with market expectations, was seen as another hint that planning is actively underway.

"If we're going to pursue another round of quantitative easing, it has to be a large enough number to make a difference," Lockhart said in an interview on CNBC television.

"As a monthly number ($100 billion) is fairly consistent with what we did before, and so I think it would certainly be in the range of numbers one might consider ... but if you were talking about $100 billion as simply the overall program, I think that's too small," he said.

Two especially dovish speeches, from the Chicago Fed's Charles Evans and New York Fed chief William Dudley, suggested some officials would like to consider explicitly raising the Fed's inflation target for a time, a controversial proposal.

Dudley said both inflation and employment are likely to remain below levels that are consistent with the Fed's mandate.

"Viewed through the lens of the Federal Reserve's dual mandate -- the pursuit of the highest level of employment consistent with price stability, the current situation is wholly unsatisfactory," Dudley said, repeating an argument he made earlier this month.

The reassurances about forthcoming stimulus were not enough to soothe U.S. stocks, which were down sharply on the day after an interest rate hike in China sparked concerns about the outlook for global growth.

VERBAL DISSENT

The view that further stimulus was needed appeared to hold sway at the central bank, but was not unanimously held. Dallas Fed President Richard Fisher said that while the economy is barely growing fast enough to create new jobs, the case for further monetary easing has not been made conclusively. "The efficacy of further accommodation using non-conventional policies is not all that clear," he said in comments prepared for delivery to the New York Association for Business Economics.

His counterpart at the Minneapolis Fed, Narayana Kocherlakota, also appeared skeptical about how much stimulus further bond purchases or quantitative easing could provide.

"My own guess is that further uses of QE would have a more muted effect on Treasury term premia," because markets are functioning much better now than in early 2009, said Kocherlakota, who will rotate into a voting seat on the Fed's policy-making committee next year.

On the other end of the spectrum, the Chicago Fed's Evans not only backed more easing but repeated his call for a price-level target, a bolder move than inflation targeting, saying that there was little chance the U.S. unemployment rate, now at 9.6 percent, would fall below 8 percent by 2012.

Dudley is a permanent voter on the Fed's policy-setting panel, while Evans moves into a voting slot next year. Lockhart won't have a vote on monetary policy until 2012.

The prospect of further Fed easing, which helped push the dollar to a 10-month low, has drawn the ire of emerging market economies contending with a flood of capital as investors chase higher yields. The dollar surged on Tuesday after the surprise Chinese central bank interest rate increase.

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Geithner vows U.S. will not devalue dollar

Tuesday, Oct 19, 2010

Calif./WASHINGTON | Treasury Secretary Timothy Geithner vowed on Monday that the United States would not devalue the dollar for export advantage, saying no country could weaken its currency to gain economic health.

"It is not going to happen in this country." Geithner told Silicon Valley business leaders of devaluing the dollar.

Geithner broke his silence on the dollar's protracted slide ahead of this weekend's meeting of finance leaders from the Group of 20 wealthy and emerging nations in South Korea, where rising tensions over Chinese and U.S. currency valuations are expected to take center stage.

"It is very important for people to understand that the United States of America and no country around the world can devalue its way to prosperity, to (be) competitive," Geithner added. "It is not a viable, feasible strategy and we will not engage in it."

Answering audience questions before the Commonwealth Club of California in Palo Alto, he said the United States needed to "work hard to preserve confidence in the strong dollar."

Geithner, normally reluctant to publicly discuss currency and market movements, has not uttered the so-called "strong dollar mantra" -- a refrain he helped create at Treasury in the 1990s -- since February.

On Friday, the dollar index hit a 10-month low against a basket of major currencies, while the greenback has been plumbing fresh 15-year lows against Japan's yen .

Many emerging market countries are complaining that Fed money creation is weakening the dollar, and causing more funds to flow into their markets, pushing up their currencies.

Talk of a "currency war" has persisted as countries take action to keep from losing export competitiveness.

Brazil on Monday moved to cool a strong rally in its currency by raising taxes for foreigners buying local bonds and trading in foreign exchange derivatives.

Finance Minister Guido Mantega said the move was aimed at reducing foreign investment into Brazil, and he urged other countries to take coordinated action against the weak dollar.

Argentina's Minister of Economy and Public Finance Amado Boudou on Monday called on developed nations to focus on creating jobs rather than actions that weaken their currencies, saying a "true currency war" was underway.

U.S. POINTS TO CHINA

The G20 finance ministers and central bank governors at the meetings in Gyeongju, South Korea are expected to tackle head-on the disparities in currency policies that are distorting capital flows in the hopes of achieving a more coordinated approach.

But U.S. officials have put most of the blame on China's highly restrictive exchange rate regime, which until recently had kept the yuan largely pegged to the dollar. The United States is pressuring China to allow the value of its yuan to rise to take some pressure off capital flows and to rebalance its economy away from exports.

On Friday, however, Geithner delayed a report about whether the yuan's value is being manipulated, saying instead that he wants to work through the G20 process to hash out a multilateral solution.

Geithner said in Palo Alto that he believes China will continue to lift the value of its yuan currency to aid the rebalancing of its economy away from exports and toward domestic growth.

Asked how much higher China should allow the yuan to rise, Geithner said: "Higher."

"You can't know how far it should go. What you know now is that it's significantly undervalued which I think they acknowledge and it's better for them, and of course very important for us, that it move. And I think it's going to continue to move," Geithner said.

However, his remarks did not square with an official Chinese state newspaper that reported the accelerated pace of yuan appreciation in recent weeks will not last long because China's trade surplus will soon peak.

Beijing has allowed its currency to rise about 2.8 percent since ending a 23-month peg to the dollar in June, with most of that rise coming since August.

Geithner said the delay in the report was an acknowledgment of the faster pace of yuan appreciation and we'd like to see that sustained."

At the G20 meetings in Gyeongju and a November leaders summit in Seoul, Geithner said he wanted to "maximize the chance that we can mobilize broader international support behind a set of improvements to the exchange rate policies of China and other emerging economies.

Asked if the dollar would lose its status as the world's reserve currency, the Treasury chief said, "not in our lifetime."

To do this, Geithner said the United States must maintain growth, but also demonstrate that it can restore budget discipline and improve its long-run fiscal prospects.

http://www.reuters.com/article/idUSTRE69H4VO20101019

World Bank blames U.S. for unruly capital flows

Tuesday, Oct 19, 2010

TOKYO/ PALO ALTO, California | Surging capital inflows threaten Asia's economic stability, the World Bank warned on Tuesday, a day after Treasury Secretary Timothy Geithner sought to draw the venom from a global row over currencies by vowing not to devalue the dollar. The World Bank buttressed the argument made by China and others that U.S. policies are sending a wave of cash flowing into higher-yielding emerging markets, undermining their export competitiveness and pumping up inflation and asset bubbles.

"We are seeing an effort by developing East Asia to deal with the large amounts of liquidity driven in very large part by the monetary policy easing in the United States," Vikram Nehru, the bank's chief economist for Asia-Pacific, told reporters in Tokyo.

Nehru, presenting a semi-annual report, urged policymakers to learn the lessons of the 1997/98 Asian financial crisis, when an influx of footloose global capital inflated property and equity prices, only for them to collapse when the money flows reversed.

"The authorities in East Asia need to take adequate precautions to ensure that they do not repeat the same mistake twice in slightly over a decade," the report said.

While capital controls were not very effective in controlling long-term investment flows, Asian countries had an array of instruments to deal with rising inflows, the World Bank said.

"If this liquidity abundance is sustained and increases, I think they are going have to take further action," Nehru said.

Thailand introduced a withholding tax on foreign purchases of government bonds last week, and Brazil on Monday increased an existing tax on foreign bond buyers to 6 percent from 4 percent.

Foreign investors in Brazil will also have to pay more tax to trade currency derivatives, blamed in part for driving up the real, the country's currency, to a two-year high.

"Our objective is to reduce foreign investment into Brazil," Finance Minister Guido Mantega told reporters in Sao Paulo.

YUAN VS DOLLAR

Strains over the constellation of exchange rates needed to put global growth on a more solid, sustainable footing are likely to dominate a meeting of finance ministers of the Group of 20 major economies in South Korea starting on Friday.

The dispute boils down essentially to the exchange rate of the yuan, also known as the renminbi.

The United States, supported by most economists, believes Beijing is unfairly holding the yuan down to give its exporters an advantage in global markets.

This is causing a broader misalignment of global currencies, Washington contends, because other developing countries are reluctant to lose competitiveness versus China by permitting their own currencies to appreciate in isolation.

Speaking in Palo Alto, California, Geithner said he believed China would continue to let the yuan rise to aid the rebalancing of its economy away from exports and toward domestic growth.

"You can't know how far it should go. What you know now is that it's significantly undervalued, which I think they acknowledge, and it's better for them, and of course very important for us, that it move. And I think it's going to continue to move," Geithner said.

China would endorse that assessment. The disagreement arises over the pace of adjustment.

China says a spike in the yuan would drive many exporters to the wall, destroying millions of jobs, but would do nothing to address what it sees as America's deteriorating competitiveness and shortfall in savings.

"We must try to minimize any possible negative impact in further exchange rate reform," a Chinese central bank spokesman said in remarks reported on Tuesday.

"We must make sure that the currency movements are controllable and avoid any possibility of over-adjustment of the yuan exchange rate driven by market forces," he told the People's Daily, the mouthpiece of the ruling Communist Party.

True to its word, China let the yuan drift slightly lower on Tuesday for the second day in a row following a relatively brisk 2.5 percent rise against the dollar since the end of August.

RETURN OF STRONG DOLLAR MANTRA

China's big fear is that Washington, having largely exhausted fiscal and monetary stimulus, is resorting to benign neglect of the dollar to galvanize its economy as part of President Barack Obama's drive to double U.S. exports within five years. Geithner flatly rejected this charge. "It is very important for people to understand that the United States of America and no country around the world can devalue its way to prosperity, to (be) competitive," he said. "It is not a viable, feasible strategy and we will not engage in it."

But the treasury chief said the United States needed to "work hard to preserve confidence in the strong dollar" -- his first utterance of the mantra "strong dollar" since February -- by maintaining growth and restoring budget discipline.

Geithner said he had delayed a report due last Friday into whether Beijing manipulates the value of the yuan to win time to drum up support within the G20 for "improvements" in the currency policies of China and other emerging economies.

This week's G20 finance ministers' meeting in Gyeongju precedes a summit of the group in Seoul on November 11-12.

Canadian Finance Minister Jim Flaherty said he hoped the meetings would lead to increased currency cooperation. "This is important so that we avoid the kinds of retaliatory actions that nations can take where they feel that they are aggrieved by the policies of particular countries," he told reporters in Ottawa.

Investors are alert to the risk of a descent into tit-for-tat protectionism, but, for now at least, many are confident that policymakers will succeed in averting conflict. "We expect international portfolio flows to continue to create rising tension on asset markets over the next several months, but we do not believe we are as yet at the brink of 'currency wars'," Ray Farris and Kasper Bartholdy, foreign exchange strategists at Credit Suisse in London, said in a note.

http://www.reuters.com/article/idUSTRE69B14B20101019

WTO chief steps into currency row, warns over trade
Tuesday, Oct 19, 2010
GENEVA | The head of the World Trade Organization has stepped into an escalating row over currency policies, saying growing disputes about exchange rates could threaten global trade. WTO Director-General Pascal Lamy said governments had largely resisted resorting to conventional trade measures such as higher tariffs to protect jobs in the wake of the crisis, but friction over exchange rates risked undermining that.
"For the moment it's a risk, but it's a risk that can be dangerous for trade," he told reporters late on Monday.

Lamy has in the past refused to get involved in discussions about currencies, arguing that such matters are primarily the mandate of the International Monetary Fund.

But the comments, following an interview in a British newspaper on Thursday, indicate that the body that polices world trade is getting increasingly concerned about currency policies.

Currency tensions are likely to dominate next month's summit of the G20.

The United States and European Union are calling on China to let its yuan appreciate, China has condemned lax monetary policy in the United States for distorting the global economy, Japan and Switzerland have been selling their currencies to ward off deflation and emerging economies from Thailand to Brazil are seeking to block inflationary capital inflows.

Underlying these disputes, economists say, is the fear that countries will slip into a tit-for-tat round of devaluation to make exports more competitive and preserve jobs.

WTO rules do include an article that requires members not to circumvent trade agreements through exchange rate policy.

But this measure has never been tested in a WTO dispute.

Lamy declined to comment on the bill passed by the U.S. House of Representatives that would allow the U.S. government to treat China's undervalued currency as a subsidy and impose countervailing duties in response.

http://www.reuters.com/article/idUSTRE69I1R520101019

Basel III to ease in new bank liquidity rule
Tuesday, Oct 19, 2010
LONDON | Global banking supervisors agreed on Tuesday to phase in the introduction of a key new global standard on lenders' minimum short-term funding cover, handing further relief to a sector facing a hefty funding gap. The Basel Committee of banking supervisors and central bankers from 27 countries met on Tuesday in South Korea, which is hosting the Group of 20 (G20) leading countries that had called for tougher capital and liquidity requirements in response to the financial crisis.
The committee had already agreed to a soft phase-in for its net stable funding ratio, which covers a bank's longer-term liquidity. That measure will be trialed from 2012 and become mandatory in January 2018.

On Tuesday the committee said it would also adopt a gradual phase-in for its liquidity coverage ratio (LCR), which will require a bank to hold enough highly liquid assets to cover 30 days of net cash outflows. The LCR observation period will start next year and the rule will become a minimum global standard in January 2015. The rules have faced fierce opposition from banks, which say they would struggle to comply, and bankers said that, while a phase-in of the LCR had been expected, they welcomed confirmation of the delay. "The Committee agreed on key details of the liquidity coverage ratio," it said.

"It confirmed that both the LCR and the net stable funding ratio will be subject to an observation period and will include a review clause to address any unintended consequences."

"The liquidity ratio and net stable funding ratio are some of the most difficult areas as international practices differ, " said Pat Newberry, chair of the UK financial services practice at PWC.

"Giving themselves time to look and think carefully has to be a sensible move. If you tighten up liquidity regimes, what does that do to lending volumes? It's much more difficult to forecast than with capital," Newberry said.

The Basel Committee also said it would finalize by year end its proposal on the use of contingent capital, also known as CoCos, bail-in bonds and other non-equity loss-absorbent instruments to pad out a bank's capital requirements.

"Getting clarity by the end of the year will help banks a lot to plan capital positions going forward," Newberry said.

Banking industry officials said that banks in Germany and France would welcome the phasing-in of the new liquidity standards.

Britain's Financial Services Authority has already proposed its own set of liquidity rules and now will come under pressure to align their introduction with the delayed Basel timetable to avoid market distortions.

Industry officials also welcomed the review clause which gives supervisors further wriggle room to delay the new rule if capital raising conditions worsen or other problems emerge.

The liquidity rules are part of a wider Basel III package which G20 leaders are set to endorse in Seoul next month.

The Basel Committee said it will publish a detailed text by year end setting out all the elements of the new capital and liquidity requirements. Financial industry experts said this timetable signaled that Basel III was unlikely to undergo any further major changes.

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Apple CEO hits out at competitors
Steve Jobs makes a rare Wall Street call as his company's stock price falls and iPad production misses predictions.
Tuesday, Oct 19, 2010

Steve Jobs, the CEO of Apple Inc, has lashed out at his company's rivals in a conference call with Wall Street analysts and investors after Apple released an earnings report that marked a rare failure by the consumer electronics company to meet analysts' expectations.

It was the first time Jobs joined such an investor call in two years, and he used the opportunity on Monday to predict increased success for Apple's iPad tablet computer and declare his competitors' smaller tablets "dead on arrival".

Shares of Apple fell six per cent in after-hours trading on Monday night after the company released a quarterly earnings report for the period between June 26 and September 25 that failed to meet Wall Street's predictions for gross margins and iPad production numbers.

Apple sold 4.19 million iPads in that time - the company's fiscal fourth quarter - falling below predictions that it would sell closer to five million. The company's gross margins - the amount of profit gleaned from sales revenue - was 36.9 per cent, slightly less than the expected 38.2 per cent.

But in other areas, Apple's business continued to boom. Days after the company's share price eclipsed $300 for the first time, the company posted a record revenue of $20.34 billion in the latest quarter.

Apple also stated a net profit of $4.31 billion, or $4.64 per share, exceeding most analysts' predictions of earnings between $3.43 and $4.41 per share. The price did fall below the $5.03 per share expected by analysts surveyed by Bloomberg News.

Rosy outlook

On the conference call with investors, Jobs predicted failure for the iPad's smaller rival tablets, manufactured by companies such as Samsung and Dell.

"The current crop of 7-inch tablets are going to be DOA, dead on arrival," Jobs said. "Their manufacturers will learn the painful lesson that their tablets are too small."

The iPad, which was released for the first time in April, features a 9.7-inch touchscreen.

Jobs said there were a "handful of credible" rivals to the iPad but that none could match the iPad's starting price of $499. Some analysts agree, the Reuters news agency reported, predicting that sales will jump when Apple begins offering the tablet in more countries and mass-market outlets such as Wal-Mart next year.

Following the release of Apple's earnings report, industry research group iSuppli increased its estimate for iPad sales in 2010 from 12.9 million to 13.8 million.

Apple has previously faced problems finding an adequate supply of component parts for the iPad, such as LCD panels, leading to delays in shipping the tablet to consumers who have purchased it. But as the company signs deals with new suppliers, iSuppli predicted Apple will sell a stunning 43.7 million iPads in 2011.

Though Apple seems to be dominating the tablet niche, it faces stiff competition in the world of mobile phones,where its operating system is tied to one carrier - AT&T. Google's Android operating system appears on dozens of companies devices, from Sony to Samsung, and is selling better than Apple.

Apple has scheduled a press conference on Wednesday that is widely expected to address the company's laptop computer line and Macintosh operating system, subjects that have "fallen behind" the popular iPhones, iPods and iPads, Dan Moran, a senior associate editor at *MacWorld* magazine, said.

Apple will likely introduce its new Macintosh operating system, Mac OS 10.7, and will probably unveil an update to the slim, ultralight MacBook Air laptop.

http://english.aljazeera.net/business/2010/10/2010101935639194872.html

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China raises interest rates
Move intended to control inflation and rapid growth even as other Asian economies move to keep their recovery on track.
Tuesday, Oct 19, 2010
China has raised its key interest rate for the first time in nearly three years, in a move intended to control inflation and rapid growth.

Tuesday's rate hike, China's first since 2007, reflected Beijing's focus on guiding growth to a more sustainable level rather than revving up the economy. China's economy grew 10.3 per cent in the second quarter.

The People's Bank of China said it was raising benchmark rates by 25 basis points, taking one-year deposit rates to 2.5 per cent and one-year lending rates to 5.56 per cent.

If there was ever any doubt about China's role in driving the stuttering global economic recovery, the impact was felt by markets across the board. Oil and gold prices tumbled, stocks turned negative in Europe and the dollar jumped.

"The interest rate rise is entirely outside of market expectations," Zhu Jiangfang, chief economist at CITIC Securities in Beijing, said.

"The recent rise in headline inflation has put the real rate into negative territory. And I think that's why the central bank needs to raise interest rates in such a hasty way," he said.

Currency war

Some analysts said the rate increase also suggested a deal was in place between China and the US to strengthen the yuan and put an end to worries about a currency war of competitive devaluations ahead of upcoming Group of 20 meetings.

But others said just the opposite was the case – with higher rates, Beijing can afford to rely less on currency appreciation to keep the economy on an even keel.

Finance ministers of the G20 major economies will aim to tackle the currency strains in a meeting in South Korea starting on Friday. The country also hosts a G20 leaders' summit in November.

Although announced by the People's Bank of China, the decision to increase rates would have received approval from the highest echelons of Chinese power, with Wen Jiabao, the Chinese prime minister, likely signing off on it.

Once a consensus has been forged in Beijing to raise or cut rates, past experience shows that moves often come in bunches.

In the view of some, it is about time for China to embark on a more aggressive tightening cycle.

To date, it has relied on lending restrictions and banks' reserve requirements to keep growth from boiling over.

"Fundamentally, policy rates are just too low for an economy that's growing around 10 per cent. To avoid bigger distortions, China needs to start moving rates to more appropriate levels," Rob Subbaraman, an economist with Nomura in Hong Kong, said.

"China's economy looks as though it's decoupling from other major economies, and its policies should as well," he said.

Debated but unexpected

A number of leading economists, including some advisers to the central bank, have urged an increase in deposit rates to keep savers' returns in positive territory.

China reported consumer inflation of 3.5 per cent in the year to August and economists expect that the pace climbed to 3.6 per cent in September.

Still, the increase in rates is surprising given that several top leaders have recently expressed confidence that inflation is under control, and have said that higher rates would potentially suck in speculative capital from abroad.

"They did it now likely because Thursday's GDP and CPI data is too strong for them," Dariusz Kowalczyk, senior economist at Credit Agricole CIB in Hong Kong, said.

China is due to report third-quarter GDP and a suite of economic data for September on Thursday.

The consensus forecast is that economic growth slowed to 9.5 per cent year-on-year last quarter, down from 10.3 per cent in the second quarter.

http://english.aljazeera.net/business/2010/10/20101019191822551864.html

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Stocks dip on China interest rise
Asian bourses fall after China announces first interest rate change in three years, in attempt to control overheating.
Wednesday, Oct 20, 2010

Asian shares have fallen after China raised its key interest rate for the first time since 2007.

The drop on Japan's Nikkei averaged 2.2 per cent on Wednesday, as investors fretted that China may be embarking on a policy tightening cycle.

The MSCI index of Asia Pacific stocks outside Japan was down 0.4 per cent by late morning, after trimming some of its losses suffered earlier in the day.

China announced its interest rate rise on Tuesday in a move intended to control inflation and rapid growth.

The move reflected Beijing's focus on guiding growth to a more sustainable level rather than revving up the economy. China's economy grew 10.3 per cent in the second quarter.

'Temporary aberration'

David Buick, from BGC Partners, told Al Jazeera: "I think China is very well known for just in case the world forgets that the government is in charge or not, they tweak it. It is a very modest increase.

"It is still about half what it was 10 years ago. The Chinese economy is in danger of overheating, particularly the property bubble. And I think that the authorities are very keen now to make sure that things do not get out of hand.

"And that does send warning shots across the bow, because it could adversely affect the level and flow of imports and exports and hence stock markets have received the news badly ... I think that we can see this as no more than a temporary aberration."

The People's Bank of China said it was raising benchmark rates by 25 basis points, taking one-year deposit rates to 2.5 per cent and one-year lending rates to 5.56 per cent.

China's economy is expected to drive the stuttering global economic recovery, and the impact of the rate change was felt by markets across the board on Tuesday. Oil and gold prices tumbled, stocks turned negative in Europe and the dollar jumped.

"The interest rate rise is entirely outside of market expectations," Zhu Jiangfang, the chief economist at CITIC Securities in Beijing, said.

"The recent rise in headline inflation has put the real rate into negative territory. And I think that's why the central bank needs to raise interest rates in such a hasty way," he said.

http://english.aljazeera.net/business/2010/10/2010102044313638669.html

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U.N. study highlights price of nature to mankind

Wednesday, Oct 20, 2010

NAGOYA, Japan | Governments and businesses need an overhaul of policies and strategies to respond to the rapid loss of nature's riches, worth trillions of dollars but long taken for granted, a U.N.-backed study said on Wednesday.

Damage to natural capital including forests, wetlands and grasslands is valued at $2-4.5 trillion annually, the United Nations estimates, but the figure is not included in economic data such as GDP, nor in corporate accounts.

That "invisibility" needs to change so steps can be taken to save ecosystems that are a vital source of food, water and income, said Pavan Sukhdev, study leader for The Economics of Ecosystems and Biodiversity (TEEB), a U.N.-backed initiative.

"We can not treat this lightly," he told a news conference on the sidelines of an Oct 18-29 U.N. meeting in Nagoya, Japan, where envoys from nearly 200 countries are aiming to set targets for 2020 to fight losses in biological diversity.

"Unfortunately, the lack of an economic lens to reflect these realities, has meant that we have treated these matters lightly, that they are not center-stage when it comes to policy discussions nor center-stage when it comes to business discussions."

Sukhdev, on secondment from Deutsche Bank, unveiled the final installment of several TEEB reports that analyze the value of nature, including forests that clean the air, bees that pollinate crops and coral reefs that are home to millions of species.

For example, halving deforestation rates by 2030 would cut damage from climate change estimated at more than $3.7 trillion, while Swiss bee colonies ensured yearly agricultural production worth $213 million by providing pollination, the report said.

SAME COIN

Destruction of coral reefs was not only damaging to marine life but also posed risks to communities, the report said. Some 30 million people are reliant on reef-based resources for food production, incomes and livelihoods.

"It has exacerbated the suffering of human beings, especially of those at the bottom of the economic pyramid," Sukhdev said.

"Development and biodiversity cannot be seen as competing choices. They are not only the same coin but they are literally the same side of the same coin."

The report highlighted recommendations for policymakers, such as the need to include the value of nature and the role of ecosystems in national accounts. Businesses must disclose values in their annual reports and accounts, it said.

Emerging economies Brazil and India threw their support behind the U.N. effort, saying they would use the TEEB findings as a guide.

"At a national level we are in discussion to implement a TEEB study of our natural capital, and the Brazilian business sector is also in planning to move toward this practical and sustainable approach to decision-making," Braulio Dias, secretary for biodiversity and forests at Brazil's environment ministry, said in a statement.

Putting a price on the role of nature has been a major focus at the Nagoya talks on biodiversity, an issue that environmental groups say has so far received far less attention from policymakers and the public than climate change.

"The conservation community has a translation problem," said Andrew Deutz, director of international government relations at The Nature Conservancy.

"We've spent decades talking about habitat degradation and species loss. The people who run the world talk in terms of economic growth and employment rates. This report could be our Rosetta Stone."

http://www.reuters.com/article/idUSTRE69E0BF20101020

US confirms $60bn Saudi arms deal
Largest ever US arms sale includes 84 Boeing F-15 fighter jets and more than 100 attack helicopters.
Wednesday, Oct 20, 2010

The United States plans to sell up to $60bn worth of military aircraft to Saudi Arabia, the US state department has announced, the largest US arms sale ever.

Andrew Shapiro, the assistant secretary of state for political-military affairs, told a news conference on Wednesday that the US administration did not anticipate any objections to the sale from Israel, traditionally wary of arms sales to nearby Arab countries.

The sale, which had been expected, includes 84 Boeing F-15 fighter jets and 70 upgrades of existing Saudi F-15s.

It also includes 70 of Boeing's Apache attack helicopters and 36 AH-6M Little Birds, lightweight helicopters often used in special operations.

Under the deal, Saudi Arabia also has the option to buy 72 Black Hawk helicopters built by Sikorsky Aircraft, a unit of United Technologies Corp.

Al Jazeera's John Terrett, reporting from Washington said "the Saudi's are not getting what Israel already has, and that is the F-35, or Joint Strike Fighter, the newest aircraft out there."

"The US congress now has 30 days to block the deal, and if they don't, then formal negotiations about the delivery date will open up."

Shapiro said the total value of the package would not exceed $60bn, although he emphasised that Saudi Arabia may not choose to exercise all of its purchase options during the programme, which will last from 15 to 20 years.

Alexander Vershbow, the assistant secretary of defence for international security affairs, said the US had discussed the matter with Israel, and concluded that it would not undercut Israel's qualitative military edge in the region.

"We have consulted with Israel as this sale has taken shape [...] based on what we've heard at high levels, Israel does not object to this sale," he said.

'Dangerous neighbourhood'

Vershbow and Shapiro both stressed that bolstering Saudi Arabia's own defence capabilities would improve US security in a vital part of the world where fears are growing over Iran's nuclear programme.

"This is not solely about Iran," Shapiro said. "It's about helping the Saudis with their legitimate security needs [...] they live in a dangerous neighbourhood and we are helping them preserve and protect their security."

"The State Department is spinning things very carefully, putting the emphasis on jobs, because this is going to preserve hundreds of thousands of US defense jobs at companies like Boeing and UTC," our correspondent reported from Washington.

Vershbow said the sale would improve Saudi Arabia's ability to co-ordinate with the US on shared security challenges "so it means we may have to station fewer forces on a continuing basis in the region".

US and international concern about Iran's growing military capability includes advances in a nuclear programme the West believes is aimed at developing atomic weapons - accusations Tehran denies.

Washington has also flagged concern about Iran's growing missile capabilities and has been helping Arab states boost their missile defenses.

That includes the expected sale of the THAAD missile defense system manufactured by Lockheed Martin Corp to the United Arab Emirates.

Similar talks are underway with Saudi Arabia.

US officials are also discussing a possible deal to upgrade Saudi Arabia's navy, which one official estimated could be worth an additional $30bn.

http://english.aljazeera.net/news/middleeast/2010/10/20101020173353178622.html

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UK announces 490,000 job cuts
Harshest austerity measures since Second World War unveiled as public spending is slashed to deal with country's debts.
Wednesday, Oct 20, 2010

Britain will cut 490,000 public sector jobs over four years under austerity measures designed to reduce the country's record deficit.

George Osborne, the finance minister, told parliament on Wednesday that the job losses were "unavoidable when the country has run out of money".

"Today is the day that Britain steps back from the brink. It is a hard road but it leads to a better future," he said.

He said he had ordered $130bn in spending cuts by 2015, aiming to reduce Britain's deficit of 11 per cent of gross domestic product (GDP) to around two per cent within five years.

The measures will also hit the welfare state, cutting child benefits and pushing the state pension to 66 by 2020.

The cuts come as figures reveal British public sector spending in September reached $25.5bn - a record high level for the month.

Analysts had initially forecast a slight rise from September 2009's public net borrowing of $24.4bn.

Protests

Small protests against the cuts are already taking place with larger marches and rallies scheduled to take place in London, the capital, later on Wednesday.

Nazanine Moshiri, Al Jazeera's correspondent in London, said demonstrations so far were not matching the scale of anti-austerity protests seen previously in Europe.

"We're not seeing anything like the kind of protests we've seen in the streets of Paris in the last few days.

"People here are looking at this as a way of blaming the previous government of the Labour party for what has happened, rather than blaming the current coalition government."

But she added the move was a "big gamble" for the Conservative-Liberal Democrat alliance.

"If the economy doesn't start to grow, who knows what could happen here," she said.

'Double-dip' risk

Ruth Lea, a British economist, told Al Jazeera that Wednesday's cuts were needed to reduce the deficit.

"If we don't cut now the generations to come will have to pay for all this," she said.

Lea added that the prospect of a "double-dip" recession was unlikely, saying: "Even though we talk about these enormous cuts they only mean one per cent year-on-year," she said.

The International Monetary Fund has strongly backed plans for an aggressive reduction of Britain's record high public deficit, describing spending cuts as an "essential" weapon.

But some economists have warned that the measures will tip Britain back into recession.

Mervyn King, the central bank governor, painted a gloomy picture late on Tuesday, saying it would be a long while before Britain could recover from the 10 per cent drop in output seen in the last recession.

The opposition Labour Party, which the current Conservative-Liberal Democrat coalition government blames for running up Britain's massive debt when it was in power, has agreed there is a need for fiscal discipline.

But it says that the coalition is cutting too much too soon.

Alan Johnson, Labour's shadow finance minister, accused Osborne of "economic masochism", warning that his cuts would leave Britain trapped in a cycle of low growth and high unemployment for years.

Wednesday's measures will see spending cut across government departments, including the Foreign Office, which will lose 24 per cent from its budget, the police force, and the interior and justice departments.

The BBC is also being affected by the measures, with the government cutting funding to the World Service.

The plans are also extending to Britain's Queen Elizabeth II, with royal household spending falling by 14 per cent in 2012 to 2013.

However the National Health Service, schools and overseas aid have been protected under the spending review.
The National Institute of Economic and Social Research think tank has said it believes the government will only be able to push through half the planned cuts.

http://english.aljazeera.net/news/europe/2010/10/2010102011504468626.html

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Toyota recalls 1.5 million cars
Car maker recalls Lexus and Avalon models in Japan and US due to brake fluid and fuel pump problems.
Thursday, Oct 21, 2010

Toyota has recalled 1.53 million vehicles, mostly in the US and Japan, for brake fluid and fuel pump problems, in the latest in a string of problems for the car maker.

Toyota Motor Corp. said on Thursday it is recalling about 740,000 Lexus, Avalon and other models for repairs in the US and 599,000 in Japan, the remainder are in Europe and other markets around the world.

The majority of the vehicles need to be fixed due to a problem with the brake master cylinder, which could lead to braking power getting progressively weaker, Paul Nolasco, Toyota's spokesman in Tokyo, said.

Some models in Japan and elsewhere, although not in North America, also have an electrical problem with the fuel pump, which could lead the engine to stall, he said.

No accidents have been reported from the two defects, Nolasco said.

Mass recalls

The models affected in the US include the 2005 and 2006 Avalon, 2004 to 2006 non-hybrid Highlander and Lexus RX330, and 2006 Lexus GS300, IS250, and IS350 vehicles, the company said in a statement from its US headquarters in California.

The statement said a small amount of the brake fluid could slowly leak from the brake master cylinder, resulting in illumination of the brake warning lamp.

If at this point the brake fluid is not replaced, "the driver will begin to notice a spongy or soft brake pedal feel and braking performance may gradually decline", Toyota USA said.

The models affected in Japan include the Crown, Crown Majesta, Harrier, Mark X, Alphard, Kluger, Lexus GS350, Lexus IS250, and Lexus IS350. The production date of the models ranges from May 2002 to November 2005.

In Japan, two models, the Lexus GS350 and the Crown, are affected by both problems.

'Disaster prevention'

Seijiro Takeshita, from Mizuho International, a London-based securities and investment banking arm of a Japanese group, told Al Jazeera that Toyota was taking a disaster prevention measure by recalling the vehicles.

"This will cause big damage to their reputation," he said.

"They were already trying to claw back [their reputation] ... so this does come at a very bad time.

"The Japanese are usually very poor at crisis management ... Toyota is no exception."

The latest moves by the auto giant come after a series of recalls that affected about 10 million vehicles worldwide in late 2009 and early 2010, undermining Toyota's once stellar reputation.

Toyota came under harsh criticism for being slow to address safety problems. US regulators fined the company $16.4m for failing to promptly tell the government about its car defects.

Since then the manufacturer has seen its US market share shrink by 1.4 points to 15.2 per cent for the first nine months of this year.

Toyota has been working to overhaul its quality controls and respond more aggressively to customer complaints in the fallout from its recall crisis.

http://english.aljazeera.net/business/2010/10/2010102194421991109.html

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G20 summit opens amid currency wars
Reports suggest a deal on tackling economic imbalances will evade ministers as fears over currency devaluations loom.
Friday, Oct 22, 2010

Finance ministers and central bank chiefs from the G20 nations have gathered in South Korea, but reports suggests that a global agreement to tackle economic imbalances and avert the prospect of damaging currency devaluations could evade them.

The G20, comprising 19 industrial and emerging-market countries and the European Union (EU), started formal meetings in the city of Gyeongju on Friday with nations from the developing world and Japan dismissing US proposals to set limits on current account balances.

The move is intended to defuse tensions over currencies that economists fear could trigger trade wars.

"We need to talk about it first, but numerical targets are unrealistic," Yoshihiko Noda, the Japanese finance minister, said.

Many emerging market policymakers are loath to allow their currencies to appreciate substantially and blame the US for financial mismanagement that led to the global financial crisis.

Competitive undervaluation

Policy makers have also accused the US of engaging in its own devaluation by flooding markets with liquidity from its quantitative easing policies, effectively printing dollars to increase the amount in circulation.

That has had the effect of pushing a wall of money into emerging markets like Brazil, forcing them to adopt a range of measures to stem capital flows which have boosted asset prices and complicated fiscal and monetary policy.

A draft statement quoted by Dow Jones Newswires, however, said the ministers will seek a temporary truce in the so-called currency wars and will pledge to "refrain from competitive undervaluation" of their currencies.

The G20 will "move towards [a] more market-determined exchange rate system", the draft said.

Yoon Jeung-Hyun, South Korea's finance minister, told reporters he was "optimistic" about the weekend meeting but did not elaborate.

And Yim Jong-Yong, the country's vice-finance minister, said separately that he believes agreement on forex disputes will be reached at some point.

"China is making its own efforts, for instance by raising interest rates," Yim said.

"They know this fight [on currency] will eventually damage both sides and lead to trade protectionism, so I believe that this issue will reach agreement."

'Lots of complaints'

The United States and European Union accuse China of keeping its yuan grossly undervalued to benefit exporters.

Beijing counters that Washington's loose monetary policy is swamping emerging markets with destabilizing capital inflows, as investors chase higher yields than they can secure from the dollar.

Some delegates said meaningful agreements at the summit were unlikely, aside from a commitment to a development agenda for poorer nations that has been backed by South Korea and a framework for financial regulation.

"One thing is clear the final agreement on this framework agreement [on economic stability] will not be made at the finance ministers' meeting," Andrey Bokarev, a Russian finance official, said ahead of the meetings.

"There is an action plan, but there are an awful lot of complaints, proposals."

Failure to reach an global agreement has already been reflected in the financial markets, although any hardening of the tone of the final communique, due on Saturday, could bolster emerging market currencies at the expense of the dollar.

http://english.aljazeera.net/news/asia-pacific/2010/10/20101022524369577 65.html

U.S. seeks $2 billion in military aid for Pakistan
Friday, Oct 22, 2010
WASHINGTON | The United States announced $2 billion in military aid for Pakistan on Friday as the two countries sought to dispel doubts about Islamabad's commitment to uprooting Islamist insurgents from safe havens on its soil.
"The United States has no stronger partner when it comes to counterterrorism efforts against the extremists who threaten us both than Pakistan," Secretary of State Hillary Clinton said.

The five-year military aid package, which must be approved by Congress, would complement $7.5 billion in civilian assistance already cleared by U.S. lawmakers.

Pakistani Foreign Minister Shah Mehmood Qureshi rejected naysayers who argue that Islamabad's heart is not in the fight against the insurgents.

"Prophets of doom are back in business, painting doomsday scenarios about our alliance," he said. "They are dead wrong."

Announcement of the military assistance, for the years 2012 to 2016, came at the formal opening of the third round of the U.S.-Pakistan Strategic Dialogue, a series of talks to expand relations beyond the fight against Islamist insurgents.

Clinton said 13 working groups focusing on issues from water to energy had agreed on plans to immunize 90 percent of Pakistani schoolchildren, improve electricity supplies and help farming families get back on their feet after devastating floods in August.

But looming over the talks is the nine-year-old war in Afghanistan and the fight against al Qaeda and other Islamist extremist groups along the Afghanistan-Pakistan border that have strained relations between Islamabad and Washington.

The Obama administration has pointedly pressed Pakistan for more aggressive action against safe havens in North Waziristan, saying in a recent report to Congress that Pakistani forces had avoided direct contact with al Qaeda and related militants, in part for political reasons.

CARROTS, STICKS AND APOLOGIES

Stepped up attacks in the region by U.S. drone aircraft have aggravated public opinion in Pakistan and relations deteriorated after a cross-border helicopter incursion killed two Pakistani border guards.

The incident prompted Pakistan to close a border crossing near the Khyber Pass to NATO supply convoys for 10 days until apologies were made by U.S. and NATO officials.

U.S. Defense Secretary Robert Gates apologized again for the incident when he met Pakistani army chief General Ashfaq Kayani earlier this week.

But U.S. officials continue to press Pakistan for more action and express growing concerns about the possibility of an attack on U.S. soil plotted by Pakistan-based groups, similar to the failed bombing in New York's Times Square this year. Clinton told officials at the plenary session of the strategic dialogue on Friday that the two sides had "productive discussions" this week about "our work together to combat terrorism and

eliminate violent extremism and the organizations that promote it that are operating in Pakistan."

"These groups threaten the security first and foremost of the people of Pakistan, of neighbors, of the United States and indeed of the world," Clinton said.

Pakistani officials raised their own concerns, saying increasing violence in disputed Kashmir threatened the stability of the region.

Qureshi urged U.S. President Barack Obama to press India for a solution in Kashmir, a Muslim majority region claimed by Pakistan and India that has been rocked by violent clashes following protests against Indian rule. "President Obama has always understood the importance of a Kashmir solution. His coming visit to the region is the time to begin to redeem the pledge," Qureshi said.

Obama is due to visit India in early November.

http://in.reuters.com/article/idINIndia-52382620101022

G20 seeks to avoid currency war
Finance ministers agree to move towards market-determined exchange rates and avoid competitive currency devaluation.
Saturday, Oct 23, 2010

The world's leading advanced and emerging countries have vowed to avoid potentially debilitating currency devaluations, aiming to quell tensions that experts have warned could threaten the global economic recovery.

The G20 - 19 industrial and emerging nations and the European Union - also agreed to give developing nations more say at the International Monetary Fund (IMF), part of what it described as an ambitious set of proposals to reform the body's governance.

After a two-day meeting in the city of Gyeongju in South Korea, the G20 said that it will "move towards more market determined exchange rate systems" and "refrain from competitive devaluation of currencies'.'

Saturday's agreement comes amid fears that nations were on the verge of a so-called currency war in which they would devalue currencies to gain an export advantage over competitors - causing a rise in protectionism and damaging the already fragile global economy.

"We are all committed to play our part in achieving strong, sustainable and balanced growth in a collaborative and coordinated way," the final communique said.

Distorted growth

The United States and European Union accuse China of keeping its yuan grossly undervalued to benefit exporters.

Beijing counters that Washington's loose monetary policy is swamping emerging markets with destabilising capital inflows, as investors chase higher yields than they can secure from the dollar.

Following the meeting, Timothy Geithner, the US treasury secretary, pressed the emerging economies to allow their currencies to appreciate and raise domestic demand to help rebalance distorted global growth.

Without naming China, he said such countries should move "away from export dependence and towards stronger domestic demand-led growth".

Geithner had also pushed in a letter to G20 members for a commitment to polices that would reduce current account and trade imbalances "below a specified share" of gross domestic product "over the next few years".

The statement said that large imbalances - such as China's vast trade surplus with the rest of the world - would be "assessed against indicative guidelines to be agreed".

'Unrealistic proposal'

The statement however, contained no numerical targets for current account surpluses or deficits. Instead, the group said that persistently large imbalances - to be assessed against indicative guidelines yet to be agreed - would warrant an assessment by the IMF.

Geithner's proposal had drawn resistance from export-reliant countries such as Japan which called it "unrealistic."

The finance ministers also agreed tougher rules for big financial companies blamed for the global economic crisis as they tackled the problem of companies deemed "too big to fail".

"We are committed to take action at the national and international level to raise standards, so that our national authorities implement global standards consistently, in a way that ensures a level playing field and avoids fragmentation of markets, protectionism and regulatory arbitrage," they said in a statement.

The rules, known as Basel III, will raise the minimum capital reserves that banks must hold as insurance against any new financial tumult.

The rules will be phased in over several years starting in 2013. They will be formally adopted by G20 leaders at a summit in Seoul, the South Korean capital, next month.

European governments see US failure to implement the previous bank capital standards, known as Basel II rules, as one cause of the 2008-09 crisis.

Under the Basel III reforms, banks of all sizes will be required to hold more reserves by January 1, 2015, with the "minimum requirement for common equity", the highest form of loss-absorbing capital, raised to 4.5 per cent of overall assets from 2.0 per cent at the moment.

'Periods of stress'

In addition, banks would be required by January 1, 2019 to set aside an additional buffer of 2.5 per cent to "withstand future periods of stress", bringing the total of such core reserves required to 7.0 per cent.

Also approved were recommendations on implementing the central clearing and trade reporting of over-the-counter derivatives - a move intended to reduce risk in the huge derivatives market.

The G20 additionally backed the Financial Stability Board [FSB] watchdog principles for reducing reliance on credit rating agencies, which came in for widespread criticism for being too close to the firms they assessed and for failing to warn of problems.

The group of 20 also agreed to a doubling of IMF quotas, or membership subscriptions, as part of a broader deal to shift more than six percentage points of voting power in the fund to dynamic emerging economies such as India, China, Brazil and Turkey.

Acceding to a longstanding US demand, the G20 also agreed to empower the International Monetary Fund to exercise greater vigilance over its members' economies, to prevent spillovers from skewed patterns of trade.

"The IMF was created to play this role but its ability to do so in practice has been constrained by the reluctance of its members to expose themselves to a candid, independent, external assessment of the effects of their policies on the global economy," Geithner said in a veiled dig at China.

http://english.aljazeera.net/business/2010/10/201010239157408853.html

The world economy and the quest for growth

It may depend on structural reforms as much as prudent macroeconomic policy

LOOK at the world economy as a whole, and you could be forgiven for thinking that the recovery is in pretty decent shape. This IMF has predicted that global GDP should expand by 4.8% this year—slower than in the boom before the financial crisis, but well above the world's underlying speed limit of around 4%. Growth above trend is exactly what you would expect in a rebound from recession.

Yet this respectable average hides a series of problems. Most obviously, there is the gap between the vitality of the big emerging economies, some of which have been sprinting along at close to 10%, and the sluggishness of many rich ones. Macroeconomic policy is also weirdly skewed: many emerging economies are loath to let their currencies rise to reflect their vigour, even as fragile rich ones are embarking on austerity programmes. And finally there is a crucial missing ingredient just about everywhere: "micro" structural reform, without which current growth rates are unlikely to last.

A world out of balance

In the emerging world the macroeconomic errors come from politicians behaving as if growth there were more fragile than it is. The pace has slowed a bit, but from breakneck speed to merely very fast. Most vital signs, from productivity to government debt, are healthy. Yet many policymakers are buying boatloads of dollars to stop their currencies rising as foreign capital pours in from Western investors seeking better returns. And emerging economies, as a group, still save more than they invest, which explains why global imbalances—notably the controversial surplus in China and deficit in America—remain so big. That makes little sense. Poor countries, especially young ones, ought in theory to invest more than they save, and so be a net source of demand for richer, older ones, all the more so when the latter are in bad shape.

In the rich world the danger is the reverse: politicians cutting back on the basis that growth is assured. Big asset busts are usually followed by years of weakness as the over-borrowed repair their balance-sheets. Experience suggests that several years of slow growth lie ahead. Rich countries are planning tax rises and spending cuts worth 1.25% of their collective GDP in 2011, the biggest synchronised fiscal tightening on record. In many places a budgetary squeeze is necessary, but not all; and, taken as a whole, cutting this much this early is a risk.

Even if demand remains strong enough to cope with this onslaught, the rich world's longer-term growth prospects are darkening—as our special report this week makes clear. Europe's working-age population is about to start declining; Japan's is already doing so.

Even in America the ageing of the baby-boomers points to a slower-growing workforce. In theory, faster productivity growth could offset this, but in most rich economies that was waning before the crisis hit—and the crash has clobbered productive potential. A feeble recovery could make matters worse, as the unemployed lose their skills, public debt builds up and firms put off investment.

A gaping growth gap between the emerging and rich worlds will, of course, shift economic heft more quickly towards emerging economies. A fast-growing emerging world is fine, but a stagnating rich one serves nobody—especially if trade tensions start to rise. Western voters may find it intolerable that the likes of China still run big surpluses, thanks in part to those weak currencies. Protectionist rhetoric is already rising in the United States.

All policies great and small

The world would be better served by policies that both improve rich countries' prospects and reorient growth in emerging economies. These should come in two parts. First, as this newspaper has often argued, macroeconomic policies must be recalibrated. Emerging economies need to allow their currencies to rise more. The rich should tread carefully with fiscal consolidation: sensible budget repairs should be less about short-term deficit-slashing and more about lasting fiscal reforms, from raising pension ages to trimming health-care costs.

Second, and just as important, is microeconomic reform. No matter what Congress threatens about the yuan, China's trade surplus will not disappear until it boosts investment in services, removes distortions that depress workers' share of income and encourages households to save less. From telecoms to insurance, China is full of service oligopolies that need to be broken up.

Similar growth tonics need to be applied in much of the rich world, both to boost domestic spending in surplus economies, such as Germany and Japan, and to raise productivity. America is more productive than the euro zone and Japan largely because the latter both have a lousy record in services (too many rules and not enough competition). Many labour markets also need an overhaul, especially in southern Europe, where it is still far too difficult to adjust wages or fire permanent workers. One advantage of the crisis for Spain and Greece is that they have been forced to make a start on this.

The United States also has its own microeconomic to-do list, albeit of a different sort. The most urgent item is the festering mass of underwater mortgages. Almost 25% of homeowners with mortgages owe more than their houses are worth. Faster, more thorough debt restructuring is needed, to make it easier for workers to move to where jobs are more plentiful and to hasten financial recovery. Schemes for unemployment insurance and training also need attention, so that high joblessness does not become entrenched.

None of these structural reforms is easy. Peer pressure could help. Rather than being fixated on harsher budget-deficit rules, the European Union's members should pledge to complete the single market in services, to open up cosy national markets to greater competition. The members of the G20 big economies could commit themselves to specific structural goals, from raising retirement ages to deregulating things like transport. A bold microeconomic agenda will not yield instant rewards. Nor is it a substitute for getting the macroeconomics right. But without it global growth will eventually falter.

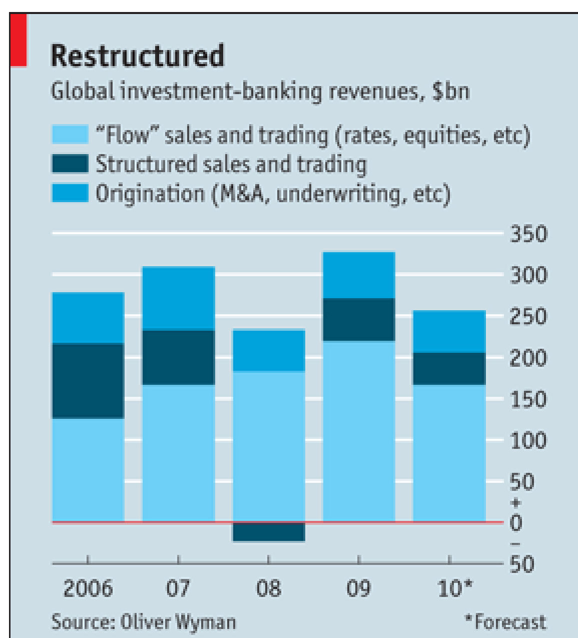
http://www.economist.com/node/17202223

Investment banking: The big squeeze

Why the industry's best days may be behind it

NEW YORK: EVEN by its own notoriously cyclical standards, investment banking has been on a stomach-churning ride in the past five years. After an apparently golden age, with quarter after quarter of record profits, came the bursting of the debt bubble, a deluge of red ink and bail-outs; then, last year, firms bounced back obscenely quickly thanks to record trading profits. Now they are being squeezed once more, and this time the slump may last.

American banking giants' third-quarter results, starting with JPMorgan Chase on October 13th, will show that trading revenues fell by perhaps 20-30% from the previous quarter. With nervy investors sitting on their hands, client activity was "painfully slow across the board", according to Jefferies, a middle-sized bank.



Things are not much better in origination businesses. Several trends that buoyed underwriting last year, such as banks' rush to raise capital and the boom in bond issuance as companies refinanced at low rates, have fizzled. Merger-advisory business has picked up but not by enough to compensate. As one Wall Streeter puts it: "If we extrapolated our third-quarter returns, we'd shoot ourselves." Overall, 2010 will be a year to forget (see chart).

The ugly results will make for difficult decisions on bonuses as the year draws to a close. Firms won't want to lose their "talent": witness Goldman Sachs's unusual mid year payout of restricted shares for partners affected by Britain's bonus tax. But they face growing pressure to cut costs, and 40-50% of their revenues still flow to employees. Chopping people often comes more easily to banks than cutting pay. Bank of America is sacking up to 5% of its capital-markets unit. Others will follow—in a reversal of a hiring spree earlier this year—unless markets improve markedly in the fourth quarter. Meredith Whitney, an analyst with a reputation for prescience, thinks up to 80,000 jobs could go on Wall Street in the next two years.

Capital-markets activity tends to be closely linked with overall economic growth. When output picks up, so will investment banking, argue optimists. But this time could be different because market and regulatory pressures have "substantially weakened" the economics of the business, says Shubh Saumya of the Boston Consulting Group. There is less leverage to supercharge returns. Some previously money-spinning activities are shadows of their former selves. Revenues from selling and trading structured products are almost two-thirds lower than in 2006. New regulations and accounting rules have made securitization less appealing.

The biggest impact will come from the Basel 3 capital requirements, which could be finalised at next month's G20 summit in Seoul. Higher charges, especially for trading, could cause global wholesale banks' risk-weighted assets to balloon by one-fifth on average, reckons Huw van Steenis of Morgan Stanley.

This will force some to reassess their exposure to racy stuff. Even JPMorgan Chase, which boasts of its "fortress" balance-sheet, has said it will cut some investment-banking exposures to counter the effects of Basel 3. In future, numerous trading businesses will no longer be able to beat their cost of capital, says Brad Hintz of Alliance Bernstein, though some of these may still be run as loss-leaders. Firms are seeking out less capital-intensive opportunities in areas like equities and advisory work.

Adding to the pressure on the industry's trading culture is America's Volcker rule, which restricts banks' "proprietary" trading, or punting with their own capital in markets. JPMorgan Chase is shifting 45 prop traders into its asset-management arm, where they can continue to place bets, but only for clients. Morgan Stanley is looking at a possible

spin-off of PDT, its quantitative-trading arm, one hope being that the bank can still make some money from the independent entity if it borrows. Senior folk at Goldman's mighty Principal Strategies group are reportedly in talks with Avenue Capital and other non-banks.

The big firms will still be able to do some gambling. Volcker allows banks to invest up to 3% of their Tier-1 capital in prop trading, hedge funds and private equity. And they can take directional bets by not hedging all of the market making trades they do for clients. Goldman, for instance, went "short volatility" in equities in the second quarter—a decision it came to rue. Overall, however, investment banks will have fewer opportunities to roll the dice.

Banks have not made it easy for themselves. They missed an opportunity to overhaul their operations and pay policies last year, instead preferring to ride the rebound and postpone difficult choices. With regulatory change looming, these must now be faced. Tushar Morzaria, chief financial officer of JPMorgan Chase's investment bank, says all banks have to wrestle with "very fundamental change".

As you would expect from an industry with a history of innovation, good and bad, firms are scurrying around for new opportunities. Bank of America, for instance, wants to expand in the middle market; only 2,000 of its 40,000 middle-sized corporate clients use both its commercial and investment banks. It and many others are throwing money and people at emerging markets. The hottest area of expansion is also, tellingly, the dullest: transaction services. This covers a host of businesses that provide steady income and are not too capital-intensive, such as corporate cash management, foreign exchange, trade finance, global custody and hedge-fund administration. Some banks have moved investment bankers into these less glamorous but more promising areas.

Working out the relative attractiveness of different businesses is not easy because the final shape of regulatory reform is unclear. In derivatives, for instance, the common wisdom is that big dealers will be hurt as trades migrate to central clearing and exchanges. But that will depend on future capital charges for cleared and uncleared assets and the precise structure of trading venues, which are still not known. Dealers could benefit from an increase in trading volume, offsetting tighter margins.

There could be other positive effects. The boss of one European bank thinks the Basel rules will cause borrowers to move away from banks and into bond markets, boosting debt-origination business for some investment banks. Others point to the $1.6 trillion cash pile on which American companies sit. If they start to deploy that in mergers and securities markets, the industry will benefit.

And even if market growth is low, there will be winners, such as the "flow monsters" that have the scale and the systems to handle vast flows of client trades in shares, bonds,

foreign exchange, rates, commodities and more. Perversely, this points to increased concentration. Among those likely to be in the top tier are Goldman, Deutsche, JPMorgan, Barclays and Credit Suisse. The risk is that acute competition in those areas drives down margins. Flow business is “the side of the boat all banks are running towards,” says Ted Moynihan of Oliver Wyman, a consultancy.

The best firms, such as Goldman, used to make returns on equity above 30%. Even the laggards could clock 20% without breaking a sweat. Now the best that most can hope for is the teens, and even that will require chopping and changing. With such a foggy outlook, it is only natural that markets value many investment banks at or below book value. If another golden age is coming, investors can’t see it.

http://www.economist.com/node/17202243

Germany's role in the world: Will Germany now take centre stage?

Its economy is booming, but its strength poses new questions

Thursday, Oct 21 2010

BERLIN: IN FRANCE workers angry about pension reforms have blockaded fuel refineries, causing 4,000 petrol stations to run dry. The Netherlands’ recently elected minority government depends for survival on support from a Muslim-baiting populist. Economies across Europe are struggling to cope with sluggish growth, lacerating budget cuts and the after-effects of borrowing binges. But there is an exception to the gloomy European rule.

No big developed country has come out of the global recession looking stronger than Germany has. The economy minister, Rainer Brüderle, boasts of an “XL upswing”. Exports are booming and unemployment is expected to fall to levels last seen in the early 1990s. The government is a stable, though sometimes fractious, coalition of three mainstream parties. The shrillest protest is aimed at a huge new railway project in Stuttgart. Amid the truculence and turmoil around it, Germany appears an oasis of tranquility.

To many of its friends and neighbours, though, the paragon is a disappointment. Its sharp-elbowed behaviour during the near-collapse of the euro earlier this year heightened concerns about Germany’s role in the world that have been stirring ever since unification 20 years ago. Speeches, seminars and scholarly articles by nervous Germans and Germany-watchers are a booming cottage industry. A recent essay published by Bruegel, a Brussels think-tank, explains “why Germany fell out of love with Europe”. Another, from the European Council on Foreign Relations, alleges that Germany is “going global alone”. Jürgen Habermas, Germany’s most distinguished living philosopher, accuses his country of pursuing an “inward-looking national policy”. “How can you not ask Germany

questions about its vision of the future of Europe?" wonders Jacques Delors, who was president of the European Commission when the Berlin Wall fell. Even a pacific and prosperous Germany causes international angst.

The German question never dies. Instead, like a flu virus, it mutates. On the eve of unification some European leaders worried that it would resume killer form. "We've beaten the Germans twice and now they're back," said Margaret Thatcher, Britain's prime minister. Such fears now look comical. But even today's mild strain causes aches and pains, which afflict different regions in different ways. America's symptoms are mild. Central Europe seems to have acquired immunity. After unification 85% of Poles looked upon Germany as a threat, recalls Eugeniusz Smolar of the Centre for International Relations in Warsaw. Now just a fifth do. It is among Germany's long-standing west and south European partners that the German question feels debilitating, and where a dangerous flare-up still seems a possibility. Germany's answer to the question matters not only to them. It will shape Europe, and therefore the world.

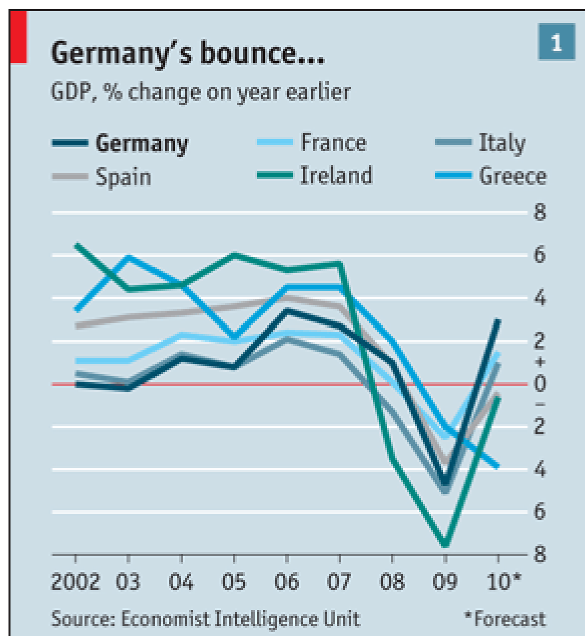
Germans have not forgotten that their country was the author of the horrors of the 1930s and 1940s but, says Renate Kocher of Allensbach, a polling firm, they want to "draw a line under the past". That does not mean ignoring its lessons or neglecting to teach them to the next generation. A new exhibition on "Hitler and the Germans" at the German Historical Museum in Berlin is drawing blockbuster crowds. But Germans are no longer so ready to be put on the moral defensive or to view the Nazi era as the defining episode of their past. Even non-Germans seem willing to move on. Recent books like "Germania" and "The German Genius" suggest that English-language publishing may be entering a post-swastika phase. Germany still atones but now also preaches, usually on the evils of debt, the importance of nurturing industry and the superiority of long-term thinking in enterprise. Others are disposed to listen. "Everyone orients himself towards Germany," says John Kornblum, a former American ambassador.

The worries below

Yet this buoyancy is checked by equally potent anxieties. Germany's bestselling book is "Deutschland schafft sich ab" ("Germany does away with itself"), a warning by a director of the Bundesbank, since forced out of his job, that too much child-bearing by the poor and by immigrants (especially Muslims), and too little by the educated classes, dooms the country to decline. The book's popularity has shaken Germany. Xenophobic parties play little role in politics, but the resentments that feed their popularity elsewhere are just as potent. A third of Germans think the country is overrun by foreigners, according to a newly published poll; a majority favour "sharply restricting" Muslim religious practice. Over a tenth would even welcome a *Führer* who would govern with "a strong hand"—a sign that the embers of extremism still glow.

Conservative politicians, long fearful of being outflanked on the right, are pandering. Horst Seehofer, head of the Christian Social Union, the Bavarian sister party of the ruling Christian Democratic Union (CDU), declared this month that Germany needs no further immigration from Turkey or the Arab world. Germany is "not an immigration country", he insisted, contradicting a hard-won consensus among conservatives. Characteristically, Angela Merkel, the CDU chancellor, sought to placate anti-immigrant sentiment without stooping to populism. Multiculturalism has "absolutely failed", she said on October 16th, implying that immigrants would be expected to integrate better into German society. But she balanced this by admitting that Islam "is part of Germany".

Despite their economic strength, Germans fear the worst. They believe their country "has passed its zenith", says Mrs Kocher, the pollster. This pessimism shapes Germany's dealings with the rest of the world. Unlike most countries, Germany is not driven by any great ambition, but rather by the fear that "things could fall apart if they don't hold on to stability," suggests Mr Kornblum.



This year's euro crisis brought out both the apprehension and the arrogance. With Greece's near default, the promise that the euro would be as stable as the Deutschmark suddenly looked like the lie Germans had always suspected it to be. As the crisis mounted Mrs Merkel delayed giving German backing to the inevitable rescue for wobbly euro countries. A €750 billion ($920 billion) package was eventually agreed on after a hectic weekend of negotiation in May. To Germans, this looked like the start of the dreaded "transfer union", a bottomless commitment to subsidise Greeks' early retirement, fix an Italian budget tattered by tax evasion and clear up after Spain's burst property bubble. "Sell your islands, you bankrupt Greeks. And the Acropolis while you're at it,"

demanded *Bild*, a popular tabloid. Mrs Merkel played to the gallery by suggesting that persistent euro sinners should be thrown out of the group.

These non-European outbursts startled not just Greeks, who brandished swastikas in response, but Europeans generally. They had grown up believing that the Germans saw their own interests as inseparable from those of their fellow Europeans. Now they glimpsed a different, ugly German, smug about his economy and untroubled by his past. Some pundits argue that Germany's brutality to Greece during the second world war should have tempered its irritation with the Greeks.

The crisis has created a new pecking order, at least temporarily. Germany, with its high-competitiveness, low-debt economy, is on top. The rest are having to adjust, including France, traditionally a joint leader of the European project. This is unsettling. "You get an enormous sense of German self-righteousness, which is very difficult to take, especially when there are solid foundations for it," says François Heisbourg of the International Institute for Strategic Studies. France, which has lagged behind Germany in making structural reforms, feels its influence waning. "France has to do its homework to be able to restore some level of influence in Europe," says Jean-Pierre Jouyet, a former French minister for Europe, now head of France's financial regulatory authority.

Whatever became of Gemütlichkeit?

Even during the golden age of European integration Germany was an awkward partner, too big to be first among equals but too small to dominate, as Helmut Kohl, the chancellor who unified Germany, put it. It never lost sight of its own interests. As early as 1960 France and Germany clashed over the founding of Europe's common agricultural policy. France regarded the Deutschmark as an instrument of economic terror, forcing it either to shadow the Bundesbank's monetary policy or to devalue the franc. But long

before the euro arrived in 1999, the German finance minister of the day, Theo Waigel, vowed it would bear "the German hallmark".

Still, the tone changed under Mr Kohl's successor, Gerhard Schröder, who headed a coalition of Social Democrats and Greens from 1998 to 2005. He was unembarrassed to flex Germany's newly acquired muscles and to employ the sort of language heard from leaders of more nakedly nationalistic countries. He accused Brussels of "blowing" taxpayers' money. He made his quarrel with the United States over the Iraq war the centrepiece of his 2002 campaign for re-election—an unprecedented affront to Germany's most important ally. With Vladimir Putin's Russia, Mr Schröder was poodle-like. The two men agreed to build an undersea gas pipeline from Russia to Germany bypassing central Europe and the Baltic states, which Poles denounced as a second Molotov-Ribbentrop pact.

After Mr Schröder's pugnacity, Mrs Merkel's consensual style looked like a return to German form. She was instrumental in ensuring passage of the Lisbon treaty, which is supposed to help the EU cope with its expansion to 27 members and creates machinery for an EU foreign policy. She repaired relations with Germany's eastern neighbours, reassured the United States and pandered less to Russia.

As a Euro-builder, she soon showed, she is not in Mr Kohl's class. During economic crises her first instinct has been to double the guard around the German treasury. She backed the appointment of relative lightweights for both the EU presidency and the foreign minister's job created by the Lisbon treaty.

"Under Merkel, Germany is no longer an actor that supports supranational development," says Hans Stark of the French Institute for International Relations. The assumption now, he says, is that individual governments, not the European collective, will remain the principal actors "and Germany has adapted to that." Germany's brightest business prospects do not involve its slow-growing neighbours but the charismatic economies of Asia and Latin America. A German acceptance of Turkish membership of the EU looks less likely than ever.

Relations between Germany and France, traditionally the twin motors driving European integration, are volatile. The methodical Mrs Merkel and Nicolas Sarkozy, the impulsive French president, are not natural partners. He recently quoted Mrs Merkel as saying that Germany was about to put in place a policy of expelling gypsies just like France's, which drew a sharp denial from the chancellery. When previous German chancellors and French presidents clicked, their relationship "cascaded down to other levels", says Mr Heisbourg, the strategist. "That is totally lacking today." Mrs Merkel and Mr Sarkozy manage to resolve crises as they threaten to spin out of control. But Franco-German ambitions for Europe have sputtered. German standoffishness toward the EU is now based in law: a

2009 ruling by Germany's Constitutional Court allowed it to ratify the Lisbon treaty but limited further transfers of power to Brussels. Soon the court may weigh in on the euro-zone bail-out.

Such omens suggest that the Berlin republic is a different sort of character from its westward-leaning, Bonn-based predecessor. Scholars had struck several awkward coinages to describe war-chastened Germany: it was a "tamed power" engaged in "attritional multilateralism". These no longer seem apt for today's more confident and self-willed Germany. But its identity is still unformed. Germany has "instincts sometimes rather than a clearly articulated policy", says a senior EU official. An American diplomat believes it is still "trying to decide what its foreign policy in the 21st century should look like". Germany is becoming more "normal", meaning more willing to use its strength and to accept responsibilities that go along with it. That looks to America like a good thing. But can Europe afford a more normal Germany?

Europe wants some nice leadership...

Germany's most pressing European business is to sort out the euro, the foundation on which the European edifice now rests. Euro members promised to observe financial disciplines, which many soon flouted (including Germany, which let its budget deficit breach 3% of GDP). That, says Germany, must never happen again. In September the European Commission proposed German-inspired rules that would limit "macroeconomic imbalances" such as excessive current-account deficits, in addition to budget deficits and public debt. Rule-breakers would face sanctions.

The reform of the euro will create a more German Europe, but not quite the economic Pax Germanica some observers are expecting. "We need German discipline," says Sylvie Goulard, a French member of the European Parliament, "but without growth it will be more difficult to make this discipline acceptable." On October 18th Mrs Merkel and Mr Sarkozy struck a deal that would weaken the sanctions regime proposed by the commission (by letting heads of government decide whether to impose them). In return, France agreed to support a debt-restructuring procedure demanded by Germany (seeCharlemagne). In Brussels that caused dismay. The Franco-German axis looked stronger. But German discipline, and the role of European institutions in enforcing it, were weakened.

German leadership is more apparent in other areas. It has assets available to none of the other big euro members, including unparalleled trade links to rising powers (nearly half the EU's exports to China come from Germany) and a leader who is taken seriously by her counterparts (David Cameron is respected, but Britain does not count). Germany is claiming leading positions in EU institutions: Uwe Corsepius, Mrs Merkel's European adviser, will become secretary-general of the European Council. Axel Weber, now head of the Bundesbank, is favoured to become the next president of the European Central

Bank. In European deliberations, Germany often sets the tone. Not until the Germans concluded that the Pakistani floods were really grave did the EU take action (by extending trade concessions). They may well take the lead in deciding whether to recognise China as a market economy in applying international trade standards.

But, despite such examples of leadership, Germany's overall direction is obscure. It is torn, intrigued by its new possibilities but painfully aware that alone it does not count for much in the world. Its population is already shrinking. Europe will lose economic and demographic bulk relative to China, India and Brazil. The EU was virtually ignored at last year's Copenhagen summit on climate change, even though it had taken the lead in setting targets to reduce greenhouse-gas emissions. This was "an enormous shock", says Guy Verhofstadt, a former Belgian prime minister who now leads the liberals in the European Parliament. "It shows we need one voice." Fear of war launched the European project; he hopes that fear of irrelevance will drive it forward.

Some quarters of the German establishment nod in agreement. Pressed for Germany's vision of Europe, Werner Hoyer, an aide to the foreign minister, says it is to secure Europe's "success in a globalised world". That means "deepening economic integration", dismantling remaining barriers to the single market and dealing with other powers through Brussels, not national capitals. "It is in our interest to convince them that the gateway to Europe is European institutions," says Mr Hoyer. He thinks Europe must "globalise its foreign policy if we don't want to be bystanders". Whether the prosaic chancellor shares these ambitions is unclear. She is a pilot who does not believe in making announcements from the flight deck.

And so Germany's partners are likely to remain on edge. The EU needs Germany's leadership more than ever, but fears its pre-eminence. Europe also needs consensus, but will not get it unless the Germans foster it. Matters will be even worse if Germany's economic self-confidence comes across as political arrogance.

America would rather see it stand tall

The Obama administration views Germany's rise not with consternation but with impatience. "Germany is emerging as a much more active world player, which is a good thing," says an American diplomat. The latest sign of that is the success of Germany's campaign this month to win a temporary seat on the UN Security Council, the first time it has challenged rival contenders. It has lately been an active ally to the United States, pressing Serbia to accept Kosovo's independence and toughening sanctions imposed on Iran. And Germany's dealings with Russia arouse less suspicion under Mrs Merkel than they did when Mr Schröder was chancellor. At a triangular meeting in the French resort of Deauville this week, Mrs Merkel and Mr Sarkozy persuaded Russia's president, Dmitry Medvedev, to attend NATO's forthcoming summit and to consider joining a European missile-defence shield.

Yet in military terms, Germany remains a midget compared not just with America but with Britain and France, which together account for 70% of the EU's military research and development and 60% of its deployable forces. "What's missing is Germany leading rather than seeing what Paris and London cook up," says a NATO diplomat. Its military deployments in Afghanistan and elsewhere are recent and unpopular. Its body of strategic thinkers is small. Germany's trading relationships bring influence, but also inhibit its willingness to join allies to fight global threats.

America and Europe are seeking slightly different answers to questions posed by Germany's growing strength. Americans, says the diplomat, hope for "an outward-looking Germany" that is less "conflicted about its weight in the world". Europeans, for their part, look to Germany for leadership, but want it to be tempered by traditional German self-restraint. In the eyes of its allies there are still two Germanys. It may have to learn to be both.

http://www.economist.com/node/17305755

A country's welcome rise: Is Turkey turning its back on the West?

No. But it might if Europe and America cannot come to terms with its success

Thursday, Oct 21 2010

ITS strategic position, next to the Middle East and Russia and astride Europe and Asia, means that Turkey has always mattered. But over the past decade its significance has hugely increased. For Turkey has gone through two big, and not always widely recognised, transformations: in its economic performance and in its foreign policy.

For most of the post-war years the Turkish economy was, to reuse Tsar Nicholas I's 19th-century phrase, "the sick man of Europe", plagued by erratic growth, soaring inflation and periodic banking busts. Today inflation is far lower, the banks are solid and Turkey boasts the fastest-growing economy in the OECD club of rich countries. Because it is resource-poor, this growth reflects fundamental strengths, especially in manufacturing and construction. Turkey makes things like furniture, cars, cement (it is the world's biggest exporter), shoes, televisions and DVD players. In a sense, it is Europe's BRIC: it might be called the China of Europe.

On foreign policy this long-standing member of NATO, with an army second in size only to America's, has always been a bulwark of the West. Turkey and Norway were the only NATO members to border the Soviet Union. But Turkey's pro-Western stance led it to neglect its neighbourhood, including many countries once in the Ottoman empire. Here, too, there has been a transformation. Backed by its strong economy, Turkey has become highly active in its diplomacy across the Middle East, in the Balkans and as far afield as Africa—and not always to the satisfaction of its allies. In a sense, Turkey has become a local diplomatic giant—the Brazil of the region.

You might imagine that Western powers would welcome such an advance. Instead, a more prosperous, bumptious Turkey is jangling many nerves. Europeans are trembling over the prospect of being asked to admit such a populous state into the European Union. The United States, which used to scold the Europeans for their reluctance, is uncomfortable with Turkey's newly adventurous foreign policy. Critics in the West are prone to hide behind the idea that Turkey is drifting towards Muslim fundamentalism and somehow "being lost" by the West. This judgment is completely wrong; yet the more that people in the West persist in making it, the greater the chance that they may genuinely lose Turkey.

The perils of democracy

In foreign policy, the government of Recep Tayyip Erdogan has certainly fallen prey on occasion to excessive Muslim solidarity. It has been too nice to Sudan's ghastly president, Omar al-Bashir, ignoring his indictment for war crimes. It made a mistake by joining Brazil in an ill-fated Iranian nuclear initiative that led to the embarrassing sight of Turkey, a member of the UN Security Council in 2009-10, voting against tougher sanctions on Iran. And its increasingly strident attacks on its once-close ally, Israel, have angered not only the Israelis but also many Americans, especially after the Turkish-led flotilla that tried to "relieve" the siege of Gaza this summer.

But wait a moment. Brazil was nice to Iran, without anyone doubting its Western credentials. On Israel, Mr Erdogan has certainly at times played to the Arab street. But many of Turkey's complaints, such as over settlement-building in the West Bank, are hardly controversial. It may have been ill-judged for the government to have been involved with those who launched the Gaza flotilla, but this would not have turned into such a catastrophe had the Israelis not killed nine people on board the leading ship. More fundamentally, the Turkish government is doing what democracies tend to do: reflecting its people's views. Many Muslims think the Palestinians have been ill-treated. From an Israeli viewpoint it is no doubt awkward to have its human-rights record questioned by an elected prime minister, rather than by the usual Arab dictators. But who would America rather hear as a Muslim voice? The autocrats in Egypt and Saudi Arabia? The clerics in Iran?

The Europeans are also in a funk—over Turkey's possible membership of the EU. Negotiations have formally been going on for over five years. No country that has begun such talks has ever failed to be offered membership. But the leaders of France, Germany, Austria and the Netherlands seem dead set against Turkish entry, as is much of their public opinion. The unresolved Cyprus dispute seems a near-insuperable roadblock. Yet if the EU chooses to exclude its own China, it will be turning away the fastest-growing economy in its neighbourhood. It will also lose any hope of influencing the region to its east. At a time when many Europeans fret about being ignored in the world, this would be an historic mistake.

How Western are they?

The common excuse for these follies is the claim that Turkey is not really Western—and is becoming ever less so. Once again, Mr Erdogan has done some unhelpful things. Critics note that, ever since his mildly Islamist Justice and Development (AK) party came to power in 2002, it has been engaged in a battle with the Kemalist secular establishment. He is intolerant of dissent, shown in his battles with critical media commentators. And he is increasingly impatient with the EU.

Yet fears of Turkey turning into the next Iran are absurd. A new tolerance of the headscarf in universities does not imply a sudden lurch into stoning adulteresses. Mr Erdogan's run-ins with his opponents have certainly created a polarised society; he should adopt a more conciliatory tone if he wins re-election next June. But his opponents in the media still write their critical columns. It is troublemakers in the army who have posed a greater threat to democracy in recent times.

In short, Turkey is heading in a good direction. It remains a shining (and rare) example in the Muslim world of a vibrant democracy with the rule of law and a thriving free-market economy. Much though Western leaders would like to turn the argument into one about Turkey, the real question is for them. Are Americans and Europeans prepared to accept Turkey for what it is: a Muslim democracy, with a different culture and diplomatic posture, but committed to economic and political liberalism? This newspaper hopes the answer is yes.

http://www.economist.com/node/17309065