

# THE WALL STREET JOURNAL.

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WSJ.com EUROPE EDITION

DJIA 21012.42 ▲ 0.36%

NASDAQ 6163.02 ▲ 0.40%

NIKKEI 19742.98 ▲ 0.66%

STOXX 600 392.37 ▲ 0.09%

BRENT 53.96 ▼ 0.35%

GOLD 1252.40 ▼ 0.19%

EURO 1.1179 ▼ 0.04%

## What's News

Business & Finance

**M**oody's downgraded China for the first time since 1989, a warning to Beijing about its growth model and illustrating the disconnect between the view inside and outside China of its economic management. **A1**

◆ **Earnings at U.S. firms** grew at the fastest pace in nearly six years in the first quarter, the latest boon to a bull market that has stretched into its ninth year. **B1**

◆ **Fed officials expected** at their policy meeting this month that it would "soon be appropriate" to raise interest rates again. **A7**

◆ **OPEC is poised** to curtail oil output for at least another nine months when it meets on Thursday. **B1**

◆ **U.S. Democratic** lawmakers have asked Deutsche Bank to provide details about its internal reviews into Russian trades and clients, as well as loans made to Trump. **B5**

◆ **IKEA CEO Agnefjäll** resigned in a surprise move less than four years after formally stepping into the role. **B3**

◆ **U.S. prosecutors unveiled** insider-trading charges related to trading in healthcare stocks allegedly based on information about imminent policy changes by the U.S. government. **A7**

◆ **GE's Immelt said** the firm would likely need more cost cuts to reach a 2018 profit target. **B4**

◆ **A U.S. appeals court** questioned the powers of the SEC's in-house courts in a case that could transform how the regulator carries out its enforcement authority. **B7**

### World-Wide

◆ **U.K. police said** they were investigating "a network" in connection with the Manchester suicide bombing, while a Libyan militia said the brother of the suspect confessed that both were Islamic State members. **A1, A3**

◆ **Trump's proposal** to help reduce the national debt by selling more of the U.S. emergency oil stockpile is reigniting a debate about whether the reserves are still crucial to economic security. **A1**

◆ **The U.S. military detailed** plans to increase spending in Europe by \$1.4 billion, supporting new NATO initiatives to fill gaps. **A4**

◆ **A meeting between** Trump and Pope Francis balanced talk of disagreements on issues such as migration with accord on other topics like abortion. **A4**

◆ **EU nations** fighting to host the bloc's top financial regulator and drugs watchdog will vote over where the agencies now based in London, will move. **A2**

◆ **Philippines security forces** closing in on a leader of the Abu Sayyaf terrorist group clashed for a second day with his armed supporters. **A5**

◆ **Taiwan's top court ruled** that defining marriage as just between a man and a woman was unconstitutional. **A5**

◆ **Trump faced** resistance in Congress over a budget plan that depends heavily on cuts to social programs and aggressive growth projections. **A6**

◆ **Justice Department** officials recently interviewed a former U.S. attorney for the post of FBI director. **A6**

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€3.20; CHF5.50; £2.00;  
U.S. Military (EUR) \$2.20

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Please see SNAP page A8



Troops from the British Army arrived on the streets in London to help guard the Houses of Parliament. The military is working in conjunction with police to provide security after the terror attack at Manchester Arena.

## U.K. Probes Attack Network

Police explore possibility a terrorist technician constructed sophisticated bomb

British police said they were investigating "a network" in connection with the deadly suicide bombing at a Manchester pop concert, as a Libyan militia said its questioning of a brother of 22-year-old suspect Salman Abedi had yielded a confession that both men were members of Islamic State.

Hashem Abedi also confessed

to being in the U.K. during preparations for Monday's attack and was aware of all plans, said Ahmed Dagdoug of Radaa, one of several large militias responsible for security in Tripoli.

Radaa, which holds sway over part of the Libyan capital, said the younger Abedi was arrested late Tuesday in the city as he picked up a wire transfer of 4,500 Libyan dinar, or about \$3,260, sent by his late brother, Salman.

By Hassan Moraje in Tunis, Tunisia, Jenny Gross in London and Wiktor Szary in Manchester, England

It was impossible to independently confirm Radaa's claim or to ascertain how such a confession would have been obtained. Libyan militias routinely resort to harsh tactics to extract information from terrorism suspects.

The group's spokesman, Mr. Dagdoug, said it was also holding Abedi's father, Ramadan Abedi, to aid in the investigation of the attack, which killed 22 people outside a concert by American singer Ari-

ane Grande. It wasn't immediately clear whether the Libyan group was in contact with British investigators, who on Tuesday in Manchester arrested a man one Western official identified as 23-year-old Ismail Abedi, another brother of the suspect.

British intelligence agencies and police made raids on more properties on Wednesday and are piecing together how Salman Abedi came to use a sophisticated bomb to carry out the deadliest attack in the country since 2005.

Please see ATTACK page A3

## A Battle for the Spoils of Brexit

European countries are vying for EU agencies due to leave Britain.

European Banking Authority

Key figures 2016

European Medicines Agency

Key figures 2015

189	Number of staff	890
130	Number of staff children	648
9,215	Number of visitors	36,000
2,345	Total space, in square meters	27,600
Office space		20,935
Meeting rooms		6,000
Storage and other services		730
Offsite storage		841
		774

Sources: European Commission; European Council

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**SECRET BALLOT:** European Union countries fighting to host the bloc's top financial regulator and drugs watchdog will vote over where the agencies now based in London, will move. **A2**

## J.CREW BOSS REGRETS UNFASHIONABLE SLIP

Retail legend says he misjudged how speed, price drive internet sales

BY KHADEEJA SAFDAR

Millard "Mickey" Drexler, the fashion genius whose ability to spot trends reshaped how Americans dress, has a humbling admission. He missed what might be the biggest trend of all—how quickly technology would change the retail industry.

"I've never seen the speed of change as it is today," the 72-year-old chairman and chief executive of J.Crew Group Inc. said in an interview at his New York office. "If I could go back 10 years, I might have done some things earlier."

The retail veteran, who redefined Gap Inc. in the 1990s and then transformed J.Crew into a household name, is now

scrambling to keep the company he took private in a leveraged buyout from ending up in bankruptcy.

Sales at J.Crew Group stores open at least a year have fallen for the past 10 quarters—the kind of slump that got Mr. Drexler ousted from the Gap in 2002. This time he owns 10% of the company, and it is lenders, not the founding family, that are putting on the pressure.

For decades, fashion was essentially a hit-or-miss business. Merchants like Mr. Drexler would make bets on what people would be wearing a year in advance, since that's how long it took to design and produce items.

Hits guaranteed handsome returns until the

Please see RETAIL page A8

Sustaining A Snapstreak Takes Work

\* \* \*

Send a photo of the floor, but don't time out

BY KATHERINE BINDLEY

Bothaina Saleh has many of the typical concerns of a 25-year-old marketing manager living in Manhattan. They include her Snapstreak, which she maintains "in the same way I make sure that I brush my teeth."

Other teens and millennials across America, too, are obsessively cultivating their Snapstreaks.

Let us explain.

Snapstreaks start with Snapchat, the messaging app that lets a person send a friend "snaps"—those photos and videos that can disappear

Please see SNAP page A8

## U.S. Now Wonders: Why Hoard Oil?

BY ALISON SIDER AND ERIN AILWORTH

President Donald Trump's proposal to help reduce the national debt by selling down more of the U.S. emergency oil stockpile is reigniting a debate about whether the reserves are still crucial to the country's economic security.

The Trump administration said Tuesday that its budget proposal calls for selling an additional 270 million barrels of oil over the next decade. Congress had already recently approved selling down some reserves to raise money for various domestic programs.

The administration now wants to increase those sales. Officials said the proposed amount could bring in \$500 million in fiscal 2018 and \$16.6 billion through 2027.

Proponents say the reserve is necessary in the event of a crisis, such as a war in the

Middle East or another violent disruption to supply, that could leave the U.S. short of oil for a period.

Critics say that rising domestic production makes such large reserves redundant and that proceeds from selling it could be put to better use.

The Strategic Petroleum Reserve, or SPR, was intended as a buffer against disruptions in the flow of imported oil. It was created after the Arab oil embargo of 1973-74, which sent shock waves through the U.S. economy.

Gasoline prices at the pump soared, feeding inflation. Drivers were stuck in long lines at filling stations that couldn't get enough fuel.

The reserve is now the

Please see OIL page A2

◆ Shale drillers in U.S. put heat on OPEC ..... B1

◆ Barkindo emerges as cartel's chief diplomat ..... B5

## Oracle #1 SaaS Enterprise Applications Revenue

#1

Oracle Cloud 14.5%

#2

Salesforce Cloud 12.4%

1,000+ Employees Segment, 2015

ORACLE®

oracle.com/applications

Source: IDC "Worldwide SaaS Enterprise Applications Market Shares, 2015: The Top 15 by Buyer Size," doc #US41913816, Dec. 2016; Table 4. For the purposes of this report, SaaS enterprise applications include the following application markets: CRM, engineering, ERP, operations and manufacturing, and SCM.

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## WORLD NEWS

**CAPITAL ACCOUNT** | By Greg Ip

# U.S., British Conservative Tactics Diverge



Donald Trump's election as U.S. president and Britain's vote to leave the European Union presented the conservative parties in both countries with a once-in-a-generation choice. They had rejected open borders in favor of a nationalist approach to immigration and trade. Would they revert to small-government conservatism on everything else, or reach across traditional divides by appealing to workers who still treasure activist government?

With his budget this week, Mr. Trump chose the first option. With its promise of balanced budgets, lower taxes and deep cuts to social programs, it is more aligned with the Republican party's right-wing Freedom Caucus than the blue-collar workers who are disillusioned with Democrats.

By contrast, British Prime Minister Theresa May has chosen the second. Last month, she launched an election with a call to reject "the socialist left and the libertarian right and instead embrace the mainstream view that recognizes the good that government can do."

It is early days, but there are signs Mrs. May's approach is paying off where Mr. Trump's isn't.

In his march to the Republican nomination last year, Mr. Trump made it clear he wasn't a traditional Republican, not just in opposing free trade, but also in his commitment to keep intact the entitlements that Americans love but which put relentless pressure on the budget: Social Security,



Theresa May and Donald Trump spoke at a joint news conference at the White House in January.

Medicare and Medicaid. That those commitments didn't align with his promised tax cuts didn't much bother voters.

In this week's budget, the president had to make actual choices, and it looks like he sided with the Freedom Caucus, which prioritizes limited government, personal liberty and low debt. How did the two reconcile their agendas? Mick Mulvaney, the former Freedom Caucus member who is Mr. Trump's budget director, "went in to the president with a list of proposed entitlement reforms—some reductions, some eliminations," Mr. Mulvaney said this week. "And we went down the list. Yes, yes, no, no, yes, no, yes, no, no."

Mr. Mulvaney advances solid, nonideological reasons for some of the cuts: Programs that don't meet their

goals shouldn't exist, and some services are best delivered by states, not Washington.

But he also advocates a change in mind-set. The budget, he says, should be looked at from the viewpoint of those who pay for benefits: taxpayers. The catch is that many Americans also see themselves as beneficiaries of those programs, if not now, then some day. That's why cuts to entitlements are deeply unpopular. At Mr. Trump's insistence, the budget doesn't touch Social Security retirement benefits or Medicare for retirees. But his proposed cuts to Medicaid already face bipartisan resistance. Though aimed at the poor, more than half of the program's recipients work. A Kaiser Family Foundation poll in February found that 57% of respondents had at some point been covered by Medicaid, or had a child, relative or friend who was once covered by Medicaid.

On taxes, too, Mr. Trump's proposals don't align with popular opinion. The lion's share of the benefits of his proposed personal and business tax cuts go to the 20% most affluent households, according to the Tax Policy Center, a think tank. From a Freedom Caucus point of view, this is logical: The rich bear most of the cost of the welfare state, so if that state shrinks, so should the bill.

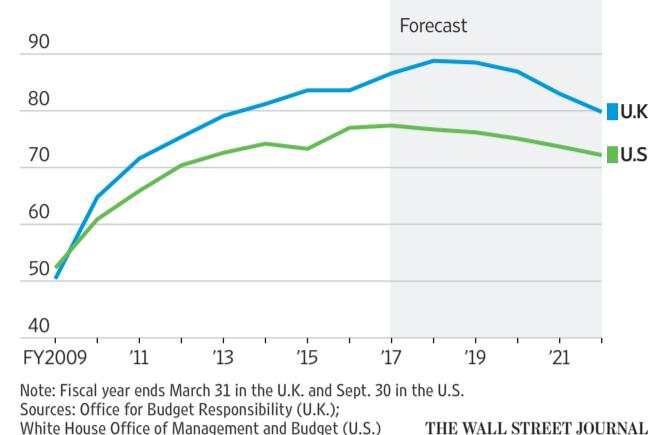
But working and middle class Americans are quite content to draw more in services than they personally pay in taxes.

Under former Prime Minister David Cameron, Britain's Conservatives cut corporate tax rates while slashing welfare spending. Since taking over, Mrs. May has steered the party in a less austere direc-

## Different Priorities, Paths

The British government has repeatedly pushed back the year when the government debt as share of GDP is projected to drop; Donald Trump wants to start now.

### Debt as percent of GDP



Note: Fiscal year ends March 31 in the U.K. and Sept. 30 in the U.S.  
Sources: Office for Budget Responsibility (U.K.);  
White House Office of Management and Budget (U.S.)

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itizen at the mercy of market forces."

For now, this is working politically. Mrs. May is leading in the polls for the June 8 election, though her lead has narrowed. She is much less polarizing than Mr. Trump: Her approval rating is 52% compared with Mr. Trump's 39%, according to polls this month by YouGov. Among those who voted Labour or Liberal Democrat in 2015, her approval is 25% and 47%, respectively; Among Democrats, Mr. Trump's is 13%.

Mrs. May may not ultimately reshape British politics or even her own party. Moreover, like Mr. Trump, her greater legacy is likely to rest on how much she claws national sovereignty back from the forces of globalism. Meanwhile, she has offered the world an alternative vision for conservative nationalism.

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In the broader budget, such gestures are small. The bigger change is "the political tone," says Paul Johnson, director of the Institute for Fiscal Studies, a think tank. It signals "a willingness for the state to...protect the citizen rather than leave the citizen at the mercy of market forces."

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## WORLD NEWS

## U.K. Suspect Was Frequent Libya Visitor

Investigators look into ties to Islamic State, which controlled parts of North African nation

By TAMER EL-GHOBASHY

Outside Iraq and Syria, the radicals of Islamic State only administered territory in one other country: Libya.

As British investigators search for links between Islamic State and the Manchester bombing, focus has turned to the North African country, where the militant group ruled one of the oil-rich nation's most important cities and used it to stage terrorist attacks and train foreign fighters.

Salman Abedi, the 22-year-old man thought by British authorities to have carried out the bombing for which Islamic State claimed responsibility, was a British citizen of Libyan descent. His journeys in and out of a country where the militant group once cast a large shadow are now a central focus of investigators, a Western security official said.

For more than a year, Islamic State controlled the port city of Sirte, imposing its signature brutal rule and exploiting the anarchy of the politically divided country to train and slip fighters into neighboring Tunisia, where they targeted European tourists.

Since a powerful western Libyan militia, aided by U.S. airstrikes, ousted it from Sirte in December, the group's foothold in the country has



**Islamic State militants, shown with Ethiopian Christian captives in Libya before executing them in 2015. Alleged Manchester attacker Salman Abedi traveled in and out of the country, where the terrorist group once had a strong foothold in the port city of Sirte.**

shrunk, but in a land where rival governments are vying for control, European and Arab officials remain concerned about the group's ability to mount attacks abroad.

Last year, the U.S. planned to kill an Islamic State leader from France who was using the messaging app Telegram to threaten his native country with bloodshed, a Western security official said. He also sent fellow Europeans to France, possibly to carry out attacks, the official said.

The militant leader, however, was hiding at the Sirte power station and any air-

strike could have caused electricity blackouts across large parts of Libya, so no raid was launched, the official said. The French militant's current location is unknown.

In January, the U.S. bombed Islamic State training camps in Libya's desert interior, illustrating Washington's concern over the continued threat posed by the group but also underscoring how far it had been pushed from the country's more heavily populated Mediterranean coast.

Islamic State's emergence in Libya began quietly in 2014, three years after long-

time dictator Moammar Gadhafi was toppled from power and killed, leaving no central government and a dangerous security vacuum the Islamist group exploited.

Comprised mostly of hardened local Islamist radicals and hundreds of militants from nearby Tunisia, Islamic State co-opted local insurgent groups and enticed new recruits with promises of prosperity and power. It could also boast of its takeover of vast swaths of Iraqi and Syrian territory in lightning speed.

On the crest of that suc-

cess, Islamic State quickly added Sirte, Gadhafi's hometown, to Mosul in Iraq and Raqa in Syria, the other jewels of its expanding caliphate. It declared the city its capital in Africa, and vowed to launch attacks across the Mediterranean into Europe.

To Sirte it drew thousands of recruits from the Arab world and elsewhere on the African continent. In February 2015, it released videos of military parades in its African capital and in another smaller Libyan city, Derna. Hundreds of fighters packed aboard pickup trucks outfitted with

heavy machine guns flying the black flag of Islamic State.

The group tightened its grip ruthlessly in parts of Libya, twice releasing videos in 2015 showing the execution of captured Egyptian Coptic Christian laborers and Ethiopian and Eritrean migrants.

Later, three Tunisian men who received training in its Libyan camps staged separate attacks on a museum in Tunis and a seaside resort in Sousse that left scores of European tourists dead.

With its expanding ability to attack outside Libya's borders, the U.S., together with Arab and European nations, began to intervene, joining a United Nations-led effort to form a unity government that could counter Islamic State's growing sway and stabilize the nation's crumbling economy. That effort remains troubled by disagreements and fighting between Libyan factions.

While the loss of Sirte and foreign diplomatic intervention have weakened Islamic State, the group maintains a presence in the country, mostly in the border regions with Algeria and Chad.

According to a Libyan military intelligence official, the group has set up camps and checkpoints in those remote areas and has carried out occasional attacks against forces loyal to Libya's government.

—Hassan Morajea  
in Tunis, Tunisia,  
Benoit Faucon in Vienna  
and Jenny Gross in London  
contributed to this article.

## Grieving Families Take Stock of Loss

BY DENISE ROLAND  
AND SAABIRI CHAUDHURI

One died in the blast in a way that shielded her sister and niece. Several were parents waiting to pick up their children.

Friends and family confirmed the identities of more victims of the bombing that claimed 22 lives as thousands of concertgoers, including many children, streamed out of a Manchester arena after watching American pop star Ariana Grande perform.

Ian Hopkins, chief constable of the Greater Manchester Police, said Wednesday that an off-duty police officer had been among those killed in the bombing. He said he wouldn't release further details at this time, based on the wishes of family members.

Kelly Brewster, a young woman from Sheffield, east of Manchester, was walking behind her sister Claire and niece Hollie when a man identified by police as Salman Abedi detonated an explosive outside Manchester Arena.

She "shielded Hollie and Claire from the damage," Ms. Brewster's uncle Paul Dryhurst told ITV television. The mother and daughter are in a hospital having shrapnel removed, he added.

Martyn Hett, a public-relations manager headed to a pub on Monday to drink Prosecco with his friend Stuart Aspinall in the sunshine, according to a post on Mr. Hett's Facebook page, before heading to the Ariana Grande concert together.

Mr. Hett, slated to leave for



Tributes are laid at Manchester's Albert Square on Wednesday.

a two-month vacation to the U.S., had spent the last few days saying goodbye to friends.

"We got the news last night that our wonderful iconic and beautiful Martyn didn't survive," a friend wrote on Twitter. "He left this world exactly how he lived, center of attention."

Friends Alison Howe and Lisa Lees were waiting outside the arena when the bomb exploded. Both women, in their 40s, were waiting outside the venue for their teenage daughters, according to local media.

"They took a caring beautiful mum and stepmother away from us all," read a Facebook post from Ms. Howe's stepson, Jordan Howe. "She was amaz-

ing to us all."

Lee Hunter, Ms. Lees's brother, confirmed her death in a Facebook post late Tuesday. "For those who don't know Lisa is gone but never forgotten I love you Lisa I'll miss you so much," he wrote.

Marcin Klis, a Polish man who worked as a taxi driver in York, northern England, and his wife, Angelika, were also waiting outside the venue for their children when the blast went off.

"Two girls, one of them a grown-up, the other a teenager, were at the concert. The parents drove over after the concert to pick their daughters up," Poland's foreign minister,

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"Two girls, one of them a grown-up, the other a teenager, were at the concert. The parents drove over after the concert to pick their daughters up," Poland's foreign minister,

Witold Waszczykowski, told local radio station RMF FM on Wednesday. "The children are safe," he added.

Fifteen-year-old Olivia Campbell, from Bury north of Manchester, was also among the victims. "RIP my darling precious gorgeous girl Olivia Campbell taken far far to [sic] soon going with the angels and keep smiling mummy loves you so much," read a Facebook post from her mother, Charlotte.

Ms. Campbell, who like many relatives spent Tuesday

frantically appealing for information, tearfully told CNN earlier on Tuesday how Olivia and her best friend had bought new outfits for the event. They were just "normal teenage children going to see one of their favorite artists," she said. "It's ended in absolute carnage."

Jane Tweddle-Taylor, a woman from Blackpool, England, in her early 50s, was also killed after going to the arena with a friend to collect the friend's children.

Jane was a very, very lovely lady and a very good mother to three daughters, liked by everybody," Ms. Tweddle-Taylor's partner, Mark Taylor, told BBC Radio Lancashire as he choked back tears. The friend and children survived, he said.

A young girl, Megan Hurley, was also identified as a victim by a woman named Helen McDermott, who set up a fundraising page for the funeral.

The youngest confirmed victim, 8-year-old Saffie Rose Roussos, was identified on Tuesday.

—Wiktor Szary contributed to this article.

## Armed Troops Patrol British Landmarks

BY ROBERT WALL

LONDON—Visitors flocking to the U.K. will face an unusual sight: armed uniformed troops at some of London's most famous landmarks as the country tightens security amid concerns more terrorist attacks could follow in the wake of Monday's fatal bombing in Manchester.

London's Metropolitan Police Service, the U.K.'s largest police force, said military personnel will be deployed at locations such as Buckingham Palace, the Downing Street home of the prime minister, embassies and the Palace of Westminster, home to the legislature.

Parliament on Wednesday

said the building would be closed to public tours and events because of the elevated threat level. The Changing of the Guard parade at Buckingham Palace was canceled for Wednesday with future plans under review, a British Defense Ministry official said.

The Bank of England Museum also closed Wednesday.

The threat level is likely to lead to greater coordination between public-safety organizations and event security staff, said Steve Park, managing director of Global Security Resources Ltd.

Venues throughout the U.K. have elevated security measures.

The Football Association said extra security would be on hand for one of the biggest domestic soccer matches this weekend. MCM Comic Con, the convention for comic

collectors and gamers, said it would have additional security for its big gathering starting Friday at the large ExCel London convention center.

The Met, as the police force is commonly known, said it was also deploying behavior detection specialists to help spot potential attackers. Security experts said those highly trained staff are critical to safeguard difficult-to-secure areas, such as the large public spaces that have become a preferred target for terrorist attacks, including the foyer of the Manchester Arena, the Bataclan theater in Paris hit in November 2015, and the Brussels and Istanbul airports attacked last year. The officers, used for years by Israeli domestic security forces, are trained to spot individuals whose actions suggest hostile intent.

The Ministry of Defence said about 1,000 soldiers are being deployed to free up armed police for other duties.

Ben Barry, senior fellow for land warfare at the International Institute for Strategic Studies, said a deployment of 1,000 troops should be sustainable for some time. "The army is the least stretched" of the country's services, he said.

The open-ended nature of the operation does raise questions, though, he suggests. "It is easy to get soldiers on the streets. It is much more difficult to get them off."

—Jason Douglas in London,

Nick Kostov in Paris, Valentina Pop in Brussels and Ruth Bender in Berlin contributed to this article.

## ATTACK

Continued from Page One

"I think it's very clear that this is a network that we are investigating," said Ian Hopkins, chief constable of the Greater Manchester Police. "There's extensive investigations going on and activity taking place across Greater Manchester as we speak."

Three arrests were made in the south of the city on Wednesday as part of the investigation, a Manchester police spokeswoman said, and another in Wigan, a town roughly 20 miles away. That brings the total in custody in Britain to five, including Ismail Abedi. Under British law, a person can be taken into custody in a terrorism investigation and held up to 14 days without charge.

British police have de-

clined to provide many details about the suicide-bombing suspect, Abedi. Home Secretary Amber Rudd told the British Broadcasting Corp. he was previously known to security services "up to a point." Officials believe he had recently returned from Libya, where his parents are believed to have lived after years in the U.K.

U.K. investigators told French authorities that Abedi had probably also traveled to Syria, according to the French interior minister.

A leading theory is that there is a technician in the U.K. who constructed the bomb, a Western official said.

"Clearly, with the raids ongoing, it's a key part of the investigation. To cause this many fatalities it has to be a viable device of a certain level of sophistication," the official said, adding that it didn't seem like something Abedi

could have done by himself. Officials were still in the initial phase of the investigation, the person said.

"It seems likely, possible, that he wasn't doing this on his own," Ms. Rudd told the BBC. "When this operation is over, we will want to look at his background and what happened, how he became radicalized and what support he might have been given."

Manchester, in England's northwest, was long a destination for radical Libyan Islamists during the Moammar Gadhafi era. Abedi, who grew up in the city, lived just miles from the scene of the attack, according to electoral records and neighbors, in a red brick house in a working-class area.

Neighbors described him as an aggressive man who didn't mix much with others in the community.

A spokesman at the nearby University of Salford said

Abedi enrolled at the university in 2015 to study business and administration, and completed a first year of study. He then "effectively dropped out, though technically he remained on our books," he said.

Abedi lived at home, not in student accommodation, and wasn't well-known to the university administration or the university imam, the spokesman said.

Prime Minister Theresa May raised Britain's threat level to "critical" late Tuesday. It has been at that level only twice, in 2006 and 2007, since the system was introduced 11 years ago.

Under the heightened alert level, military personnel are replacing police officers guarding key places and big events around the country, in an emergency plan called Operation Temperer.

Up to 3,800 military personnel were deployed on Brit-

ain's streets. Armed officers were stationed at key locations, including Buckingham Palace and Downing Street and Westminster, where Britain's Parliament sits. Parlia-

ment was closed to visitors and all tours, events and banquets were canceled, a spokesman said.

Islamic State claimed responsibility for the attack. British police haven't commented on the Islamist extremist group's assertion. U.S. officials cautioned they hadn't verified any connection between Islamic State and the attack.

Security officials are likely to review days and weeks of security camera tapes at the venue to assess if Abedi did reconnaissance on the venue and, if so, whether he was accompanied, according to a private-sector security expert. Forensic analysis of the bomb also could yield clues about who bought components to build the explosive device.

—Jason Douglas, Tamer El-Ghobashy, Denise Roland, Robert Wall, Mike Bird and Georgi Kantchev contributed to this article.



ASSOCIATED PRESS

Salman Abedi, the 22-year-old Manchester attack suspect.

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## WORLD NEWS

# U.S. Gives NATO An Unexpected Military Boost

BY CAROL E. LEE  
AND JULIAN E. BARNES

The North Atlantic Treaty Organization got a surprise as the U.S. military detailed plans to increase its own military spending in Europe by \$1.4 billion, supporting new NATO initiatives to fill military gaps.

Washington's plan, which comes as NATO is striving to meet President Donald Trump's demand for more counterterrorism work and greater European military spending, is at odds with Trump administration threats to cut military support for Europe.

Wednesday's news came as U.S. Secretary of State Rex Tillerson said Mr. Trump plans to deliver a tough message that Europe needs to increase its military spending at Thursday's meeting of NATO leaders.

Mr. Tillerson told reporters traveling on Air Force One that Mr. Trump "really wants participating NATO members to step up and fully meet their obligations of the burden sharing."

NATO Secretary-General Jens Stoltenberg highlighted the U.S. spending plans at a news conference. He said he didn't think there was a contradiction between the push to increase European spending and the additional U.S. military commitment.

"This is a commitment to our collective defense from the U.S., not only in words but also in deeds," Mr. Stoltenberg said.

NATO leaders will meet briefly on Thursday during a single dinner session. Officials said many subjects are likely to be raised by leaders during their four-minute speaking slots.

NATO is expected to unveil military spending agreements Thursday that will include European commitments to boost funding for military capabilities that NATO has identified as critical.

ing for next year, up from \$3.4 billion this year.

The plan is part of the Trump administration's budget proposal unveiled this week.

European Command said it would increase air defenses, enhance surveillance capabilities and position more weaponry in Europe for troops from the U.S. It also said it would boost anti-submarine warfare assets and rotate more Marines to Europe.

"It demonstrates the commitment of the United States to Europe," said Lt. Gen. Ben Hodges, the senior U.S. Army commander in Europe. "It should remove once and for all any doubts our allies or potential adversaries have about how much we care about stability and security in Europe, and what we are willing to do to deter Russia or any other potential adversary."

NATO officials have said European military budgets are increasing, rising by \$10 billion last year, with further boosts expected this year.

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Pope Francis exchanged gifts with U.S. President Donald Trump and first lady Melania Trump at the Vatican on Wednesday.

# Pope and Trump Set Aside Past Differences at Vatican

BY CAROL E. LEE  
AND FRANCIS X. ROCCA

VATICAN CITY—U.S. President Donald Trump and Pope Francis met for a fence-mending encounter that balanced talk of stark disagreements on issues such as migration with accord on other topics, including abortion.

Seated across from each other in the pope's private study on Wednesday, Mr. Trump and the pontiff spoke for 30 minutes, aided by an interpreter. Before leaving the Vatican, the president told the pope, "Thank you, thank you. I won't forget what you said."

During his talks later with Prime Minister Paolo Gentiloni of Italy, he said his meeting with the pope was "fantastic."

"He is something," the president said of the pontiff, who during last year's presidential campaign criticized Mr. Trump's views on immigration and said the candidate's plan to build a wall along the U.S.-Mexican border made him "not Christian."

After Wednesday's meeting with the pope, the president tweeted effusively: "Honor of a lifetime to meet His Holiness Pope Francis. I leave the Vatican more determined than ever to pursue PEACE in our world."

In a short communiqué following the visit, the Vatican highlighted points on which Mr. Trump and the pope agree, including abortion and religious liberty, as well as their notable differences, including health care and immigration.

One longstanding point of contention the Vatican communiqué didn't mention was the environment. After their private

conversation, however, the pope gave the president a copy of his encyclical on the environment, in which he argues that capitalism has contributed to the degradation of the environment at the particular expense of the poor. The president thanked the pope, saying he would read it.

The visit caps a whirlwind tour by Mr. Trump through countries that are home to the holiest sites for three of the world's leading religions: Islam, Judaism and Christianity. The president's trip to Saudi Arabia, Israel and Vatican City is intended to try to unify religious leaders around an effort to combat extremism.

From the relatively modest Vatican guesthouse where Pope Francis lives, he was driven to the Apostolic Palace in the used Ford Focus that was donated to him early in his papacy.

Soon after, Mr. Trump arrived in a motorcade of about 50 vehicles.

Inside the pope's private study, Mr. Trump told the pontiff it was "a very great honor" to meet him. The first lady, who wore a tea-length black dress as well as the black veil that is traditional for female guests meeting the pope, was part of the presidential entourage, as was the president's elder daughter, Ivanka Trump, also clad in black.

After the meeting, Mr. Trump gave Pope Francis a gift of first-edition copies of writings by Martin Luther King Jr., a nod to the pontiff's reference to the civil-rights leader during his 2015 address to a joint session of Congress.

In addition to his encyclical on ecology, Pope Francis gave

Mr. Trump copies of some of his other writings, including a message on nonviolence that he said he had personally signed for the president. He also gave him a medal bearing an olive tree, a sign of peace. "We can use peace," the president responded.

After his meeting with the pope, Mr. Trump met Vatican Secretary of State Cardinal Pietro Parolin. Their talk lasted 50 minutes, an unusually long time.

In its communiqué on Mr. Trump's visit, the Vatican high-

*'I leave the Vatican more determined than ever to pursue PEACE in our world.'*

lighted a "joint commitment in favor of life, and freedom of worship and conscience" between the Holy See and Mr. Trump's administration.

Those were apparent references to abortion and to the demand by U.S. Catholic leaders for a religious exemption to the contraception mandate in the Affordable Care Act, which Mr. Trump has promised to provide.

The references were a significant concession to the White House because the pope hasn't made such issues a priority.

But that point of agreement was offset by a call for collaboration on "health care, education and assistance to immigrants." U.S. bishops have said that Mr. Trump's plans to overhaul the health-care law must ensure that no one loses cover-

age.

On international affairs, the communiqué highlighted an "exchange of views"—diplomatic parlance that typically suggests disagreement—over the "promotion of peace in the world through political negotiation and interreligious dialogue, with particular reference to the situation in the Middle East and the protection of Christian communities."

Wednesday's meeting was closely watched given the contentious history between the two leaders.

Mr. Trump's meeting with the pope comes as his White House debates whether to withdraw from the international climate-change agreement to cap carbon emissions that world powers reached in Paris in 2015.

Mr. Trump, a Republican, was sharply critical of the accord and opposed it as a candidate. He had planned to decide the issue before his trip this week to the Middle East and Europe, but aides convinced him to delay it until after he returns.

U.S. Secretary of State Rex Tillerson later said he didn't know if the president and the pope had discussed climate change, but that the subject had come up in the meeting with Cardinal Parolin, which Mr. Tillerson also attended. The cardinal encouraged the president to remain in the Paris accord, and Mr. Trump replied that he hadn't made a final decision, Mr. Tillerson said.

Mr. Tillerson said the president and pope had some "pretty extensive conversations around extreme terrorist threats and extremism, radicalization of young people."

**Holiday Update**

The Europe edition of The Wall Street Journal will not be printed on Monday, May 29, in observance of the U.K. Spring Bank Holiday.

## JBS Holding Company In Talks Over Fine

J&F Participações, the holding company of meatpacker JBS involved in Brazil's vast corruption scandal, is willing to shell out at least \$1.3 billion as part of a leniency deal with prosecutors, a person close to the discussions said.

JBS became the latest focus of Brazil's "Car Wash" corruption investigation last week when the Supreme Court released plea-bargain testimony from its executives, who said they bribed 1,829 politicians, including President Michel Temer. He has denied wrongdoing and has rejected calls to resign.

J&F has been in negotiations with Brazilian authorities over the leniency agreement, according to the company.

The talks between the company and prosecutors had been halted Friday after an impasse over the size of the fine J&F will have to pay, according to prosecutors last week. The prosecutors said they were asking for a fine of 11.2 billion reais (\$3.4 billion). J&F proposed a payment about a 1 billion reais, the prosecutors said Friday.

Negotiations advanced on Tuesday, with representatives of J&F now agreeing that the company would pay a 4 billion reais fine, according to a person close to the talks. J&F didn't have an immediate comment on the status of the talks.

—Luciana Magalhaes

## PAKISTAN

### Chinese Nationals Abducted in Quetta

Armed men abducted two Chinese nationals in the city of Quetta in southwestern Pakistan on Wednesday, police said, a rare incident that is likely to raise security concerns around the country's many China-backed infrastructure projects.

The kidnapping comes as thousands of Chinese have moved to Pakistan over the past two years to support investment under Beijing's flagship One Belt, One Road infrastructure building program across Asia and Europe.

Three Chinese nationals, two women and a man, were leaving a language center when four armed men in a sedan accosted them and tried to force them into the car, police said. One of the women managed to flee, as the kidnappers drove away with the other two.

—Qasim Nauman and Saeed Shah

## CANADA

### Key Rate Is Left Unchanged at 0.50%

The Bank of Canada left its main interest rate unchanged at 0.50%, while sounding a positive note about recent economic indicators that point to "very strong" growth in the first quarter.

The central bank said it expects growth to tail off somewhat in the second quarter.

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## WORLD WATCH

### BRAZIL

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## MEXICO

### Foreign Investment Inflows Hit Record

Mexico received a record amount of foreign direct investment in the first quarter, defying fears the administration of U.S. President Donald Trump would discourage companies from risking capital south of the border.

Preliminary foreign direct investment was \$7.95 billion in the January-March period, up

0.6% from the preliminary amount reported for the year-earlier period and the most ever for a first quarter, according to the Economy Ministry.

—Anthony Harrup

## INDONESIA

### Deadly Blasts Rock Jakarta Bus Terminal

A police officer and a suspected suicide bomber were killed Wednesday in a pair of explosions that ripped through a busy bus terminal in the Indonesian capital, police said.

A spokesman for the Jakarta police said that the remains of the civilian fatality "might be the person" who carried a bomb. At least four other people were injured by the blasts, he said. He didn't disclose other details.

—Anita Rachman



The area of Quetta where two Chinese nationals were kidnapped.

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## WORLD NEWS

# Clashes Escalate in Southern Philippines

BY JAKE MAXWELL WATTS

Security forces closing in on a senior leader of the Abu Sayyaf terrorist group, who has pledged to create an Islamic caliphate in the troubled southern Philippines, clashed for a second day with militants who came to his rescue.

A combined police and military operation attempted on Tuesday to arrest the leader, Isnilon Hapilon, sparking the battle in the city of Marawi. The effort was unsuccessful and complicated by fighters from the Maute group, an organization aligned with Mr. Hapilon, who attacked the city, occupying buildings and waving a black Islamic State flag.

The fight took another twist Tuesday evening when a Roman Catholic bishop in Marawi said he received a call from the militants claiming to have taken several of his congregation and a priest hostage, according to the official news website of the Catholic Bishops' Conference of the Philippines. The militants threatened to kill the hostages if their demands for a cease-fire and safe passage out of Marawi weren't met, the Conference news service reported. There was no immediate confirmation from government officials.

President Rodrigo Duterte, who declared martial law in



Troops patrolled in Davao City on Wednesday after martial law was declared in Mindanao province.

the entire southern province of Mindanao late Tuesday while visiting Moscow, said Wednesday that skirmishes continued with the Maute group, "showing the group's capability to sow terror." He said that a local police chief had been beheaded by the group and that he would consider extending martial law to the entire Philippines if he felt it necessary.

Mr. Hapilon, 51 years old, leads a branch of another ter-

rorist organization, the Abu Sayyaf group, which is known for kidnapping and beheading foreign tourists. His faction, which Mr. Duterte has pledged to destroy, has preoccupied the military since 2014, when he publicly declared loyalty to Islamic State.

"I do think that Hapilon has taken on something of a symbolic importance," said Marc Singer, director of business intelligence at risk consultancy

PSA Group in Manila. "Central Mindanao is now a kind of complex chess board where the pieces are all in disarray and you have any number of disparate groups" fighting for influence.

Mr. Hapilon's group hails from the southwestern island of Basilan, but it has brought fighters to the main southern island in Mindanao and raised his profile by striking alliances with other militant groups.

Other elements have split off and conducted their own operations, some more ransom-hungry than Mr. Hapilon's overtly religious focus.

Lawlessness in Mindanao, home to around 22 million people, has become a concern for security services internationally as Islamic State's strongholds in the Middle East are destroyed. Dozens of fighters loyal to the group have fled to the Philippines to join local extremist gangs, seeking a way to continue their fight.

Several groups are "auditioning for recognition" by Islamic State, Alan Peter Cayetano, the Philippines' foreign secretary said during a press conference in Russia.

Abu Sayyaf started as a religious splinter group from an independence movement in the Muslim south, loosely allying itself with al Qaeda in the mid-1990s. Its tactics have varied, from kidnapping and murder, to a ferry bombing in 2004 and a bus bombing in Manila in 2005.

The Philippine armed forces, which received assistance from the U.S. after the Sept. 11, 2001, terror attacks, have periodically killed Abu Sayyaf leaders and splintered the group further. Now, it survives mostly on kidnappings for ransom and other illicit business, with Mr. Hapilon one of the few leaders with enough seniority to unite mem-

bers inside and outside Abu Sayyaf itself.

Mr. Hapilon's stature was boosted when Islamic State leadership anointed him as its "emir" in the Philippines. Philippine officials said Mr. Hapilon was wounded in a January airstrike, sparking speculation at the time that he might have been killed.

Mr. Hapilon is on the U.S. Department of Justice list of most-wanted terrorists worldwide with a reward of as much as \$5 million. He was personally involved in several kidnappings, including a 2001 incident when 20 people, including an American who was later beheaded, were taken from an island resort.

The Philippines' inability to dislodge groups such as Abu Sayyaf and Maute has alarmed its neighbors. In February, Australian Foreign Affairs Minister Julie Bishop said her country was readying itself for the possibility of Islamic State declaring a caliphate in the southern Philippines.

Yet many security experts play down the capability of Mr. Hapilon and his allies to set up a caliphate, arguing that Mindanao's militant groups are too splintered by ethnicity and ideology to gain the critical mass necessary to gain de facto control of a large amount of territory.

## Taiwan Ruling Advances Cause Of Gay Unions

BY TE-PING CHEN

Taiwan's top court ruled that current law defining marriage as exclusively between a man and a woman was unconstitutional, paving the way for the first same-sex marriage law in Asia.

Celebrations and protests broke out across Taiwan on Wednesday after the island's constitutional court ordered the legislature to change the law to permit gay civil unions within two years. If the legislature failed to act, the court said same-sex couples could register to marry in any case.

"Today is a watershed," said Chen Yi Chen, a 37-year-old lawyer in Taipei who said she and her girlfriend of six years had until recently not seriously talked of marriage because the prospect seemed so unlikely.

The plaintiff in Wednesday's case, Chi Chia-Wei, had pushed for more than three decades to advance same-sex marriage rights. The effort gained pace in recent years as Taiwan emerged as a beacon for gay-rights supporters in Asia, annually hosting a gay-rights parade that attracts tens of thousands of participants, some from around the region. President Tsai Ing-

wen, who was elected last year, has expressed support for same-sex marriage.

By early Wednesday evening, the news was the eighth-highest trending topic on China's Twitter-like Weibo, with users posting rainbow flags and hearts and at least one hashtag racking up more than 16 million views.

The court said the need to create "permanent unions of intimate and exclusive nature are equally essential to homosexuals and heterosexuals," citing freedom of marriage as important to safeguard human dignity.

Taiwan's greater tolerance for sexual minorities is unusual within Asia, particularly in countries with larger Christian populations and amid a rise of a more conservative Islam in Indonesia and other areas. Two men were publicly caned in Indonesia on Tuesday as punishment for having same-sex relations.

Neither same-sex marriage nor civil unions are recognized in mainland China. Still, the issue has proved polarizing even in Taiwan, with both supporters and opponents of same-sex marriage—including Taiwan's small, but vocal Christian population—staging large rallies last

year to support their positions.

In the run-up to the verdict, opponents staged protests and circulated commentary online, including in the form of satirical cartoons, one which depicted a large building labeled "Marriage" cracking after a gray column was removed and replaced with one painted in rainbow stripes.

The self-ruled, democratized

cally governed island split from mainland China after the civil war with the Communists ended in 1949.

Beijing has increasingly worked to sideline Taiwan, especially following the election of Ms. Tsai, whose Democratic People's Party officially supports independence. This week, under pressure from Beijing, Taiwan was denied ob-

server status at the World Health Assembly in Geneva.

Advocates for gay marriage in Taiwan say they hope the move can help inspire other nations in Asia.

"We have a very tricky diplomatic position," said Wayne Lin, chair of the Taiwan Tongzhi (LGBT) Hotline Association, a support group.

"But I think Taiwan can

show that we are a country who cares about human rights—and we can show that LGBT rights isn't something Western, it's something for all Asian countries."

On her official Facebook page, Ms. Tsai appealed for tolerance and understanding in the wake of the verdict.

—Jenny W. Hsu contributed to this article.



Supporters of same-sex marriage cheered the Constitutional Court's ruling outside the Legislative Yuan in Taipei on Wednesday.

## DEBT

*Continued from page A1* among ministries, banks and companies. That makes it less vulnerable to the outside world's assessment of its credit risks.

The downgrade news triggered an early sell-off in Chinese stocks on Wednesday, with shares in Shanghai falling more than 1% before recovering.

David Rubenstein, co-founder and co-CEO of **Carlyle Group**, in an interview in Beijing on Wednesday said Carlyle, which has invested \$1 billion a year in China on average over the past four years, is increasing its investment. "The U.S. was downgraded a few years ago as well, and that hasn't stopped us from investing in the U.S.," he said.

Yet the downgrade amplifies growing unease among foreign institutions about the Asian giant's debt levels, about which the International Monetary Fund, World Bank and Bank for International Settlements, among others, have long expressed concern. China's foreign debt at \$1.42 trillion is tipped to rise this year but remains, at 13% of gross domestic product, among the lowest globally by

### Outside View

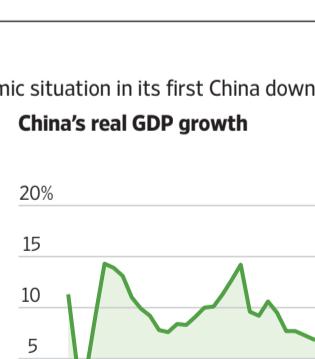
Moody's cited a worsening economic situation in its first China downgrade since 1989.

#### Moody's rating action on Chinese government



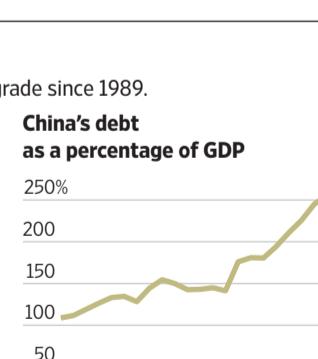
Sources: Moody's Investors Service (ratings); National Bureau of Statistics (GDP growth); Bank for International Settlements (debt-to-GDP ratio)

#### China's real GDP growth



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#### China's debt as a percentage of GDP



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the early 1990s. As with Japan, heavy capital-spending levels have been central to China's growth.

A sharp run-up in real-estate prices is one common point between China of today and Japan of the late 1980s.

The nation's real-estate speculators soon paid the price for their enthusiasm. By the early 1990s, land prices were beginning a 15-year string of annual declines.

The collapse of the bubble exposed vulnerabilities in poorly regulated corners of Japan's financial system, another potential parallel with today's China.

Yet another parallel: Around 1990, it was clear that Japan's population was destined to start falling in about 15-20 years' time, which is in fact what happened. Likewise, the United Nations projects that China's population will peak around 15 years from now, in the early 2030s, and shrink sharply thereafter.

—Andrew人民

### China's Downgrade Echoes Japan's Path

Some economists have long warned that China faces the same fate as Japan, with a debt-fueled boom followed by years of stagnation as the country works its way through the hangover.

After Moody's decision to downgrade China on Wednesday, the two countries at least now have sovereign credit ratings, at A1, to match.

But as China grapples with some of the same problems Japan faced a quarter of a century ago—from bubble-prone property markets to fragile banks—it's downgrade to the same credit rating is a reminder that it is still unclear whether it can escape the sort of prolonged economic malaise that has afflicted its neighbor.

Concerns about China's economy voiced by the likes of Moody's have some echoes of the problems Japan faced by

started citing a "new normal" of slower, better-quality growth, but such talk has subsided, giving way to a renewed emphasis on growth and stability in advance of a once-in-five-years Communist Party

Congress this fall. China's economy grew 6.7% year on year in 2016, its slowest pace in a quarter-century.

—Lingling Wei, Liyan Qi and Grace Zhu contributed to this article.

## U.S. NEWS

## White House Budget Faces Swift Pushback

The president's plan gets a cool reception as lawmakers bristle at cuts to programs

President Donald Trump faced swift resistance from Democrats and a range of Republicans on Capitol Hill after

*By Kate Davidson,  
Kristina Peterson  
and Natalie Andrews*

offering a 10-year plan to balance the federal budget that depends heavily on cuts to government safety-net programs and expectations of a big gain in economic growth.

The White House budget proposal for the fiscal year that begins Oct. 1 would cut federal spending by \$4.5 trillion over 10 years. But it leaves mostly untouched the big entitlement programs—Social Security and Medicare for retirees—and proposes increases to infrastructure spending, a new parental-leave program and a short-term boost to military spending.

With those priorities set—in addition to the shared Republican goal of cutting taxes—the White House offered up significant reductions in other spending programs to further the aim of reducing budget deficits. But the call for rolling back programs that touched their constituents made lawmakers bristle.

The proposal, which serves as a recommendation to Congress, is likely to be largely rewritten when lawmakers craft their own budget resolutions.

"I hate to say it, but I would say the budget was dead before the ink was dry," Rep. Don Young (R., Alaska), who opposes the budget's elimination of two programs in his state.

Payments to Medicaid, the



Mick Mulvaney, the president's budget director, testified before lawmakers on Wednesday.

### Mnuchin Calls for Debt-Limit Increase

Treasury Secretary Steven Mnuchin asked Congress to increase the debt limit—without policy conditions attached to it—before lawmakers leave for their summer recess.

Mr. Mnuchin told the House Ways and Means Committee on Wednesday that he favors a

so-called clean debt ceiling increase.

That preference is in opposition to the position that Republicans have taken for the past six years, when they have tried to pair spending cuts with debt-limit increases.

Congress is scheduled to leave Washington around July 28 and return after Labor Day in September.

*—Kate Davidson  
and Richard Rubin*

federal-state health program for the poor, would be cut by more than \$600 billion over a decade from levels projected under current law in addition to proposed Medicaid cuts under the House bill repealing and replacing much of the Affordable Care Act.

The food-stamp program would be cut over 10 years by \$193 billion, the student-loan program by \$143 billion, dis-

ability payments by \$72 billion and farm subsidies by \$38 billion.

"The proposed cuts to some federal programs are not mere shavings; they are rather deep and harmful to my district spanning Kentucky's Appalachian region and other rural, impoverished parts of the country," said Rep. Hal Rogers (R., Ky.), a former chairman of the House Appropriations

Budget Committee.

Democrats lambasted the overall budget proposal.

"This is the budget you write if you think working families have it too easy," Sen. Ron Wyden (D., Ore.) said.

On Wednesday, White House budget director Mick Mulvaney said the administration is open to extending the 10-year budget-scoring window for its tax plan to get around congressional rules that forbid bigger deficits after a decade.

That move might help Republicans get their tax and fiscal policies to comply with congressional budgeting rules that would otherwise limit them.

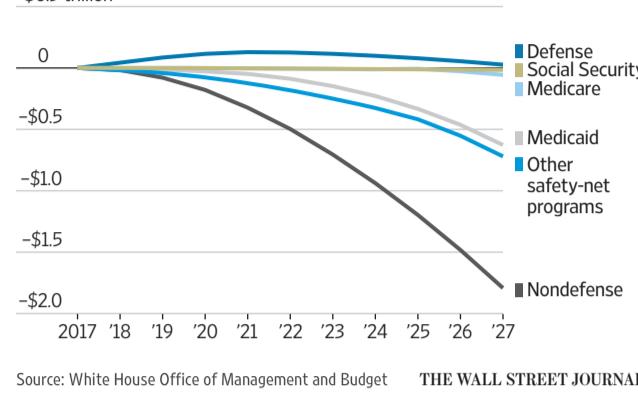
In all, nondefense spending as a share of the economy would fall to just 1.5% by the end of the next decade, well below the lowest level in records going back to 1962.

Besides wide-ranging spending reductions, the proposal depends on a projection that

### Spending Trends Under Trump

President Donald Trump proposes balancing the budget by cutting Medicaid and other programs while largely maintaining or increasing funding levels for defense and Social Security.

#### Cumulative change in spending



Source: White House Office of Management and Budget

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economic growth will reach 3% by 2021 and stay there through 2027, bolstering government revenue and holding down the need for support programs like unemployment insurance.

That growth projection is more aggressive than the Congressional Budget Office projection of 1.9% over a decade or the Federal Reserve's 1.8% projection. It also assumes the country's economic expansion won't be interrupted by another economic downturn.

The plan drew praise from some Republicans for proposing to balance the budget over 10 years and boosting military spending. GOP lawmakers have also backed overhauling federal funding for Medicaid in previous congressional budgets. Still, many balked at cuts to foreign aid, farm subsidies, health-care programs for low-income families and other programs that mattered back home.

"It's nothing new—it's just a lot of people who don't know what the hell is going on in farm country," said Senate Agriculture Committee Chairman

Pat Roberts (R., Kansas), who objected to proposed cuts for farm subsidies and new limits on crop insurance, as well as cuts to the Supplemental Nutrition Assistance program, also known as food stamps.

With Mr. Trump traveling, his deputies were left to defend the plan.

Mr. Mulvaney said Monday the plan will boost economic growth by adding workers to the labor force, in part by requiring them to have jobs to qualify for assistance programs such as food stamps, in addition to funding a new parental-leave program.

Despite the resistance he will surely face, the president has important allies in Congress; most notably House and Senate leadership with a mutual incentive to ensure the Republican economic agenda doesn't stall in Congress.

"We finally have a president who is willing to actually balance the budget," said House Speaker Paul Ryan (R., Wis.).

*—Peter Nicholas  
and Richard Rubin  
contributed to this article.*

## Winners and Losers In the Proposed Budget

The president's budget proposal serves as a blueprint for his goals and priorities. Here is how some departments would fare:

### Defense

The administration is asking for \$640 billion in defense spending, more than \$50 billion over current congressional budget caps, to pay for modernization, readiness and operations.

One of President Donald Trump's most prominent defense spending proposals during the campaign was to build up the Navy to at least 350 ships from more than 280 in the fleet now. The proposed budget makes small inroads on that score, including funding toward two Virginia-class submarines, two Aegis destroyers and a littoral combat ship.

*—Gordon Lubold*

### State

The proposal includes a 32% decrease to the State Depart-

ment and U.S. Agency for International Development budget to \$37.6 billion from \$54.9 billion. The budget also includes a 29% cut to foreign assistance, to \$25.3 billion.

The U.S. would contribute \$5.3 billion in humanitarian assistance funds in 2018 under the proposal, a 31% decrease, though officials said the U.S. would still contribute the most in this area by at least about \$2 billion.

The full budget would significantly cut back on contributions to international organizations, which includes the United Nations, international peacekeeping efforts and the World Health Organization and others. Bilateral economic assistance, foreign military financing and global health funding would also face deep cuts.

*—Felicia Schwartz*

### Interior

The proposed \$11.7 billion budget for the Department of

the Interior raises spending for national parks and oil and gas development, while taking the ax to climate change and other science programs in a plan that has outraged environmental groups.

The spending plan represents an 11% decrease from last year, and if enacted would be the lowest budget for the land and water agency in five years. Hardest hit would be agencies like the U.S. Geological Survey, whose staffing would be slashed by nearly one-fifth.

*—Jim Carlton*

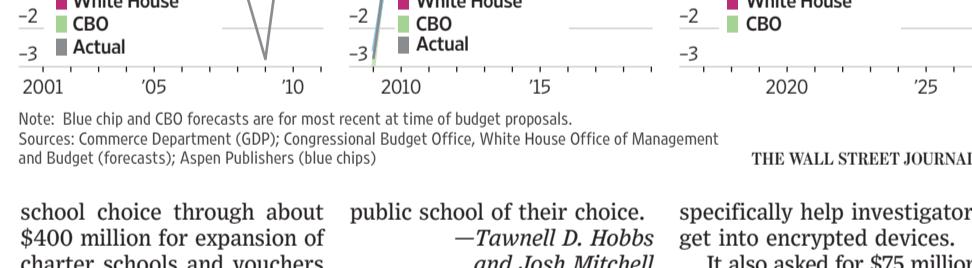
### Education

A significant cut to college work-study programs and elimination of funding for certain teacher-training and after-school programs are among \$9.2 billion in cuts proposed for the U.S. Department of Education, with some savings being shifted to help fund school-choice initiatives.

The budget would bolster

### Fiscal Forecasts

Compared with his recent predecessors, President Donald Trump's economic forecasts are significantly more optimistic over a decade than those of private-sector and government economists.



Note: Blue chip and CBO forecasts are for most recent at time of budget proposals.

Sources: Commerce Department (GDP); Congressional Budget Office, White House Office of Management and Budget (forecasts); Aspen Publishers (blue chips)

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school choice through about \$400 million for expansion of charter schools and vouchers for low-income students to attend private and religious schools.

An additional \$1 billion in Title 1 funding, typically targeted for schools with high poverty rates, would be used for a new grant program focused on open enrollment to allow students to attend the

public school of their choice.

*—Tawnell D. Hobbs  
and Josh Mitchell*

### Justice

The administration proposed 300 new federal prosecutors to combat violent crime and prosecute more immigration violations. It also proposed adding \$100 million for national security priorities, including 20 new cyber agents at the FBI and 80 positions to

specifically help investigators get into encrypted devices.

It also asked for \$75 million, including 450 positions to help process a backlog of immigration court cases. That includes 75 new immigration judges. The agency's overall budget is down 3%, which officials attributed to one-time construction cost reductions and money left over from prior years.

*—Aruna Viswanatha*

## Former Federal Prosecutor Interviewed for Director's Job at FBI

BY DEL QUENTIN WILBER

Top Justice Department officials recently interviewed a former U.S. attorney to be the next FBI director, as President Donald Trump's administration continues its search for someone to lead the law-enforcement agency.

That search has been less public during Mr. Trump's current overseas trip, but Attorney General Jeff Sessions and Deputy Attorney General Rod Rosenstein spoke last week with Kenneth Wainstein, a top national security official in the GOP administration of former President George W. Bush, according to a person familiar with the selection process.

Mr. Wainstein, a Republican and widely respected defense lawyer, is seen as having the bona fides and experience to lead the Federal Bureau of Investigation after Mr. Trump's abrupt firing of James Comey as the agency's director on May 9, according to Justice Department officials. He served as U.S. attorney for the District of Columbia during



ALEX WONG/GETTY IMAGES

Kenneth Wainstein testified earlier this year before the Senate Judiciary Committee in Washington.

part of Mr. Bush's presidency. But at least one action in Mr. Wainstein's background could pose a challenge to his nomination. In August, Mr. Wainstein and 49 other former Republican national security officials signed a letter saying

Mr. Trump lacked the "character, values and experience to be president."

Mr. Wainstein couldn't be reached for comment Wednesday.

The search for a new director continues in the aftermath

of Mr. Comey's dismissal and the fallout over the White House's evolving explanations for the firing.

Mr. Trump, a Republican, has been accused of asking Mr. Comey to back off an investigation into Michael Flynn, the

president's first national security adviser, an allegation Mr. Trump disputes. Mr. Flynn resigned in February after giving false statements about his communications with Russia's ambassador to the U.S.

Mr. Comey was spearheading the federal investigation into Russia's alleged interference in the 2016 presidential campaign and whether associates of Mr. Trump colluded with Moscow.

Mr. Trump has denied any form of collusion and called the federal investigation, now led by a Special Counsel Robert Mueller, a "witch hunt." Russian officials have denied meddling in the election.

Mr. Trump's administration hasn't said when it plans to complete its search for a new director. In the days after Mr. Comey's firing, the Justice Department interviewed several candidates to act as an "interim director" until a permanent director takes office.

Those interviewed included Acting Director Andrew McCabe, who served as Mr. Comey's deputy. He has been

running the bureau since Mr. Comey was fired, and it is now unclear if the administration still plans to install an interim chief before a permanent successor takes over.

Mr. Sessions has interviewed at least 10 candidates for the job, according to Justice Department officials. Mr. Trump and Mr. Sessions sat down with four top candidates last week before Mr. Trump's departure for his first overseas trip as president.

Those interviewed at the White House included Mr. McCabe, former Sen. Joe Lieberman (D., Conn.), former Republican Oklahoma Gov. Frank Keating and Richard McFeely, a former top FBI official.

A number of candidates have taken themselves out of the running, including Sen. John Cornyn (R., Texas), Rep. Trey Gowdy (R., S.C.) and former Justice Department official Alice Fisher.

The FBI's top job has generally gone to a former top federal prosecutor or senior law-enforcement official, not a political figure.

## U.S. NEWS

# Fight Over Speech Goes To the States

By DOUGLAS BELKIN

Demonstrators have chased away conservative speakers over the past few months at the University of California, Berkeley, and Middlebury College in Vermont.

Taking action to avoid similar scenes, universities in Illinois and Texas rescinded speaking invitations this month to a Republican senator and a Nobel Prize-winning scientist before they even showed up.

Now, state legislatures, most led by Republicans, are advancing bills they say are intended to support free speech. The laws include measures to suspend troublemakers, remove free-speech zones that limit protests to small areas on campus, and cut off money to schools that don't protect free speech.

"There's been censorship of free speech on campuses around the country," said Jesse Kreme, a Republican state representative in Wisconsin who is sponsoring a bill there. "We should have a free marketplace of ideas; people shouldn't be shouted down for expressing themselves."

In the past few months, governors have signed legislation protecting free speech on campus in Colorado,

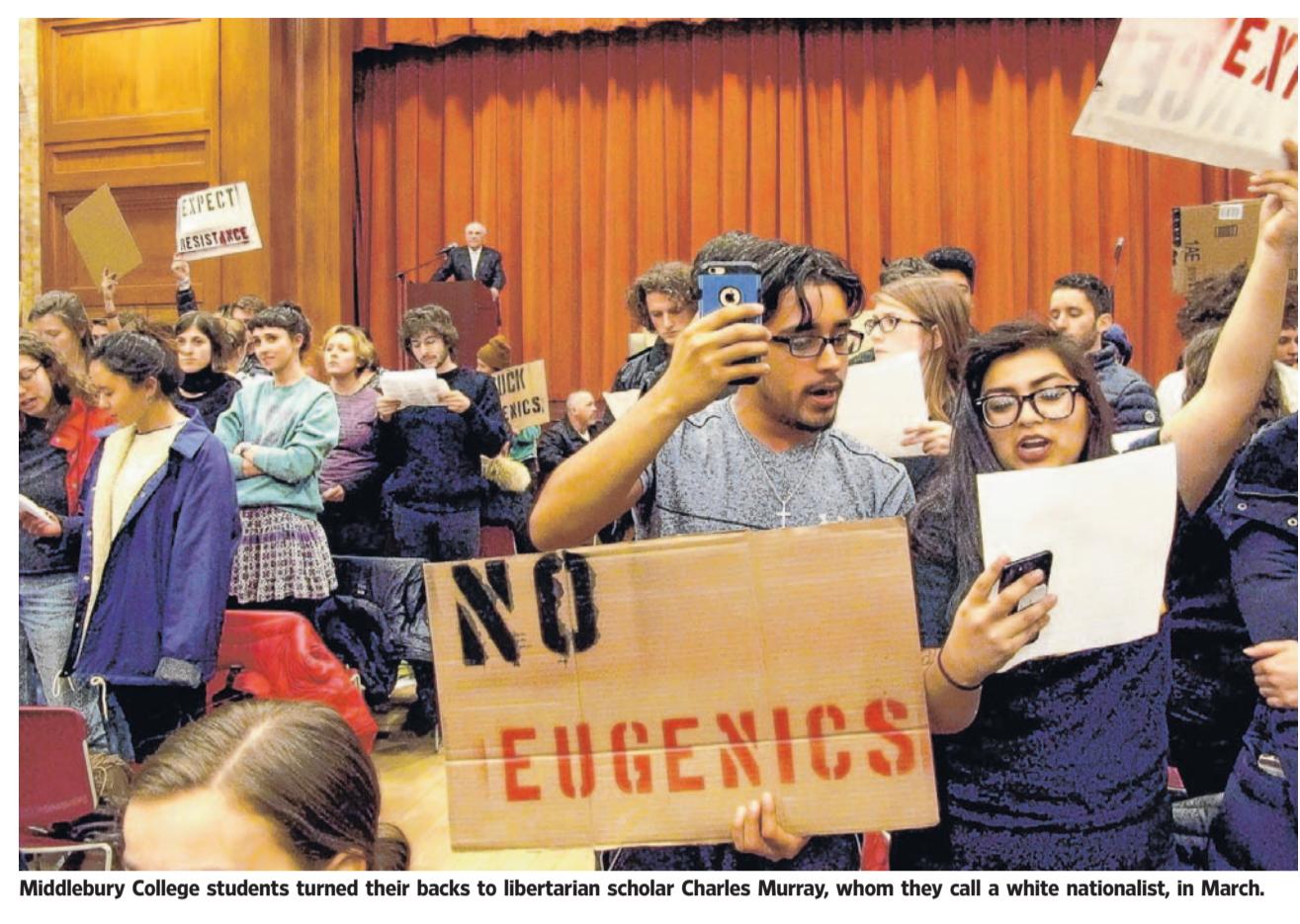
Tennessee, Utah and Virginia. Meanwhile, Republican legislators have proposed bills in Illinois, Wisconsin, Texas, California, North Carolina, Michigan, Louisiana and Georgia.

Republicans control the legislature in three of the four states where governors—two of them Democrats—have so far signed the bills. The GOP controls the legislature in six of the eight states where such legislation has been proposed.

Caiden Nason, the president of the Democratic-student group on the Berkeley campus, said he thought the legislation proposed for California was overwrought. He believes any speaker who comes to campus with provocative views needed to come prepared.

"If you can't handle someone yelling at you then you probably shouldn't speak here," he said. "People are going to be loud sometimes."

Much of the proposed legislation is based on a model bill published in January by the Goldwater Institute, a conservative-leaning think tank in Phoenix. It prohibits school administrators from bowing to political pressure and rescinding invitations to controversial speakers, mandates that every freshman be taught about the campus's free-speech policy and require schools to dis-



Middlebury College students turned their backs to libertarian scholar Charles Murray, whom they call a white nationalist, in March. LISA RATHKE/ASSOCIATED PRESS

pline students who twice interfere with the free speech rights of others.

By interference, the model law refers to "protests and demonstrations that infringe upon the rights of others to engage in or listen to expressive activity."

The proposal nullifies any speech codes, some of which restrict protests to designated areas on campus. It also requires an annual report summarizing how school administrators handled free-speech issues.

"You want to carry a sign and march on the sidewalk? You can do that right up to the

point where you block someone else's ability to speak," said Jonathan Butcher, co-author of the Goldwater Institute's model legislation. "If you want to ask an antagonistic question, great, we want that to happen, but you cannot shout down a speaker and force them to leave the room."

The American Association of University Professors said this month it supports freedom of expression on campus but opposes any legislation "that interferes with the institutional autonomy of colleges and universities by undermining the role of faculty, administration and governing board

in institutional decision-making."

In Wisconsin, where a bill based on the Goldwater Institute model was fiercely debated in a public hearing last week, critics have accused lawmakers of overreach.

"I think there is a concerted effort by right-wing groups in this country to try and make hay on this issue," said Matthew Rothschild, executive director of the Wisconsin Democracy Campaign, which promotes government transparency.

"If someone yells 'You lie,' at a speaker, is that enough to get them suspended?" Mr. Rothschild asked. "How about if they laugh derisively?"

The bill is still in a House committee but Mr. Kreme said he expected it to be passed out of the Republican-controlled legislature and signed into law by GOP Gov. Scott Walker next month.

In California, Republican Assemblywoman Melissa Melendez has introduced an amendment to the state constitution aimed at protecting speakers on public and private campuses. Her bill is based on the Goldwater model. Included is a mechanism that would allow the state to cut a campus's budget if it doesn't comply.

## Fed Signals It's Ready to Lift Rates

By NICK TIMIRAO

Federal Reserve officials expected at their policy meeting this month that it would "soon be appropriate" to raise short-term interest rates again, according to minutes of the gathering released Wednesday, a signal the U.S. central bank could lift its benchmark rate at its next gathering in June.

The Fed also moved toward a consensus on a plan to shrink its \$4.5 trillion in holdings of Treasury and mortgage securities later in the year by gradually allowing increasing amounts of those securities to mature without reinvesting them.

Officials were inclined to stick to their plan even though the economy appeared to stumble in the first quarter. That slowdown was seen as transitory, the minutes said. Moreover, some officials expressed concern about recent softness in inflation, but not enough to force them to scrap plans to raise rates twice more this year.

The next meeting is June 13-14, which will be followed by a press conference from Fed Chairwoman Janet Yellen.

"Most participants judged that if economic information came in about in line with their expectations, it would soon be appropriate for the committee to take another step in removing policy accommodation," the minutes said.

Before Wednesday's release of the account of May's meeting, traders in futures markets



Officials of the Fed, whose Washington headquarters is shown above, will meet on rates June 13-14.

placed an 83% probability on a Fed rate increase by June, according to CME Group. The minutes are likely to solidify those expectations.

Fed officials left their benchmark short-term interest rates unchanged within a range between 0.75% and 1% at the meeting May 2-3. Several Fed officials in recent weeks have said they believe the economy will still be strong enough to warrant two more rate increases this year.

"Although incoming data showed that aggregate spending in the first quarter had been weaker than participants expected, they viewed the slowing as likely to be transitory," the minutes said. Officials expected continuing job

gains, rising household income and wealth and buoyant consumer sentiment to bolster spending in the months ahead. "Participants generally indicated their assessments of the medium term economic outlook had changed little since the March meeting."

With their forecasts stable, officials effectively believed they had a green light to move again.

Inflation has wobbled in recent months, a cause of concern for some officials, but one most were prepared to look past for now. The Fed's preferred inflation gauge, the price index for personal-consumption expenditures, briefly surpassed the Fed's annual 2% target in February but posted

a greater-than-expected drop in March, with annual prices up 1.8%. A separate inflation gauge released since the May meeting, the Labor Department's consumer-price index, also showed a lower trajectory in April. Prices excluding food and energy were up 1.9% on the year, the first time the annual gain in core prices had been below 2% since October 2015.

Officials generally believed the deceleration in price pressures would prove transitory, with inflation stabilizing around 2% over the medium term amid sustained improvement in the labor market. But some officials expressed uncertainty about the greater-than-expected weakness.

## Insider Tips Alleged In Medical Stocks

By BRODY MULLINS

Federal prosecutors announced insider-trading charges against a government official, two hedge-fund investors and a Washington consultant for allegedly conspiring to trade health-care stocks based on information about imminent policy changes by the U.S. government that hadn't yet been made public.

The charges on Wednesday, filed by the Manhattan U.S. attorney's office, relate to tips allegedly relayed by the official from a key government health agency, the Centers for Medicare and Medicaid Services, to a consultant in the political-intelligence business, David Blaszcak.

The tips concern information about government-funding levels for cancer treatments and kidney dialysis from 2012 to 2014, according to prosecutors.

Mr. Blaszcak then allegedly relayed that nonpublic information to two investors, Theodore Huber and Robert Olan, who worked at the New York-based hedge fund Deerfield, prosecutors alleged.

According to the prosecutors, the hedge-fund investors used the nonpublic information to recommend trades in the stocks of four health-care companies that could be affected by the coming announcements from the agency. The trades resulted in more than \$3.9 million in illegal

profits, according to the Securities and Exchange Commission, which announced parallel civil charges on Wednesday.

The hedge fund paid firms that employed Mr. Blaszcak at least \$193,000, according to the SEC. The indictment by the Manhattan U.S. attorney says the firms were paid more, at least \$263,000.

Mr. Huber "did absolutely nothing wrong," said his lawyer, Barry Berke. Mr. Berke said that Mr. Huber's research was based on detailed and rigorous analysis. Lawyers for Messrs. Blaszcak, Olan and Christopher Worrall, the CMS official, didn't respond to a request to comment.

In a statement to The Wall Street Journal in 2014 given in connection with an article it published that year, Mr. Blaszcak said: "I only use public information in preparing all my reports," and "I am proud of my record, and if needed, will vigorously fight any false allegation."

A CMS spokesman declined to comment. A Deerfield spokesman said it "is committed to maintaining a strict culture of compliance and the highest ethical standards. We are cooperating fully with the government's investigation."

In political intelligence, lobbyists, former government officials and other insiders mine the halls of Congress and federal agencies for nonpublic information that could be used to profit from trading stocks.

## U.S. WATCH

## HOUSING

### Sales Decline Amid Shortage of Homes

Home sales declined in April, a tepid start to a spring selling season marked by a dearth of homes available for purchase.

Sales of previously owned U.S. homes last month fell 2.3% from March's revised level to a seasonally adjusted annual rate of 5.57 million, the National Association of Realtors said Wednesday.

This spring selling season promises to be the most competitive in years, with a flood of new buyers entering the market at a time when inventory is near 20-year lows. April's data suggest the home shortage could mean weaker sales activity than otherwise would be the case, based on the strength of the economy.

"Demand is easily outstripping supply in most of the country and it's stymieing many prospective buyers from finding a home to purchase," said Lawrence Yun, NAR's chief economist. The supply of homes on the market has fallen year-over-year for 23 consecutive months, according to NAR. There was a 4.2-month supply of homes on the market at the end of the month, down from 4.6 months a year ago.

—Laura Kusisto and Sarah Chaney

## PHILANTHROPY

### University of Chicago Gets \$100 Million Gift

The University of Chicago on Wednesday announced a \$100 million gift to support research into the human immune system.

The donation comes from the family of Craig and Janet Duchossois.



CELEBRATION: The USS Kearsarge moves up the Hudson River as part of New York's Fleet Week.

## VERMONT

### Governor to Veto Marijuana Bill

Vermont Gov. Phil Scott said Wednesday he is vetoing a bill that would have made the state the first to legalize marijuana through legislation rather than a ballot measure, but he also left the door open for legalization.

The bill, passed by the Vermont House and Senate, would have made it legal for adults 21 and over to possess up to an ounce of marijuana and grow a limited amount starting in mid-2018. The bill also called for a commission to propose yet-more legislation that could have created a taxed, regulated market later on.

The bill passed by a slim margin in the house, making it difficult to overturn the veto.

—Jon Kamp

sois, whose holdings include Churchill Downs, where the Kentucky Derby takes place. The privately held **Duchossois Group Inc.** is valued in excess of \$3 billion, according to its website. The gift comes as the wealth gap expands between the nation's wealthiest schools and other, less well-off institutions. In 2014, the

40 richest schools held two-thirds of total cash and investments at four-year institutions, according to Moody's Investors Service.

—Douglas Belkin

## IN DEPTH

## RETAIL

*Continued from Page One*  
next season.

Now, competitors with high-tech, data-driven supply chains can copy styles faster and move them into stores in a matter of weeks. Online marketplaces drive down prices, and design details such as nicer buttons and richer colors are less apparent on the internet. Social media adds fuel to the style churn—consumers want a new outfit for every Instagram post.

"The rules of the game have changed," said Janet Kloppenburg, president of JK Research, a retail-focused research firm. "It's not just about product anymore. It's also about speed and pricing."

Mr. Drexler's plan is to emphasize lower prices, pivot toward more digital marketing and adopt a more accessible image. "We became a little too elitist in our attitude," he said.

Many visionaries focus on doing what they do best, even when the ground shifts beneath them. From newspapers to television, successful companies have been upended by disruptive technologies. Facebook Inc. is now the world's largest publisher; Netflix Inc. is worth twice as much as CBS Corp.

"The incumbent leaders never see it coming," said Clayton Christensen, the Harvard Business School professor who introduced the theory of disruptive innovation 20 years ago. "They focus on their best customers and try to provide what they need, but the customers who first defect [to new technology] are usually the least profitable."

Mr. Drexler, known as the "merchant prince," built some of America's most recognizable apparel brands, including Old Navy, Banana Republic and most recently Madewell. He focused on details such as the feel of the fabric, the weight of the buttons and the plaid inside waistbands, according to former executives who worked with him at J.Crew and Gap. Higher quality allowed J.Crew to charge a premium for its casual, preppy styles.

The New York City native, who doesn't have his own Instagram, Facebook or Twitter



BRIAN ACH/GETTY IMAGES

**Mr. Drexler said J.Crew gave a perception of being higher priced than it was. Above, performer Sandra Bernhard models J.Crew.**

account, was sharing thoughts with employees on a loudspeaker—hooked up through his phone—before Twitter was launched. He paid attention to firsthand shopper feedback on frequent visits to stores long before Amazon.com Inc. was collecting user data. He was also selling clothes online before many other specialty retailers. Nearly half of J.Crew's sales now come from the web.

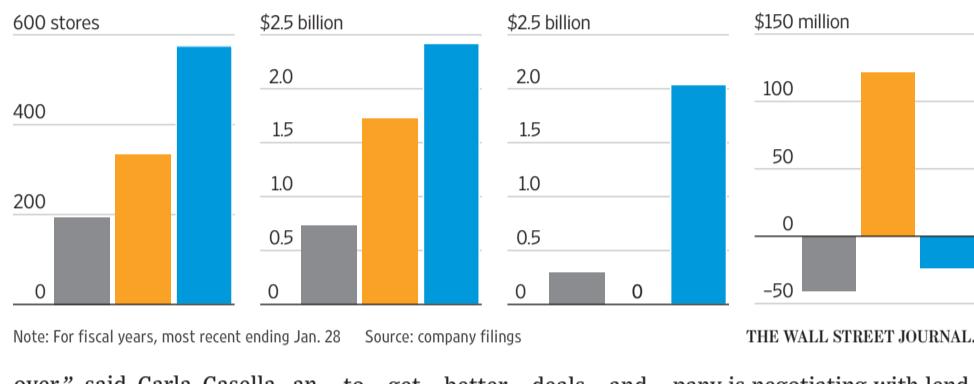
But Mr. Drexler didn't appreciate how the quality of garments could easily get lost in a sea of options online, where prices drive decisions, or how social media would give rise to disposable fashion. Online, price has more impact than the sensory qualities of clothing. "You go into a store—I love this, I love this, I love this," he said. "You go online and you just don't get the same sense and feel of the goods because you're looking at a picture."

J.Crew has about 460 stores, a smaller base than many other chains that are now shrinking their footprints. But it has still struggled as more shoppers compare prices online and buy less expensive, trendy clothes rather than a lasting wardrobe. Amazon.com and other algorithm-based websites can change prices by the hour based on demand, and the variety of options makes it easy to mix and match brands.

"The days of people wearing head-to-toe J.Crew are

## Fashion Do's and Don'ts

J.Crew Group's stores and revenue have increased since Mickey Drexler became CEO in 2003, but its debt has soared since a leveraged buyout in 2011, and it recorded a loss in 2016.



Note: For fiscal years, most recent ending Jan. 28  
Source: company filings

over," said Carla Casella, an analyst at J.P. Morgan Chase & Co.

Zinniah Munoz, a 20-year-old makeup artist in New York City, said she would rather buy a style at a lower price than pay extra money for a brand name. "I'm always vigilant of not posting the same style twice" on Instagram or Facebook, she added.

At an industry conference in 2010, Mr. Drexler played down the impact of technology on prices, arguing that quality products are the key to success: "At the end of the day, I think the franchise lasts as long as the creative product gets flown through."

Today, with nearly two billion people using Facebook every month, he feels differently: "You cannot be successful without being obsessed with the product, obsessed with social media, and obsessed with digital," he said. "Retail is now about all that."

Mr. Drexler said he hasn't given up on quality. Instead, he is now lowering prices on about 300 items and creating an analytics team dedicated to optimizing prices for each garment.

"We're being much more competitive in our pricing," he said. "We're not going to allow our competitors to take from us."

Madewell, which caters to younger shoppers and offers cheaper prices, has outperformed the J.Crew brand, but represents only about 14% of the group's annual revenue.

Mr. Drexler is also expanding the company's supply base beyond predominantly China

to get better deals and shorten the time it takes to get products into stores.

The moves are aimed at keeping prices consistent, rather than unloading leftover inventory through discounts, and at retuning J.Crew's identity as an affordable and accessible brand for everybody—not just the fashion-forward crowd.

Last month, Mr. Drexler cut 250 jobs, primarily from headquarters, and said he would part ways with Jenna Lyons, the group's longtime creative chief who was the driving force behind J.Crew's most high-price and daring styles, such as sequined blazers and feather skirts.

Mr. Drexler is also putting more of the brand's resources behind digital marketing, and shifting away from a one-size-fits-all monthly catalog. Mailings will be targeted based on customer data gleaned from the company's online business.

The New York-based company is carrying more than \$2 billion of debt and has less than \$150 million in cash, following Mr. Drexler's leveraged buyout in 2011 with TPG Capital and Leonard Green & Partners. It has paid its past three interest payments by issuing new debt.

To buy time, Mr. Drexler and his fellow directors performed a complicated financial maneuver that put the company's brand and intellectual property out of the reach of debtholders. Investors are fighting the moves in court, arguing it is tantamount to a default.

At least \$560 million of debt is due in 2019. The com-

pany is negotiating with lenders to push back the due date and lower its debt load by offering to swap some of the debt for equity.

"It's unclear whether they will come to an agreement," said Raya Sokolyanska, an analyst at Moody's. "It would still leave the company highly leveraged," adding that J.Crew's capital structure is unsustainable.

Private-equity firm TPG's first big bet on J.Crew was in 1997, when it acquired a majority stake. It recruited Mr. Drexler to run the business in

### Shoppers were put off by \$800 skirts and \$1,900 sweaters in J.Crew Collection.'

2003 after cycling through four CEOs in five years. By the time TPG sold the last of its shares in 2009, the firm had made more than seven times its investment.

Mr. Drexler had nearly tripled revenue and transformed what was largely a catalog business by going in the opposite direction of his predecessors and competitors. He increased prices and elevated quality—even creating a library at headquarters to document the unique hues the brand invented each season.

When sales slipped in 2010, TPG swooped back in. In 2011, the firm partnered with Leonard Green and took the company private in a \$2.8 billion deal.

In 2014, TPG and Leonard Green were negotiating a sale of the company to Uniqlo owner Fast Retailing Co. while at the same time hiring bankers for a potential IPO, when clothing sales began to fall again. The sale plans evaporated, and by the end of the year the company wrote down the value of its stores by more than \$500 million and its brand name by \$145 million.

TPG co-founder David Bonderman recently acknowledged J.Crew and its peers are struggling with declining mall traffic and the shift to online shopping. "The internet has proven much more resilient and much more important than most of us thought a decade ago," he said at a conference this month.

In an email, TPG co-founder James Coulter wrote, "We believe Mickey and the J.Crew management are getting the strategy and team in place to position J.Crew to succeed in this new world."

In recent years, customers have become closely attuned to prices. After sales began to fall, Mr. Drexler said he addressed style problems—such as "boxy" cuts that were unpopular among J.Crew customers—and quality issues, particularly pilling cashmere and T-shirts with thin fabric. Still, the company had to offer discounts of 40%-50% to move inventory.

J.Crew eventually determined shoppers were looking for better value and that many people were put off by the \$800 skirts and \$1,900 sweaters in the "J.Crew Collection"—an expensive line spearheaded by Ms. Lyons featured prominently in marketing and window displays, even though it represented a small portion of merchandise.

"We gave a perception of being a higher-priced company than we were—in our catalog, online and in our general presentation," said Mr. Drexler. "Very big mistake."

Ms. Lyons didn't respond to requests to comment.

Some of the quirky designs were too much for Tricia Louvar, a 42-year-old writer and illustrator in Sisters, Ore. She had shopped at J.Crew in the past, but began finding the clothes increasingly impractical and unaffordable. In a widely shared open letter to Ms. Lyons in 2015, she wrote:

"I still can't wrap my head around the price of an 'everyday outfit,'" which she tallied up at \$596 and said was equivalent to the price of a new computer or 298 school lunches.

In April, Mr. Drexler named Somsack Sakhounmuong, who has been with the company since 2001, to the post of chief design officer, but he won't take the high-profile role that Ms. Lyons had. J.Crew "won't be about any designer," Mr. Drexler said. "We're getting back to being who we are—much more comfortable, approachable, democratic and friendly."

Ms. Louvar said she returned to a store a few weeks ago for the first time in two years and bought several new pieces. "The prices felt more reasonable," she said. "It was more like the J.Crew I remember."

Samantha Bombel and Bret Francis got their streak restored.

alive after she was grounded and he confiscated her phone—by borrowing a friend's phone to log in.

Mr. Whalen and his wife, Rebecca, hit 100 days on their own streak in April. "I don't know that we actually went into it with the notion that we were going for a streak," says Mrs. Whalen, 43. "It's his way of kind of trying to keep that spark alive."

Kim Kroll, 43, a high-school teacher from Lapeer, Mich., recently celebrated a 100-day streak with her husband, Tim Kroll, 44.

Their daughter Elizabeth, 17, has had streaks with both of them but says she is more committed to snapping friends. "Sometimes it's nice to not just see the dog filter on my dad's face."

She goes to great lengths to keep streaks alive—her longest still going hit 437 days on Tuesday, she says—snapping even friends she is angry with. "I'm not going to be mad forever so why jeopardize a Snapstreak?" she says. "I'll send a blank picture."

To save a streak with a friend whose phone died, Ms. Kroll got hold of the friend's password. "I had to log in for four days and Snapchat myself."



SAM DETH/GETTY

**J.Crew CEO Mickey Drexler, center, is refocusing on lower prices and a more accessible image. The company said last month it was parting ways with creative chief Jenna Lyons, in pink.**

day, even when not feeling creative, by snapping her shoes, or "I take a picture of the sky with the temperature filter on it."

Snapchat lets users doctor images with filters it calls "lenses"—to superimpose dog features on their faces, say—or add "bitmoji" cartoons and other elements. Snaps can include text, voice alterations and more.

When Ms. Saleh is feeling creative she covers her face with a Kim Kardashian emoji and mimics the celebrity's personality. She once chronicled the serial tale of a broken office water cooler for a week—anything to sustain a streak.

In an argument with your snapping significant other? Remember the bigger picture, as 19-year-old Samantha Bombel of Garfield, N.J., has done for more than a year to maintain a streak with her boyfriend. They usually exchange selfies. During one fight, Ms. Bombel says, she sent "just a picture of the ceiling."

"There's definitely been times," she says, "where I've been like, 'I'm still not talking to you, by the way, but I have to Snapchat you.'"

The couple's streak was at 387 days on Tuesday, she says. On day 354, they were to-

gether and forgot to snap. "I checked my phone and I was like, 'I don't think we have our Snapstreak anymore,'" says Ms. Bombel. "And then he checked his phone, and we both started freaking out."

Desperate, her boyfriend emailed Snapchat's support desk, which gave the couple a "one-time courtesy," she says, and their streak survived.

A Snap spokeswoman says the support team evaluates streaks case by case and reinstates them in certain circumstances. Snap doesn't give details, she says, to prevent users from gaming the system.

After Alyssa Vuong, 20, an Iowa State University student, dropped her phone in the ocean over spring break, she kept up her streaks using someone else's phone for a few days before giving up.

She had a streak of around 70 days with friend Kyle Hatton, 22, who can see her apartment from his and takes photos of her in her window to snap her. He let the streak die on a trip to the French Riviera.

"I kind of wanted to enjoy the environment," Mr. Hatton says.

He made up to Ms. Vuong by signing a one-year Snapstreak contract with her.

Summer camp is the streak snag for Meghan Sweeney, 13, of Carmel, Ind. A streak with her best friend—168 days as of Tuesday, she says—is among 15 she has going, and she is signed up for three summer camps this year.

For two weeks, she won't have a phone and her best friend will be with her at camp. They may keep their streak alive by commissioning someone to snap between their accounts.

Ms. Sweeney says she isn't as addicted as friends—one has 82 separate streaks, she says. "Some of my friends, they'll, like, talk about it at

lunch and they'll be like, 'I lost my 90-day streak with this person; I'm so sad,' " she says. "Some people overreact a little."

Parents maintain streaks, too, including Keith Whalen, 43, of Jordan, N.Y., who calls himself "very antisocial media." His daughters pressured him to download Snapchat and "I decided just to appease them," he says. "Then it became kind of addictive."

This month, he says, he lost an 86-day streak when his younger daughter forgot to snap him. "It was a little devastating," he says. His older daughter kept their streak alive after she was grounded and he confiscated her phone—by borrowing a friend's phone to log in.

To save a streak with a friend whose phone died, Ms. Kroll got hold of the friend's password. "I had to log in for four days and Snapchat myself."



SAMANTHA BOMBEL

**Samantha Bombel and Bret Francis got their streak restored.**

Continued from Page One seconds after the recipient views them and that have addicted the social-media masses.

Send a snap, get one back within 24 hours; send another, get another. After three days, it's an official streak that continues as long as each person sends a snap within a 24-hour window.

A streak earns a flame emoji and a number showing how many days the chat has gone on. An hourglass appears when time is running out.

Snap, which introduced Snapstreaks in April 2015, says it coined the term but declines to say how many streaks are going on. It reported 166 million daily Snapchat users in its most-recent quarter.

The critical task: Do whatever it takes to beat the clock. Dropped your phone in the ocean? Borrow a friend's, log on and snap. Grounded with no phone? Get a friend to log on as you and send snaps.

Can't think of anything to photograph? The floor will do. Ms. Saleh has sustained a streak with an Atlanta friend she says hit 159 days on Tues-

# LIFE & ARTS

**THE MIDDLE SEAT** | By Scott McCartney

## Get Ready to Unpack for Security

Travelers should expect more carry-on items, like food and tablets, separated into bins

Arlington, Va.

**CHANGES ARE COMING** to airport security checkpoints: TSA wants you to declutter your bags.

New procedures, such as requiring all food or all electronics larger than cellphones be placed in bins separately, are still being tested. Changes haven't yet been finalized, but senior Transportation Security Administration officials agreed to discuss them publicly for the first time. Decisions will be made in a few weeks, with new rules implemented after the summer travel rush, once screeners are trained and announcements made.

Tests began at small airports like Colorado Springs, Colo., Boise, Idaho and Lubbock, Texas. Travelers have since run into them in Los Angeles, Phoenix, Las Vegas, Boston, Detroit, Fort Lauderdale, Fla., and San Juan, Puerto Rico.

Many have been confused by unusual procedures. In Kansas City, Mo., in early May, screeners forced passengers to remove all paper from bags, down to notebooks. That test didn't go well and was halted after a few days, TSA says.

"It has to be efficient and it has to be effective," says Darby LaJoye, assistant administrator for security operations. "We are far

enough along that I am very optimistic that what we are piloting is working."

Airline baggage fees prompt travelers to load up carry-on cases, which has created problems at X-ray machines. Pictures of the insides of overstuffed bags take more time to read. Screeners must be able to identify each item in the bag—anything that can't be cleared as safe has to get manually checked, officials say.

Forcing travelers to dump more out of bags, sometimes without warning, will likely confuse and anger fliers until they get used to new rules. TSA figures lines won't lengthen because the total time at the checkpoint will be the same. Tests have shown TSA can slow down the process of decluttering bags at the start of security, known as divesting, but gain the time back by speeding up X-ray reading and reducing manual bag checks.

TSA says new procedures likely will be confined to standard screening lines and not PreCheck lanes, where trusted travelers get expedited screening and get to leave more items in bags.

Mr. LaJoye says TSA has been considering changes at X-ray machines for about 18 months. "It is not any one particular item we're



Densely packed bags are more likely to get inspected manually by TSA officers, such as this one at Washington's Reagan National Airport on Monday. New machines to verify identifications, below left, are also coming.

worried about. It's not about paper or food or anything. It's how best to divest those items," he says.

Based on pilot-program results, he says officers likely will focus more on travelers when they first start hoisting their bags on tables for the X-ray machine, asking them to remove items and put them in separate bins.

Those items could change line-by-line, airport-by-airport. Compliance will be optional, TSA officials say, but not complying may lead to opening a bag for manual inspection.

When checkpoints are busy under current rules, bags pile up waiting for manually screening, and lines can get long. "The more items in a bag, the more complicated it becomes," says a TSA explosives specialist involved in the pilot program.

To demonstrate, he runs a bag packed with all kinds of electronics and food items through an X-ray machine at Washington's Reagan National Airport, followed by an uncluttered bag with clothes, a quart-sized bag of toiletries and paperback book.

TSA's X-ray displays color items in bags by their density—most stuff is orange, blue and turquoise more dense, metal shows up as black.

The cluttered bag appears on the screen looking like a kindergarten art project gone haywire. With the uncluttered bag, shapes

are easy to identify. Even if the cluttered bag doesn't get pulled out for manual checking, it takes the screener more time to study the image.

"There's not any one thing in that bag that says red flag. But there's so much going on it takes time to figure out what it is," the explosives specialist says.

**The new rules likely will be implemented after the completion of the summer travel rush.**

managers. "We run the risk of, certainly for the U.S., of creating an environment that is really bad for business."

TSA says it will step up enforcement of the two-item limit—one bag that fits in an overhead bin and one under the seat in front of you.

Trans-Atlantic travelers may face other restrictions, such as expanding a cabin laptop ban from select Middle East and Persian Gulf airports to all flights from Europe. But a full ban, which may be hard to enforce at many European airports on flights bound for the U.S., is hardly a sure thing. The airline industry is lobbying for alternative measures.

Another change starting to roll out: TSA will begin using machines to verify ID instead of officers manually studying passports and driver's licenses. The ID verification machine testing will start at Washington Dulles Airport later this month, then spread to Atlanta, Boston, Chicago, Austin, Texas and Washington Reagan Airport.

The machine checks for fake IDs and matches up names with passenger lists—no boarding pass will be needed at the TSA checkpoints when the machine is in use. Officers can still clear someone manually if a false alarm is triggered.

TSA tested the technology with a shipment of fake IDs out of China that was intercepted by customs officials.

**MUSIC REVIEW** | By Jim Fusilli

## FOOTWORK GOES GLOBAL

BY JIM FUSILLI

**THE MUSIC** of composer-producer Jlin, the stage name of Jerrilynn Patton, now resides in that delicious, liberating place where it's not easily defined, as demonstrated on her new album, "Black Origami" (Planet Mu).

Ms. Patton's recordings have their roots in footwork, the form of electronica that came to prominence—at least in Chicago, where it originated—in the 1990s. A narrow definition of footwork perceives it as frantic dance music with a high number of beats per minute, an onslaught of percussive notes of short duration and subordinate roles for melody and harmony. But Ms. Patton's music doesn't aim to serve dancers. Instead it employs a variety of tempos and unexpected interludes, and at times sounds like minimalism filtered through house music and the rattle of Chicago's L.

On "Black Origami," her second full-length album, complex synthetic passages draw influences from cultures far from the South Side. The title track taps into Middle Eastern and South Asian modes and instrumentation, while "Nyakinyua Rise" relies on layers of African shakers and hand drums as counterpoint to tribal-like chants. Dope Saint Jude, a rapper from Cape Town, South Africa, provides the jabbing top line on "Never Created, Never Destroyed." Though



Ms. Patton continues to display an uncanny and often-dazzling knack for the use of drum sounds, the stuttering pipe-band snare of footwork often appears as an accent rather than a primary feature.

Growing up in Gary, Ind., where she still resides, the 30-year-old Ms. Patton took piano and drum lessons. After her drum teacher was killed in 2006, Ms. Patton chose to halt her training and instead focused on making footwork tracks on her laptop by chopping up and recasting samples.

She began to question whether she could have an original sound if she stuck to footwork, which is alternately known as juke and whose most notable practitioners include RP Boo, Traxman and the late DJ Rashad. Once Missy Elliott and others brought footwork to the mainstream, Ms. Patton saw the risk of codification that limited creativity. "It became trendy to be trendy, not a trendsetter," Ms. Patton recalled when we spoke by phone. She set out to find her own style.

When she began to issue her original recordings, two tracks, including the aptly titled "Erotic Heat," found their way onto the 2011 footwork compilation "Bangs & Works Vol. 2" (Planet Mu). Popping with subtlety, tension and restrained sensuality, "Erotic Heat" foreshadowed her quest for distinction. Her 2015 debut, "Dark Energy," opened with "Black Ballet," a track that featured a piano motif, strings and brass before an op-

eratic voice entered accompanied by the kind of percussion more aligned with a classical ensemble.

On "Black Origami," Ms. Patton is more concise in her writing, despite the expansion of the colors of her synthetic sound palette. In "Kyanite," birdlike effects flit around scat-singing, tight patterns on the taut drums and a motif that invokes a pungi, a Middle Eastern flute. The most prominent features of the too-brief "Calcination" are the air and space she leaves around the timpani or kick drum. "Hatshepsut" suggests a row of percussionists in a snappy marching band. Created with the experimentalist Holly Herndon, "1%" features rhythmic, staticky pulses and bursts under spoken voices, one of which is a recording of a telephone operator; another, culled from the film "Resident Evil," repeats "You're all going to die down here."

Ms. Patton says she is at work now on music for a ballet and is eager to score a film. On "Black Origami," she performs "Holy Child" with avant-garde composer and multi-instrumentalist William Basinski, a musical descendant of minimalists like Brian Eno, Philip Glass, Steve Reich and others. Their collaboration, which fits hand in glove with several tracks on the new album, illustrates how far from footwork cliché Ms. Patton has traveled, as well as where she might go in the years ahead.

*Mrs. Fusilli is the Journal's rock and pop music critic. Email him at jfusilli@wsj.com.*



Jlin's new album is 'Black Origami'

## OPINION

## REVIEW &amp; OUTLOOK

## North Korea's Missile Advances

Pictures of dictator Kim Jong Un applauding as another North Korean missile ascends into the sky have become routine. But the Hermit Kingdom's two most recent launches deserve special attention, because they show Pyongyang nearing its goal of deploying a nuclear-armed intercontinental ballistic missile (ICBM) that could destroy American cities.

On May 14 the North launched a new intermediate-range missile it calls the Hwasong-12. The missile traveled fewer than 500 miles, but that's because it was fired at a very steep angle to avoid flying over neighboring countries. If launched at the optimum angle, it could have a range of 2,800 miles, which means it threatens the U.S. island of Guam. That's the farthest of North Korea's missiles so far, not counting the rockets it used to launch satellites.

The Hwasong appears to use a new high-performance engine tested in March and was displayed in a Pyongyang military parade in April. Even more startling is that North Korea developed the sophisticated Hwasong engine from scratch instead of adapting a Russian or Chinese design.

The missile appears to be a single-stage, liquid-fueled rocket that could become the first stage of a new ICBM. That would allow the North to abandon the derivative designs it previously cobbled together to achieve the necessary thrust for longer ranges. In its current form the Hwasong is also road mobile, making it more difficult to find and destroy. The North Koreans further claim the Hwasong can carry a "large, heavy nuclear warhead."

On Sunday the North successfully tested another relatively new missile, the Pukguksong-2. While its range is shorter at about

1,000 miles, it is solid fueled and can be moved using a domestically produced transporter, both of which improve its survivability.

**The latest tests mean  
American cities will  
soon be in Kim's reach.**

Based on a submarine-launched missile that may be a modified Chinese design, the Pukguksong's first test in February was also successful. That suggests the missile will prove reliable, and North Korean media are reporting that Kim has ordered mass production.

The North also took advantage of the steep trajectory of both missiles to work on one of the last remaining obstacles to ICBM deployment—a re-entry vehicle capable of withstanding the heat and vibration of the fall through the atmosphere. The North Koreans say the Hwasong "verified the homing feature of the warhead under the worst re-entry situation," and that may be more than a boast. The U.S. and South Korea have confirmed that the test warhead survived and transmitted data.

The North still has to overcome obstacles to targeting the U.S., not least designing an ICBM re-entry vehicle. While the Kim regime is believed to have partially miniaturized an atomic weapon, it hasn't tested a hydrogen bomb. But that is little comfort. On Tuesday when U.S. Senators asked Vince Stewart, director of the U.S. Defense Intelligence Agency, how long North Korea needs before it can deploy an ICBM, he answered that it "is on a pathway where this capability is inevitable."

This month's tests mean advances in Pyongyang's nuclear and missile programs are coming much faster than analysts thought possible. If the U.S. and its allies don't take steps to stop it now, the world will soon wake up to a nuclear North Korea far more dangerous and disruptive than the one we have today.

## Supreme Court Patent Victory

U nanimous U.S. Supreme Court decisions that create tectonic shifts in law are rare, but on Monday an 8-0 majority in *TC Heartland v. Kraft Foods* rejected a lower court's statutory interpretation that has enabled rampant forum shopping in patent-infringement cases.

The case hinged on a 1948 law that limits patent litigation to "the judicial district where the defendant resides, or where the defendant has committed acts of infringement and has a regular and established place of business." Kraft sued Indiana-based TC Heartland, which distributes products under the Sunkist and Skinnygirl brands, in the federal district of Delaware for patent infringement.

Heartland challenged Kraft's ability to bring suit in Delaware and sought to move the case to Indiana, but its motion was denied based on the U.S. Court of Appeals for the Federal Circuit's 1990 precedent that rewrote the statute to include any place a defendant conducts business or sells a product. Nowadays, that can be anywhere.

So-called patent trolls who extort businesses by obtaining intellectual property rights and demanding large settlements to avoid litigation have made their home in the plaintiff-friendly Eastern District of Texas. During the past two years, about 40% of patent cases were filed in lovely, restful Marshall, Texas, which boasts fewer than 25,000 residents.

## Board of Scientific Conformity

T ime was when a newly elected American government could appoint its people to run it. These days that's a source of controversy, as Trump cabinet officials seek to name new science advisers.

Administrator Scott Pruitt is replacing half the members of the Environmental Protection Agency's Board of Scientific Counselors, and Interior Secretary Ryan Zinke has suspended some 200 science panels pending a review. To listen to the critics, they are "gutting" and "shutting down" federal science and "ousting" and "silencing" respected academics.

Ignore the hyperventilation. Mr. Pruitt is merely choosing not to renew some board members nearing the end of their initial three-year term.

Nobody is getting fired, and board members can reapply. Past practice has been to hand scholars a second term, but Mr. Pruitt is under no obligation to accept Obama appointees. Mr. Zinke's review is temporary, and America will survive if the invasive-species advisory panel misses a meeting.

Both actions are a step toward reforming a scientific bureaucracy that holds enormous power over regulations despite uniform points of view and clear conflicts of interest. The EPA's Board of Scientific Counselors, which is charged with ensuring that the agency's science is sound, nonetheless waved through the Obama Administration's dubious climate models and arbitrary "social cost of carbon" calculations.

The EPA's more than 20 scientific advisory boards are in particular stocked with academics

**Trolls who forum shop  
for judges will now  
have a harder time.**

As 17 states noted in an amicus brief supporting Heartland, the Eastern District of Texas is popular because "local practices and rules depart from national norms in ways attractive for incentivizing settlement for less than the cost of litigating the early stages of patent cases." The district's judges are averse to summary judgment, and its case assignment system provides a "predictable formula litigants can use to select their preferred jurist." Translation: Plaintiffs can't lose in Marshall.

The Heartland case didn't involve patent trolls or the Eastern District of Texas, but both will likely be significantly affected by the Supreme Court's ruling. In a 13-page opinion for the Court, Justice Clarence Thomas overturned the Federal Circuit's 1990 ruling and harked back to the Supreme Court's 1957 *Fourco Glass* decision that "definitively and unambiguously held that the word 'residence' in the 1948 law 'refers only to the State of incorporation.'

Antonin Scalia must be smiling upstairs at the Court's return to the plain meaning of the statutory text.

who receive EPA grants. As part of a 2016 lawsuit, the Energy and Environment Legal Institute showed that 24 of the 26 members of EPA's then clean-air advisory panel had received or were receiving EPA grants. The institute estimated the 24 received \$190 million. At the EPA's ozone panel, 17 of 20 advisers received \$192 million in agency grants.

House Science, Space and Technology Chairman Lamar Smith has shown that advisers use these grants for research—and then sit on the government panels that peer review that research. They then review EPA rules based on their own research.

Greens are slamming Mr. Pruitt's office for suggesting he may consider industry experts for board positions, but why not? This was routine before greens intimidated Administrations into barring those voices. A rigorous science doesn't shrink from competing points of view or evidence. The EPA should have conflict-of-interest rules that apply equally to grant-receiving academics and business executives.

Mr. Zinke's review is aimed at ensuring that Interior's boards contain more state and local advisers, particularly from communities near public lands. This is part of the Trump Administration's broader goal of re-establishing a more balanced partnership between the federal government and the states—much-needed after the imperial dictates of the Obama years.

Messrs. Pruitt and Zinke could eliminate those boards that aren't required by statute. But if they're going to exist they should be more than rubber stamps for the progressive agenda or tickets for federal grants.

## Ford's Turmoil Is Not About Tesla



BUSINESS WORLD  
By Holman W. Jenkins, Jr.

Now let's consider the defenestration at Ford Motor Co. of Mark Fields. Ford's stock price under his three-year leadership has been down 37%. Tesla's is up nearly 50%. This has been all the explanation the media needs.

A New York Times report lays the meme on thick, blaming the car efforts of "Google, Apple, Uber and not least Tesla, the electric-car maker now valued more highly than any of the Detroit giants. The upheaval at Ford, the nation's No. 2 auto maker by sales, after G.M., reflects the challenges that lie ahead for companies that cannot adapt to that new landscape fast enough."

Really? Is that really what's happening? Then why is Fiat Chrysler, a notable laggard compared with General Motors and Ford in all the gee-whiz categories, enjoying the best share performance of all—up 60% in the past year?

The theory falls even flatter with a simple thought experiment. Suppose GM or Ford burned cash the way Tesla does, putting off for the long term any hope of profits. Would the market applaud and give either a Tesla-like multiple? Not in a million years.

The people like Mr. Fields and GM's Mary Barra who run car companies aren't dumb. If they could mint stock-market wealth by investing heavily and not worrying about profits, they wouldn't need to be asked twice.

To continue with the now-standard narrative, GM's stock price has held fairly steady while Ford's has dropped, so this must mean GM is doing a better job of not falling behind Tesla, Google, etc.

Here's the truth about GM. It's valued on the profits it generates from cars and trucks—mostly trucks. Its diversion of a few billion in capital toward autonomy, ride-sharing, electrification, etc., is looked on indulgently by investors because they see what's going on.

Such investments are partly a brand-burnishing accompaniment to hardheaded business decisions to withdraw from unprofitable markets such as India, Russia and Europe, and to minimize the burden of manufacturing profitless small cars for the domestic market under U.S. fuel-economy regulations.

It's the sense that GM's Ms. Barra is shedding unprofitable cost structures. It's the sense that she is focusing GM on those geographical and product markets (trucks, SUVs) that can provide acceptable returns. This is why GM is perceived as playing the underlying game better—the underlying game being all about capital efficiency and rationally maximizing shareholder value.

Yes, technology will transform even these vehicles. What boat owner won't want computerized help in keeping the trailer straight when backing up? But these will remain vehicles that suburban and exurban Americans will want to own and drive themselves (and cherish) for a long time to come.

GM's leaders don't kid themselves or their shareholders that profits from new "mobility" businesses will be the salvation of the old, metal-bashing business. Making vehicles needs to be profitable in its own right. Ford shareholders want to know that Ford's leadership understands this too.

## What Germany Owes Its Neighbors

By Taylor Dinerman

P resident Trump was wrong to say Germany "owes" the U.S. for its defense. But Berlin is paying nothing like its fair share for the defense of Europe.

Last July, in response to Russia's aggressions in Ukraine, the North Atlantic Treaty Organization agreed to deploy four multinational mechanized battalions of roughly 1,000 men each to the Baltic states and Poland. These units—led in Estonia by the U.K., in Latvia by Canada, in Lithuania by Germany and in Poland by the U.S.—are "tripwire" forces. They'll be stationed in a forward area where Russia, according to one German expert, has a five-to-one military advantage.

The idea is to reassure these four nations that NATO will protect them from attack.

Add the American brigade now stationed in Poland on a rotating basis, and the U.S. is deploying four battalions in the region. The Western European NATO nations, including Britain, are deploying only two. That's the kind of imbalance Mr. Trump complains about.

Why should the U.S. and Canada bear a greater burden for the security of Germany's neighbors than Germany does?

After the Soviet Union fell apart in 1991, European leaders were convinced that direct threats to their homelands were a thing of the past and that all they needed were "projection" forces.

Countries like the Netherlands, Italy and especially Germany spent their reduced defense budgets on forces designed to intervene in Third World nations. They built amphibious landing ships and heavy transport aircraft instead of tanks and self-propelled artillery.

As a result, the European military powers—which were all ready to sup-

port British, French and U.S. humanitarian interventions in Africa, or post-9/11 operations in Afghanistan and the Middle East—are unable to provide protection to their allies in Eastern and Central Europe.

Not only have these nations failed to reach the 2% of gross domestic product they'd agreed to spend on defense, but the money they allocated went to hardware irrelevant to Europe's needs.

## Why should the U.S. bear a greater burden in Eastern Europe?

Germany has recently agreed to a slow buildup of its tank forces, but even that will still leave NATO with far too small an armored force to defend its Eastern European members. If, as seems likely, the current German coalition government is re-elected, Berlin will continue to resist paying its portion of Europe's defense budget.

The U.S. shares the blame for encouraging Europe to develop a more "expeditionary" mind-set. "Out of area or out of business," was, alas, an American slogan. Mr. Trump should not hesitate to say America was wrong. NATO's European members have to take responsibility for collective security in their own neighborhood.

Mr. Trump is also asking NATO allies to do more in Afghanistan and against Islamic State. It would be nice if they did—but for now it would make more sense if they prioritized protecting their fellow NATO members in Central and Eastern Europe.

Mr. Dinerman writes on space policy and national security.

## OPINION

# The Senate's Challenge in Trump's Washington

By Joseph Rago

**I**t try to kind of ignore the noise and focus on the agenda," says Mitch McConnell during an interview last week. By nature the imperturbable Senate majority leader is as well equipped as anyone to maintain the appearance of political normality, though the permanent turmoil of the Trump presidency isn't making it easy.

Some of Mr. Trump's priorities—the plan to repeal and replace ObamaCare, tax reform, deregulation—are, Mr. McConnell says, "the kinds of things a conventional right-of-center Republican president would have done." This familiarity explains why

## The FBI-Russia affair helped reflate health reform by distracting the president's critics.

"virtually all our members, from an agenda point of view, are very comfortable," the Kentuckian adds. "We could do with a lot less drama. It is distracting. But I try to put that aside and concentrate on what we are trying to achieve for the country."

Less conventional is Mr. Trump's firing the FBI director amid the investigation into the alleged Russian nexus. The irony is that the FBI-Russia affair helped refloat health reform in the Senate, by lending Mr. Trump's critics something to be outraged about other than the bill the House passed on May 4.

This breathing room officially ended on Wednesday when the Congressional Budget Office published its cost-and-coverage estimate for the House bill.

Background conversations over the past two weeks with senators, staffers and lobbyists suggest the health debate will test whether Congress can conduct business in the absence of traditional presidential leadership. Mr. Trump rarely practices persuasion, such as giving speeches that identify national problems and explain how better policies can fix them. Nor does he seem to conserve political capital or recognize the limits of a job-approval rating that's 15 points under water.

The GOP's 52 senators have their own difficulties, not least reconciling potentially irreconcilable differences that don't break on neat ideological lines. The Venn diagram for a compromise on, say, Medicaid doesn't leave a lot of overlap between an entitlement reformer like Pat Toomey of Pennsylvania and Tom Cotton of Arkansas, where ObamaCare's expansion increased enrollment by 64%—to nearly one of three Arkansans.

Same for insurance premiums: Everybody says they're unified around lowering consumer rates as the most important goal, though without reaching even a rough consensus about how to do so. One option would be to relax ObamaCare's regulations and mandates, as the House bill partly did, but the trade-off is reopening the emotional debate about pre-existing conditions.

The forum for accommodating these differences is a partnership between Ted Cruz and Lamar Alexander. The Texas controversialist and the Tennessee chairman of the Health Committee assembled a six-member working group several weeks ago. It has since grown to 13 members and is now open to all wings of the party. The group meets every Tuesday and Thursday and any GOP senator who wants to attend is welcome. Health care is also the first item at Senate Republicans' three-a-week lunches.



GETTY IMAGES

Majority Leader Mitch McConnell at the Capitol on April 7.

The GOP's unlikely advantage is that focusing on health-care substance has become a reprieve from the latest Trump irritations. "We're working harder to educate ourselves than we ever have," says one senator, though grade that on the Capitol Hill curve. Several lawmakers invoke the influence of a 3-by-8½-inch card that Mr. Alexander often hands out, which lists rudimentary facts about the U.S. insurance market, such as the share of Americans with employer-sponsored coverage (61%).

In public, senators claim they're putting the House bill aside and writing their own, but this is more a rhetorical reset to try to make a positive case for legislation that the House did a less-than-compelling job selling. If the Senate comes to an agreement, that will probably mean keeping the basic architecture of the House effort but allowing a longer transition period, as states wind down Medicaid to block grants, and making tax credits more generous to less affluent, older and rural constituents.

Mr. Cruz and his allies don't have a reputation for working well with others. Attribute his new amiability, a colleague suggests, to a different political context from the Obama years: Mr. Trump's election meant "the entire universe changed." (Let's hope he's wrong about that.)

The other motivation—which applies beyond Mr. Cruz—is this once-in-a-generation legislative opportunity. Whatever Mr. Trump's flaws, he's a latecomer to politics and hasn't promised voters for seven long years that he'd repeal and replace ObamaCare. The Senate GOP did. Now the president will sign whatever bill Congress sends him, however imperfect. If 50 senators plus the vice president can't do their job, they'll look dishonest and feckless, and more to the point they'll waste the chance to improve the American health system.

The backstop, finally, isn't even the ObamaCare status quo. It's a bailout of the ObamaCare status quo.

Moderate Republicans, like Louisiana's Bill Cassidy, and Democrats from Trump states, like Indiana's Joe

Donnelly, have opened a back channel on a short-term stabilization bill. The idea is to dump a bunch of money onto the ObamaCare exchanges beset by rising premiums and fewer choices. Twelve states have one Republican and one Democratic senator, and they're likely to pull the trigger by July if repeal and replace fails.

Bipartisanship otherwise remains elusive. The Democrats' political gamble, Mr. McConnell says, is that "this issue will do for us what it did to them"—i.e., lead to electoral defeat. "They don't see any incentive in participating in anything that looks like a serious replacement."

As for the predictions of midterm doom, Mr. McConnell's theory is that voters are "very results-oriented." If so, then the solution is to power through the attacks and push through a bill that fixes the problem.

"The hard left has done a good job of demonizing what's going on. You see that reflected in the polls, that people have decided by pretty significant margins that they don't like whatever it is we're doing—they're not sure what we're doing, but they don't like it," Mr. McConnell says. "But when all the noise settles down, what's really going to make a difference is: Are there insurance options? What are the rates? And I think people will focus on whether they think we're in a better place than we were when we started."

So for all that, how much progress has the Senate made? "Steady," replies one senator. Forward progress? No, "steady," he repeats. Nobody would go on record reliably confident of an outcome.

And what about Mr. McConnell—is he optimistic? "Oh, I don't like using a word like that," he says. "This is a tough challenge, and we're going to keep working on it."

Mr. Rago is a member of the Journal's editorial board.

## Trump Is More Optimistic Than Reagan, and That's Not Good

By Jason Furman

President Trump has outdone Ronald Reagan in at least one respect: unrealistically rosy forecasts for economic growth. In 1981, President Reagan's first budget predicted growth well above the consensus of private forecasters, in a bid to justify large tax cuts and increased defense spending. When the promised growth didn't materialize, the deficit and debt ballooned.

## His budget assumes 3% growth and includes a basic math error.

Now Mr. Trump is leading the economy down a primrose path that is even more unrealistic. The administration's budget, released this week, assumes long-run growth of 3%, a full percentage point higher than the Blue Chip consensus of professional forecasters and 1.1 percentage points above the prediction of the nonpartisan Congressional Budget Office.

Few will be surprised that Mr. Trump is a brash budgeter, but the magnitude of his stretching here is breathtaking. Under the 24 budgets produced by Presidents Bill Clinton, George W. Bush and Barack Obama,

the long-run growth forecast never exceeded the Blue Chip consensus by more than 0.1 percentage point.

Defenders of Mr. Trump's optimism might argue that a continuation of 1.8% annual growth, the average since 2001, isn't inevitable. During the Reagan era, the economy grew 3.1% a year, purportedly spurred by tax cuts and regulatory reforms. A closer look, however, shows that the 1980s aren't an argument for optimism—precisely the opposite.

There are two components to economic growth: adding more workers and increasing their productivity. Faster growth in the 1980s was the result of the former, an expanding workforce driven by two irreproducible demographic factors: the baby boomers entering their prime working years, and women continuing their influx into the workforce.

From 1980 to 1990 labor productivity—the amount of goods and services the average worker can produce in an hour—grew only 1.6% a year, below the figure marked since 2001.

Today the baby boomers are hitting retirement. As a result, Reagan-era productivity gains of 1.6% a year would now generate economic growth of only 1.7%. It's certainly possible that productivity growth could soar even higher, or that workers who have dropped out of the labor force could rejoin it, driving growth up to or

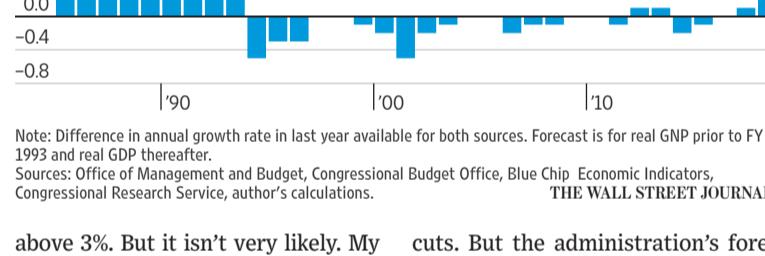
above 3%. But it isn't very likely. My simulations, based on historical data, suggest a one in 25 chance of hitting this target over the next decade.

Of course the right set of policies can make a difference, and I have no objection to dynamic scoring in principle. The Obama administration, like its predecessors, incorporated the effects of its proposed policies into its budget calculations.

The problem is that the Trump administration has locked in its assumption of 3% growth despite having yet to release detailed plans for tax reform and other proposals. One can debate the net economic effects of new trade restrictions, limits on immigration, deregulation and tax

## Great Expectations

Percentage-point difference in long-run real output growth forecast, administration vs. Blue Chip consensus, FY1985-2018



Note: Difference in annual growth rate in last year available for both sources. Forecast is for real GNP prior to FY 1993 and real GDP thereafter.

Sources: Office of Management and Budget, Congressional Budget Office, Blue Chip Economic Indicators, Congressional Research Service, author's calculations.

THE WALL STREET JOURNAL.

cuts. But the administration's forecast doesn't reflect even a cursory analysis of these plans. It simply presupposes 3% growth without explaining how the administration's policies will get the country there.

These forecasts are far from an exact exercise. Over the past eight years growth consistently underperformed the Obama administration's expectations, as well as most other projections. But the primary purpose of the larger economic forecast is to project the path of the federal budget deficit. Under the Obama administration the deficit generally was lower than we predicted, in part because interest rates and unemployment rates consistently fell faster than expected.

Any business that made plans based on such Pollyannaish projections for sales growth—compounded by basic accounting errors—would invite bankruptcy.

The president's budget assumes unrealistic 3% growth to justify tax cuts, increased defense spending, and a promise not to touch Medicare or the retirement portion of Social Security. In reality it will run up the deficit, slow economic growth and increase the national debt. Mr. Trump is digging a hole for himself with this budget. Congress should think twice before jumping in alongside him.

Mr. Furman, a senior fellow at the Peterson Institute for International Economics, was chairman of the White House Council of Economic Advisers from 2013 to 2017.

## Let the Private Sector Help Tackle the Migration Crisis

By George Clooney

As the most powerful leaders in the world gather in Sicily this week for the annual G-7 Summit, they will address today's most pressing challenges. The list is daunting—terrorism, famine, geopolitical instability and the phenomenon of uncontrolled immigration, to name a few. A bolder, broader approach is essential if lives are to be saved.

The statistics drive home the severity of the problem. Conflict or per-

secution has displaced 65 million citizens—more than at any time in history. And nearly 100,000 of the asylum seekers are unaccompanied children. If it were a state, this vulnerable population would constitute the 21st-largest country in the world.

Another 20 million people, including 1.4 million children, are at risk of death from imminent famines in places such as Nigeria, Somalia, South Sudan and Yemen.

The debilitating impact of these issues is contagious and can weaken

the will of us all. In fact, the Aurora Humanitarian Index, an international survey released this week, reveals just 9% of the respondents believe they can make a difference in solving the global refugee crisis.

The world needs new recruits to succeed in addressing today's challenges. For decades, the G-7, G-20 and United Nations have declared commitments to save the most vulnerable from war, famine, disease and other calamities.

At last fall's U.N. General Assembly, global leaders pledged to help this group by providing more assistance to countries where populations are at risk, better access to education for children, more humanitarian aid, and increased help for resettling refugees.

The challenge for leaders gathering at the G-7 summit in Italy this weekend is how they can mobilize global support for a comprehensive action plan that implements the U.N.'s declarations.

Any such plan should consider several additional tools to overcome inertia and galvanize progress.

First, we need to empower and highlight the "Power of One," the role individuals can play in implementing change from the bottom up. You can trace it from a brave Yazidi girl in Iraq to a doctor in the Nuba Mountains in Sudan all the way to a refugee in my home town of Augusta, Kentucky.

We all understand that it's not acceptable to only take care of yourself. That spirit is exemplified by a

group meeting this week in Yerevan, Armenia, as part of the Aurora Prize Initiative. Humanitarians from civil society, academia and business will discuss how to overcome indifference and take action on many of the same humanitarian challenges being

## Businesses and NGOs can boost transparency and aid in resettling migrants.

addressed in Italy. The Aurora gathering will honor individuals who put themselves at risk to help the most vulnerable populations in such places as Afghanistan, the Democratic Republic of Congo, Somalia, Sudan and Syria.

We have seen the difference these real-world saviors make, without fanfare. They are the doctors, nurses, aid workers, journalists and human rights activists who put their lives on the line every day. The G-7 must highlight their impact and stress the need to protect them.

We have to be more creative in addressing the root causes of the crises, especially corruption. I'm one of the founders of the Sentry—a nongovernmental team of financial forensic investigators and country experts who are identifying the stolen assets of the war criminals who are fueling conflict in Africa. There are of course many similar initiatives that are

working to collect information that would help identify and stop widespread corruption. The G-7 should use this information to freeze and seize these illicit finances and create a consequence for those laundering through international banks the billions of dollars that have been stolen from some of the poorest countries on earth.

Finally, we need to harness the power of business to advance humanitarian solutions. With ample resources and less bureaucracy, the private sector can play a much more important role in addressing famine, providing health care and education, and delivering clean water.

More and more business leaders want to incorporate humanitarian efforts into the work of their companies. The international yogurt manufacturer Chobani, for example, not only helps resettle refugees but also employs and educates them so that they can enjoy a better life. This needs to become the norm, not the exception, for 21st-century businesses.

To succeed in addressing these global issues, world leaders should make a real effort to incorporate missing elements in pursuit of a more comprehensive strategy. We have so much work to do. We need all hands on deck.

Mr. Clooney is a co-founder of The Sentry and serves as the co-chair of the Selection Committee for the Aurora Prize for Awakening Humanity.

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## LIFE &amp; ARTS

## FASHION

# Gabriela Hearst's Rise

Inspired by feminist icons, the designer uses luxe fabrics and a range of shapes to reach women

BY RAY A. SMITH

**DESIGNER** Gabriela Hearst thinks a lot about how women feel when they dress—bloated or slim and how fabrics feel against their skin.

A recent collection spanned sleek, nipped-and-tucked overcoats, dresses and double-breasted suits as well as languid velvet trench coats, a flowy oversized wool car coat and a breezy silk twill shirtdress.

"Those are the water-retention looks," Ms. Hearst said, with a laugh, while referring to the more relaxed ensembles in her fall 2017 runway show, held during New York Fashion Week in February. "I don't know if sometimes men realize that our body changes. We're different types of skinny during the month. There's days where we don't want to wear things this tight and there's days where we want to wear things this tight."

Ms. Hearst's take on womenswear has earned her two-year-old label a nomination for the Council of Fashion Designers of America's Swarovski Award for Emerging Talent. The awards ceremony takes place June 5 in Manhattan. If Ms. Hearst wins, it would be her second big award this year. The designer, who was born in Uruguay and raised on a sheep farm there, won the International Woolmark Prize for womenswear in January.

The self-described feminist's rise comes as women's fashion moves toward pantsuits and less frilly looks amid increased global attention on women's rights. Ms. Hearst held an intimate first runway show in fall 2017—after holding small presentations previously, which was a parade of sophisticated dresses, jumpsuits, suits and coats for women looking to project confidence and authority in a glamorous but not girly or overtly sexual way.

Ms. Hearst said the collection was inspired by brave, outspoken



Left, Gabriela Hearst, in her office in New York. She designs glamorous, not girly, looks, above and below.



FROM TOP: REBECCA GREENFIELD FOR THE WALL STREET JOURNAL (2); GETTY IMAGES

women, such as longtime political activist Angela Davis, and three senators elected in November—Tammy Duckworth, Kamala Harris, and Catherine Cortez Masto. Lightweight variations on turtlenecks in the collection referenced Ms. Davis, who wore them in the 60s and 70s. "In different ages, women feel differently about their skin," said Ms. Hearst, who is 40 and a former model. She describes her turtlenecks as "so soft next to your body, you can have a second skin that feels beautiful, so you don't have to kill yourself at the gym."

She cares about "how things feel" on the skin. She often pairs extra-fine knitwear under a suit or a sleeveless dress. "There's something psychological to women and tact," she said, referring to the sense of touch.

When Ms. Hearst started researching materials for the suits in her line, she noticed that the

men's suiting fabrics were actually kind of nicer than the women's," and used the superior men's suiting fabrics instead. The inside of Ms. Hearst's blazers have a silver-coated lining to protect against radiation. "There's a theory about cellular phones and your reproductive organs," she said. "It's controversial but it doesn't cost me that much to line the blazers inside." A number of limited-edition looks in the collection recycled overstocked fabric from Loro Piana.

Ms. Hearst shuttles between Uruguay, where she has a foreman manage the ranch she inherited from her father, and New York. She lives with her husband, Austin, a businessman and grandson of William Randolph Hearst, their two eight-year-old twin girls, Mia and Olivia, and 23-month-old Jack.

She and her husband are the sole investors in the company,

which now has 10 full timers, nine of whom are women, and which Ms. Hearst runs out of a sprawling office with showroom and design studio in Manhattan's Chelsea neighborhood.

The company sells on its website and at luxury retailers including Bergdorf Goodman, Net-a-Porter and Matchesfashion.com. Before launching her label, Ms. Hearst cut her teeth designing for Candela, a contemporary fashion label she started in 2004 and left in 2014.

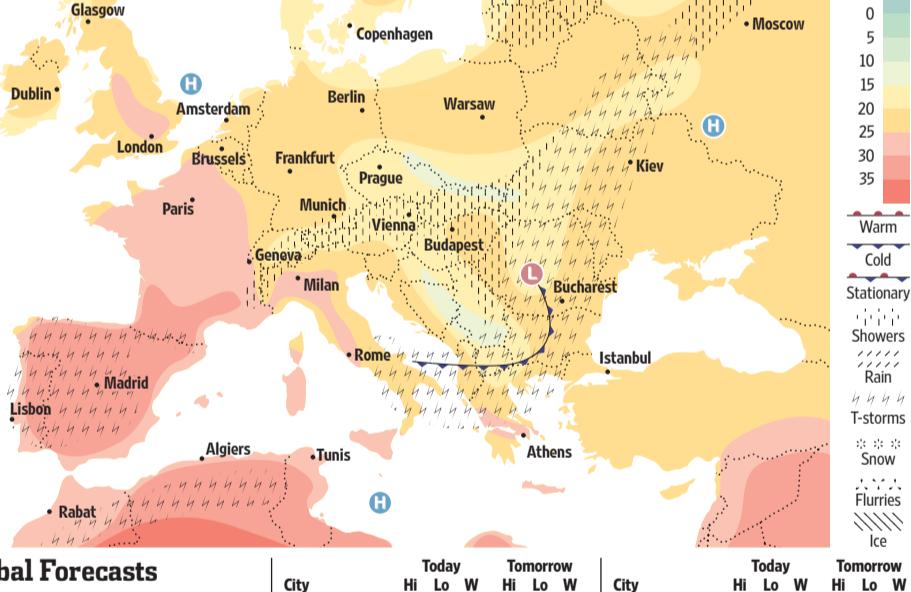
Ms. Hearst will compete against other womenswear designers from Brock Collection, Monse, and Sies Marjan, as well as the designer of Off-White, a men's and women's label. This year, the CFDA consolidated the award, which acknowledges how designers are increasingly blurring men's, women's and accessories collections, said Steven Kolb, the CFDA's president and

chief executive officer. Ms. Hearst now also makes shoes and bags.

Prices range from \$450 for cashmere/silk knits to \$5,000 for double-faced cashmere coats, with dresses in the \$1,200 to \$3,700 range.

"I believe in what women can do," Ms. Hearst says. She pointed to a photo of her mother she keeps in her office. "She used to compete in rodeo when she was 18. Then she was a Taekwondo black belt in her 30s."

## Weather

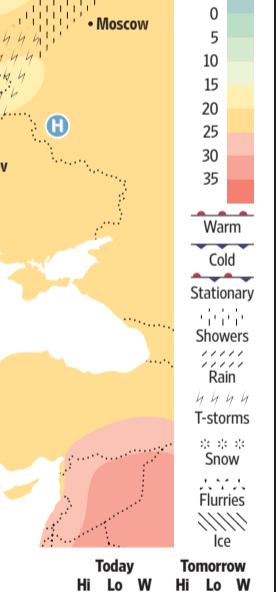


## Global Forecasts

s...sunny; pc...partly cloudy; c...cloudy; sh...showers; t...storms; r...rain; sf...snow flurries; sn...snow; l...ice

City	Today			Tomorrow		
	Hi	Lo	W	Hi	Lo	W
Amsterdam	22	11	pc	25	14	s
Anchorage	10	3	sh	11	5	c
Athens	25	17	pc	23	15	t
Atlanta	22	14	sh	28	19	s
Bahrain	36	20	s	24	23	s
Baltimore	22	14	t	25	14	pc
Bangkok	33	25	t	31	25	t
Beijing	29	15	s	31	16	s
Berlin	20	11	pc	22	11	pc
Bogota	19	9	t	21	10	pc
Boise	20	8	pc	22	9	pc
Boston	13	11	r	15	11	sh
Brussels	23	13	pc	26	15	s
Buenos Aires	18	8	t	16	5	pc
Cairo	32	20	pc	34	22	s
Calgary	14	4	c	18	8	pc
Caracas	32	26	pc	32	26	pc
Charlotte	22	14	t	27	16	s
Chicago	19	11	pc	24	14	t
Dallas	34	23	s	36	26	pc
Denver	23	8	t	20	8	t
Detroit	19	12	sh	22	13	pc
Dubai	39	27	s	38	27	s
Dublin	22	13	s	22	13	c
Edinburgh	23	13	s	24	13	pc
Frankfurt	22	12	pc	25	13	s

## AccuWeather.com



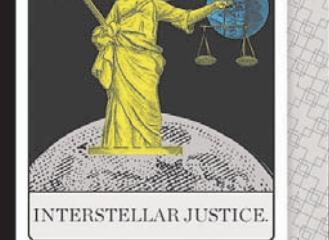
## HYBRIDS | By Nancy Cole Stuart

Across	Down
1 Not excluded from Lucy and Ricky's landlord	27 Like the blood in the pulmonary veins
5 Fleet	28 Fountain drinks
9 Fleet	29 Helvetica look-alike
13 Garden center buy	30 "The Ponder Heart" author
15 "Gypsy" composer Styne	32 Human or ostrich, e.g.
16 "That makes sense now"	33 Retro copier
17 Hybrid vehicle for use on the water?	34 Area of common interest
20 FDR based it on Romeo said the lark was its herald	35 Seed benefit
21 Port au Prince	36 Chihuahua chum
22 Rio de Janeiro	37 Unlocked
23 Riyadh	38 Bankruptcy
24 Salt Lake City	39 Floor plan extra
25 San Diego	40 Fine print
26 Salt Lake City	41 Playoff games
27 San Francisco	42 Requires much from
28 San Juan	43 Go after
29 Santo Domingo	44 Trillion: Prefix
30 São Paulo	45 Shop alternative
31 Seattle	46 Set, as a price
32 Seoul	47 Give an honorable mention
33 Shanghai	48 Person who works with figures
34 Singapore	49 Carry on
35 Stockholm	50 Broad player
36 Sydney	51 Hybrid vehicle for use by Venetian carabinieri?
37 Taipei	52 Suitable standard?
38 Tehran	53 Chuck of "Meet the Press"
39 Tel Aviv	54 Second, say
40 Tokyo	55 November symbol
41 Toronto	56 Chuck of "Meet the Press"
42 Vancouver	57 Slip setting
43 Washington, D.C.	58 Bouquet source
44 Zurich	59 Market indicator

► Solve this puzzle online and discuss it at [WSJ.com/Puzzles](http://WSJ.com/Puzzles).

## Previous Puzzle's Solution

WAGE	PABST	ETAS
EROS	ADLER	GRIT
BAKERS	DOZIE	GARR
SLA	OTTO	HEIDI
ISR	PROMISED	LAD
TETLEY	CAR	EITE
EASE	OVERTURES	
GRAD	PRIZE	
CEASELESS	YODA	
ALB	DAS	TESTED
EARD	DISASTER	HAD
SPEED	CITI	ERR
ASAP	CLOTHESLINE	
REST	BELLE	ALES
SSTS	SEDER	TOSS



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# BUSINESS & FINANCE

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Thursday, May 25, 2017 | B1

Euro vs. Dollar 1.1179 ▼ 0.04%

FTSE 100 7514.90 ▲ 0.40%

Gold 1252.40 ▼ 0.19%

WTI crude 51.36 ▼ 0.21%

German Bund yield 0.405%

10-Year Treasury yield 2.266%

## U.S. Profits Barrel Along

**Companies push pace of earnings growth, heartening investors; buybacks less a factor**

BY AKANE OTANI

Earnings at U.S. companies grew at the fastest pace in nearly six years in the first quarter, the latest boon to a bull market that has stretched into its ninth year.

With nearly all companies in the S&P 500 having reported results, aggregate earnings for the first quarter are on track to grow 13.6% from

the year-earlier period, according to FactSet, the highest growth since the third quarter of 2011. The gains were broad, ranging from heavy-equipment maker **Caterpillar** Inc. to social network **Facebook** Inc. to regional bank **U.S. Bancorp**.

Beyond the jump in growth, many investors have been encouraged by signs that the quality of the results is improving. That contrasts with recent years, when investors worried that corporate share buybacks and ultralow interest rates were juicing stock gains in the absence of business improvement.

Fresh signs of corporate strength, alongside solid U.S.

economic data and relative calm in financial markets this year, have helped send the S&P 500 up 7.1% through Tuesday's close.

"We should have continued growth in the markets, a lot of it driven because we have a stable economy and solid corporate earnings," said Omar Aguilar, chief investment officer at Charles Schwab Investment Management. "That gives me reason to be more optimistic."

Sales are picking up after many companies had turned to reducing costs and delaying investments in infrastructure to boost profits through the recovery from the financial crisis. Revenues are expected

to grow by 7.7% from the year-earlier period, according to FactSet, the highest rate since the fourth quarter of 2011. Sixty-four percent of companies beat analysts' expectations for revenue for the latest quarter, according to analysis from FactSet, above the five-year average of 53%.

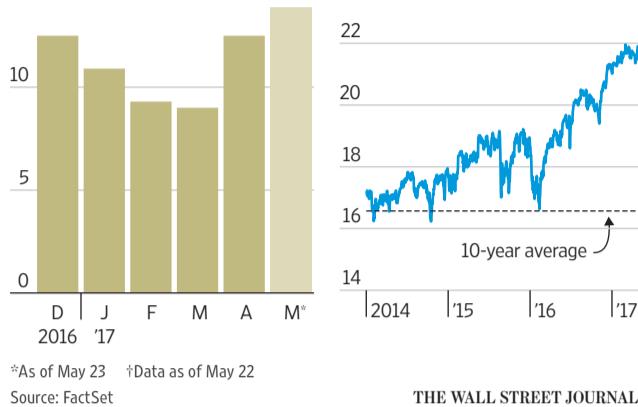
Companies also are spending less to repurchase their own shares this year, easing some investors' concerns that buybacks have been pumping up earnings growth. Share repurchases among firms are tracking 18% lower than a year ago and 1.4% lower than the

Please see **PROFITS** page B2

### Rosier Outlook

S&P 500 companies posted better-than-expected earnings growth in the first quarter, helping to justify higher stock valuations.

#### Expectations for first-quarter earnings

<sup>\*</sup>As of May 23    <sup>†</sup>Data as of May 22

Source: FactSet

THE WALL STREET JOURNAL.

## Funds Battle Tech Firms For Talent

BY LAURENCE FLETCHER AND SARAH E. NEEDLEMAN

The battle for quantitative talent has turned some of the richest money managers into underdogs. Why? Because they are up against the likes of **Alphabet** Inc.'s Google and **Facebook** Inc. for hiring the world's top minds.

"Google is trying to hoover up every data scientist in the world," said Luke Ellis, chief executive of **Man Group** PLC, the world's largest publicly traded hedge-fund manager. "Google has got more money than I have. I can't compete with Google just on that."

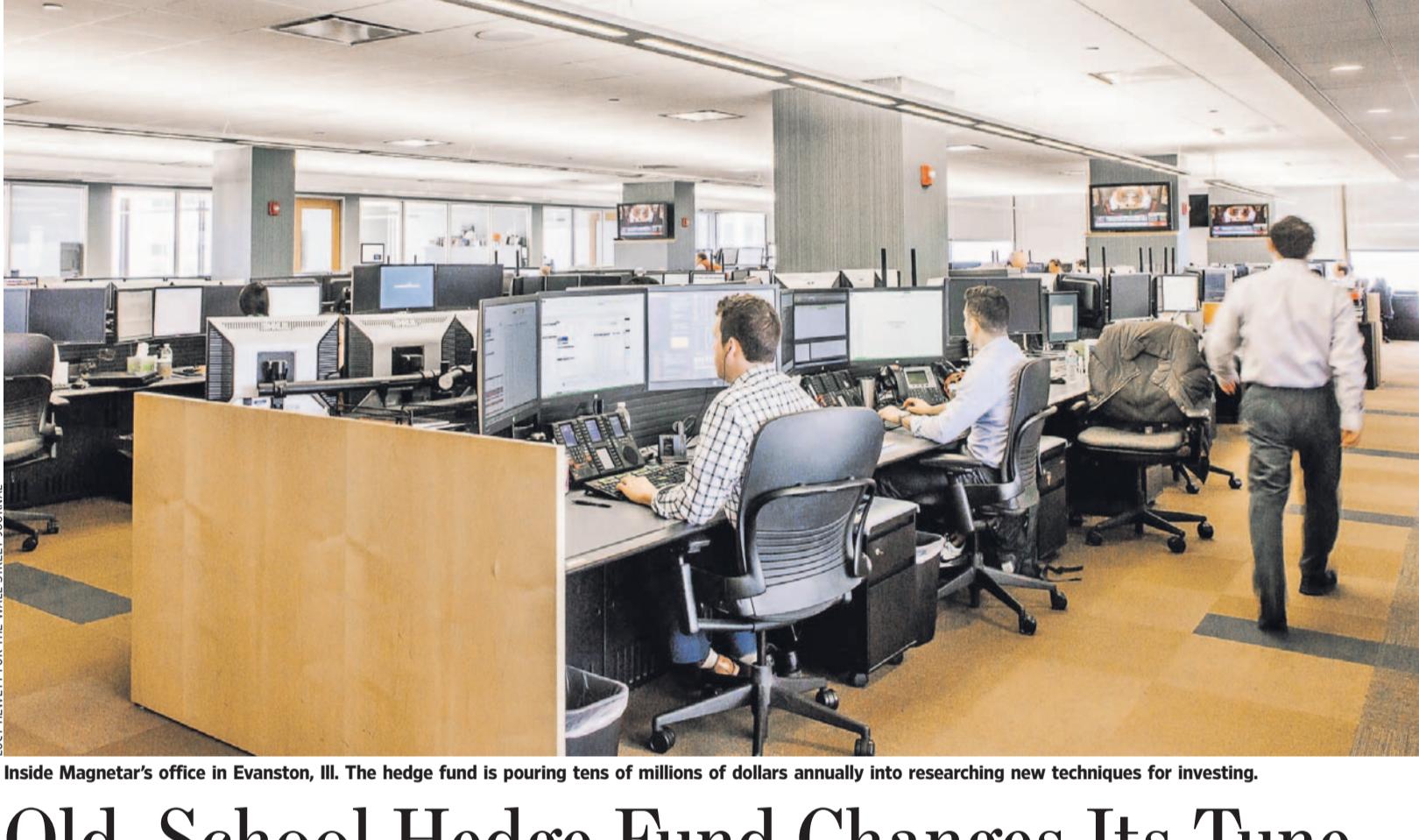
London-based Man Group attempts to get these data scientists at their source. The firm has donated millions to Oxford University to put its name on a quantitative research laboratory, hoping that prospective employees get acclimated with the firm and its culture early in their career.

The trouble is that across the corporate world—be it hedge funds, tech giants or even the Fortune 500—companies are desperate to hire the same type of people. They seek top graduates or postgraduates who can build software that learns to spot patterns in anything from photos on social media to financial futures markets. To appeal to tech talent, some financial firms offer the kind of office perks common at tech companies.

At Kenneth Griffin's hedge fund **Citadel**, the firm pitches candidates on running their own projects hand in hand.

Please see **TALENT** page B2

THE WALL STREET JOURNAL.



Inside Magnetar's office in Evanston, Ill. The hedge fund is pouring tens of millions of dollars annually into researching new techniques for investing.

## Old-School Hedge Fund Changes Its Tune

BY ROB COPELAND

EVANSTON, ILL.—Alec Litowitz, founder of one of the country's largest hedge funds, raised a simple question at the firm's investment committee meeting: How often do mergers fall apart?

No one had the answer, so the **Magnetar Capital** LLC founder assigned a team of analysts to pore through three decades of data to find out. They calculated that while 7% of announced transactions eventually collapse, the market behaves as if nearly twice as many do. Mr. Litowitz rea-

soned a computer program could make money exploiting that discovery and thousands of others. So began six years ago a billion-dollar quantitative effort at Magnetar designed to help the \$13.5 billion firm buck a hedge-fund massacre waylaying its peers and set to rest memories of controversial trading by the firm on subprime housing during the financial crisis.

Like high-end restaurants, hedge funds often roll out new menus to entice investors to keep coming back, and quantitative trading is the latest special du jour. In the

### THE QUANTS

Machines and their masters are the undisputed new kings of Wall Street

wake of years of disappointing investment performance and client defections, hedge funds are emphasizing a systematized, algorithmic approach to investing.

Magnetar's quantitative push is different from many of its high-speed quant competi-

tors, who parse reams of data in the hunt for an edge—even one they can't explain.

Magnetar is taking a more manual approach. Discoveries such as the types of corporate acquirers more likely to see through to the end of a tough deal are translated into algorithms that trade automatically. "We start with intuitions and then go see if the data backs it up," says Mr. Litowitz.

The shift is particularly remarkable because Magnetar and Mr. Litowitz for years represented the prototypical headstrong hedge fund, investors and industry executives

say. An adrenaline junkie who competes in triathlons and off-road mountain bike races, 50-year-old Mr. Litowitz was one of Kenneth Griffin's first hires at hedge-fund giant **Citadel** LLC. He racked up such profits that Mr. Griffin awarded him part-ownership of the firm.

Mr. Litowitz left to start Magnetar in 2005. The firm launched with \$1.8 billion in capital, marking one of the largest hedge-fund launches of the time. The firm commanded high fees even by the standards of the era, passing on many of its costs directly to

Please see **FUND** page B2

THE WALL STREET JOURNAL.

HEARD ON THE STREET | By Anjani Trivedi

## Investors in China: Watch Out



In a sign of the times, Moody's has cut China's credit rating for the first time in nearly three decades. Investors in China Inc. and its banks should heed the warning.

In downgrading China—putting the country on par with the likes of Japan and Israel—Moody's pointed to the string of stresses debated ad nauseam by China watchers, as Beijing grapples with slowing growth, rising debt and an increasingly creaky financial system.

But investors should take a second look. China's sovereign rating is important because it helps other bond issuers in the country to get a credit rating higher than they might otherwise be afforded.

Take China's banks, for example: Moody's gives the broader sector a baseline credit assessment of Baa3 based on indicators like loan-to-deposit ratios and counterparty risk. But because the government owns much

of the banking system and—it is assumed—would provide it with support in a crisis, banks are in practice able to issue debt at higher ratings.

Bank of China, one of the country's big four banks, has a base rating of Baa2, but any debt it issues is rated at A1, four notches higher.

**China's sovereign rating is important because it helps other bond issuers' ratings.**

By this logic, a notch down in China's rating should push down those of issuers that rely on government backing. In July 2007, when Moody's upgraded China, it simultaneously upgraded seven Chinese banks.

Any broader downgrade for Chinese companies and banks, which have been big issuers of debt in the U.S. dollar market, would be costly. One barometer of the way investors already seek

higher compensation for the unknowns that come with operating in China is that it costs \$78,000 to insure against \$10 million of Chinese debt for five years, compared with \$60,000 for the same amount of Israeli debt or \$37,000 for Czech debt. Meanwhile, the yield on five-year U.S. dollar bonds issued by A1-rated **Industrial & Commercial Bank of China** is already at 3.2%, compared with a 2.8% yield for bonds issued by similarly rated **Goldman Sachs**.

With a regulatory crackdown in force, Chinese companies and banks have been struggling with rising funding costs in home markets. They have also been hopping between onshore and offshore markets to issue debt wherever it is cheaper.

The move by Moody's may now make it more expensive to issue debt abroad as well. While the pain for China's government from the downgrade is manageable, it could prove painful for the country's debt-addicted bond issuers.

## Shale Oil Puts Heat on OPEC

BY LYNN COOK AND BENOIT FAUCON

VIENNA—OPEC's back is against the wall and U.S. oil producers put it there.

The Organization of the Petroleum Exporting Countries and a coalition of other countries including Russia are poised to curtail oil production for at least another nine months. The truth is the group has little choice, as U.S. drillers stepped up production following OPEC

cuts announced in November to ease a global glut.

U.S. oil output is now on pace to exceed 9.9 million barrels a day in 2018, a record, according to the U.S. Energy Information Administration.

For OPEC, competing against American shale oil now entails competing against Wall Street and its financial engineering—a prospect that has bedeviled government-run oil companies from Saudi Arabia to Nigeria.

Meanwhile, OPEC members and other big oil-pumping nations, which are set to meet here Thursday, have grown weary of lower prices, currently just above \$50 a barrel, and determined to take about 2% of global supplies off the market in an effort to shrink bloated oil inventory levels and put a floor under crude prices.

Saudi Arabia is particularly eager to boost oil values because

Please see **SHALE** page B2

THE WALL STREET JOURNAL.



Shale-oil production in North Dakota has contributed to a steady increase in U.S. crude output.

ROBYN BECK/AGENCE FRANCE PRESSE/GETTY IMAGES

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## PROFITS

Continued from the prior page fourth quarter of 2016, according to S&P Dow Jones Indices data as of Wednesday.

Buybacks push up per-share earnings, which can make the shares that remain on the market more valuable. But they also have been criticized by investors who see them as a way for companies to prop up share prices in the short term at the expense of focusing on investments that drive longer-term growth.

Ten of the 11 sectors in the S&P 500 are on track to post quarterly earnings growth in the first quarter, with financial and technology companies reporting among the biggest improvements, according to FactSet.

**Bank of America** Corp.'s first-quarter profit jumped 40% from a year earlier, surpassing analysts' expectations, as trading revenue jumped and rising interest rates boosted its net-interest income—a key measure of lending profitability. Shares of the bank are up 5.8% in 2017.

Facebook's first-quarter profit surged 76% to \$3.06 billion, as advertisers spent more money on its platforms and the company's number of active users continued to rise. Its shares have jumped 29% this year.

"When we look at how earnings came in this quarter and how they're expected to come in the rest of the year, people's concerns about the

stock market should really be allayed," said Jonathan Golub, chief equity strategist at RBC Capital Markets.

S&P 500 companies have now posted earnings growth for three straight quarters, after five consecutive quarters of declines, according to FactSet. The rebound is expected to continue. Analysts polled by FactSet estimate the broad index will post earnings growth of 6.8% for the second quarter and 11% for the full year.

Much of that is because a prolonged slump in commodities prices eased at the end of last year. About a third of the S&P 500's earnings growth in the first quarter came from energy companies, according to FactSet, where results improved alongside oil prices, which sank to their lowest levels in more than a decade in early 2016.

Some worry that this year's stock rally could stumble if economic measures—including U.S. auto sales—that disappointed in the first few months of the year show continued weakness.

"I see some danger signs for growth moving forward," said Ed Keon, managing director and portfolio manager with QMA, a multiasset manager owned by Prudential Financial, who added that he has pulled back from U.S. stocks this year while shifting more money into their European counterparts. Still, Mr. Keon said he doesn't see an end to the bull market soon.

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## BUSINESS NEWS

# Ford Deputies Expand Roles

As new CEO focuses on strategy, two top lieutenants will steer day-to-day decisions

BY CHRISTINA ROGERS

The top agenda item for Ford Motor Co. Chief Executive Jim Hackett is carving out a clear strategy for the 114-year-old auto maker's role in an evolving car business. For just about everything else, he can rely on Joe and Jim.

Ford's executive shuffle, announced Monday, led to broader roles for current Americas Chief Joe Hinrichs and current Europe Chief Jim Farley. They will leave specific regional duties, with Mr. Farley taking charge of global markets, and Mr. Hinrichs running global operations.

The moves hand considerable sway over day-to-day decisions to the pair of executives. As Mr. Hackett succeeds Mark Fields at the helm and looks to accelerate innovation and energize the workforce, analysts say his top lieutenants are being positioned as candidates to eventually succeed him for the top job.

In a note to investors, Barclays analyst Brian Johnson said the new job descriptions signal both are "vying to take over as CEO after Hackett's work is complete." He said "both have big challenges and perhaps the board's thinking is this will move them to cut deeper, act faster."

A Ford spokesman said the company doesn't comment on succession planning.

Ford last week said it would cut white-collar head count by 10%, or 1,400 people, in North America and Asia following similar actions in Europe and South America. In an interview, Chairman Bill Ford said more "hard actions" need to be taken to address underperforming parts of the business, but declined to elaborate.

Mr. Farley, 54, is an ex-Toyota Motor Corp. executive with a sharp tongue and bulletproof resume. He was recognized by



**Joe Hinrichs, left, and Jim Farley, shown in 2014, have global duties under Chief Executive Jim Hackett.**

the board as a top performer in 2016 after posting a \$1.2 billion profit in Europe, a sharp improvement from 2015.

Mr. Farley—recruited by Mr. Ford and then-CEO Alan Mulally—stanchred red ink and increased margins to 4.2% in Europe, a market long burdened by overcapacity and pricing wars. He aimed to further slim down Ford's European operations, targeting long-term operating margins of 6% to 8% even as crosstown rival General Motors Co. withdrew from the market, selling off its Opel AG busi-

ness campaign that has endured for years after Ford repeatedly changed slogans and approaches.

Mr. Hinrichs, 50, made his name on the manufacturing side, and spent the past 4½ years running North America, a region that drives nearly 90% of the company's profits. He was a candidate to succeed former Mr. Mulally as CEO before the job went to Mr. Fields in 2014.

### New Ford chief wants to accelerate innovation and energize the workforce.

Last year, Mr. Farley oversaw an effort to eliminate hundreds of salaried jobs in Europe through buyout offers—saving \$200 million annually. He shifted the focus to higher-profit cars and sport-utility vehicles to better compete in the region.

Mr. Farley joined Ford as a rising star, coming to the U.S. auto maker after serving as the face of Toyota's aggressive efforts to remake its image and better appeal to youth. Mr. Farley was a member of Mr. Mulally's restructuring team and rolled out the company's "Drive One" advertising

An Ohio native, Mr. Hinrichs has remained a source of stability for Ford in its most vital region amid a flood of new managers and the initiation of business ventures, including the Smart Mobility innovation unit that Mr. Hackett headed before becoming CEO.

Mr. Hinrichs is a blunt leader. In 2010, with Ford on the rebound after the financial crisis, he chastised a room full

of top executives for underinvesting in rapidly growing Asian markets, which he was running at the time.

He has tackled manufacturing challenges, including moving the profitable and high-volume F-150 from a steel body to aluminum. Well liked by the workforce, he negotiated cost-saving labor deals that helped keep Ford out of bankruptcy and competitive with foreign rivals.

Ford's North American operations have churned out some of the company's biggest profits in history under Mr. Hinrich. Bolstered by increased demand for pricey trucks and SUVs, Ford's operating margins in the region have topped 10%, rivaling financial results posted by luxury auto makers.

Having previously spent time at GM and in private equity, Mr. Hinrichs joined Ford as a plant manager in Sterling Heights, Mich., in 2000 and quickly rose through the company's manufacturing ranks.

Within six years, he was named vice president of North American manufacturing and later ran Ford's Asia region, overseeing industrial expansion in China.

# Health Startups Feel the Squeeze

BY RUTH SIMON

As Congress grapples with possible repeal of the Affordable Care Act, political uncertainty is prompting some health-technology startups to revamp their sales pitches or products, while others are finding it tougher to attract fresh capital.

The challenges are likely to be greatest for young firms with limited resources, companies tied directly to the insurance market or that sell to hospitals facing potential cuts in Medicaid, say some investors and others that work with startups.

It is still too early to tell how repeal of the ACA might play out or even whether it will happen. Republicans in the Senate have said they plan to put their own stamp on the bill that cleared the House this month, though the debate is expected to be contentious.

"One of the big advantages of a startup is to be able to pivot and fall into new opportunity," said Dr. Hubert Zajicek, chief executive officer of Health Wildcatters LLC, a Dallas health-care startup accelerator. "But this is change that has spelled more uncertainty. That is not change you can prepare for."

Some startups are shifting strategies to focus more on direct sales to consumers. Pillys Inc., a maker of Bluetooth-enabled smart pill bottles, has stepped up efforts to sell its product online and in pharmacies and is spending less time marketing to health-care providers.

The Seattle-based company is spending heavily on digital advertising and has hired a public-relations firm instead of sending an employee to conferences, said CEO Jeff LeBrun.

Venture-capital investors poured \$4.9 billion into health-care startups in the first quarter of 2017, up from \$3.6 billion a year earlier, according to Dow Jones VentureSource. Nearly 70% of those funds went to drug-development and medical-device ventures.

Political uncertainty has made some investors and customers more cautious about digital health companies. "The funding bar went up" after the election, said Anne DeGheest, an investor and founder of San Francisco-based HealthTech Capital. Investors are "asking for a higher level of sales and market validation."

The number of digital health startups receiving funding dropped to 124 in the first quarter of 2017, the lowest

quarterly total since the first quarter of 2011, according to StartUp Health, a startup mentor. The amount raised was comparable to last year's total, as investors funneled bigger sums into later-stage startups.

Many entrepreneurs say the appetite for health-care technologies that cut costs and improve quality will remain strong regardless of the political climate. The response to uncertainty is to "lean even harder on the clinical literature backing up what we do and the return on investment business case," said Adam Brickman, a spokesman for Omada Health Inc., a six-year-old startup that provides digital tools for diabetes prevention.

The San Francisco-based company works with roughly 70 employers, health plans and health systems.



**Smart pill bottles made by Pillys are Bluetooth-enabled.**

And some hospitals will continue to invest in new technologies regardless of what happens to Medicaid and the ACA, said Lee Perlman, president of GNYHA Ventures Inc., the for-profit arm of the Greater New York Hospital Association.

But others will only look to technologies "with short-term impacts that will allow them to do more with less."

"In the end, it will be a scalability issue," Mr. Perlman said. "If forced to choose between providing basic patient care and new investment, basic patient care will win."

Juan Pablo Segura, founder of Babyscripts, which uses an app and internet-connected medical devices to remotely track the health of pregnant women, has seen a shift in mood.

"There are plenty of health systems out there investing in the future, but there just isn't that massive push we felt before," said Mr. Segura, whose Washington startup works with more than a dozen hospital systems.

Babyscripts is focusing its sales efforts on the large hospitals that are early adopters of new technologies and less on smaller private practices more likely to be unsettled by any changes in health-care reimbursement laws.

# IKEA's Agnefjäll Steps Down as CEO

BY SAABIRA CHAUDHURI

IKEA Chief Executive Peter Agnefjäll has resigned in a surprise move less than four years after formally stepping into the role.

The Swedish furniture maker on Wednesday said it is naming Jesper Brodin, currently head of its product range and supply chain, as its new CEO starting Sept. 1.

Under the 46-year-old Mr. Agnefjäll, who became CEO in

September 2013, the company has responded to the growth of online shopping and center-city living by opening click-and-collect locations and other smaller, urban-focused formats. It also has spent more money on sustainability initiatives, established a shopping-center business and increased the diversity of its workforce.

"There are not going to be any major changes in strategic direction," said a spokeswoman, who added that Mr. Agnefjäll was leaving his own accord. "No doubt it was Peter's sole decision," she said.

IKEA said Mr. Agnefjäll had begun taking on CEO duties as early as 2012, making it five years that he had held aspects of the role.

"I believe it is a natural time for me to take a change of path," Mr. Agnefjäll said. "These years have meant a lot to me, both personally and professionally."

IKEA has reported stronger

profit and sales in recent years but has struggled to find appropriate labor and new products that meet its standards in India, a large untapped market in which it plans to open its first store early next year.

The 48-year-old Mr. Brodin will have to deal with the challenges presented by India and find a way to speed IKEA's revenue growth while continuing to adapt to changing buying behavior and making IKEA's supply chain more efficient.

**A Lotus Evora 400 at an auto show last month. China's Geely is looking to expand into the Southeast Asian market.**

July, said DRB-Hicom's group managing director Syed Faisal Albar. He added that it wouldn't be at a premium to what DRB-Hicom paid when it bought the stake from Malaysia's sovereign-wealth fund, Khazanah Nasional Bhd., for about \$412 million in 2012.

DRB-Hicom will continue to hold a controlling stake in Proton after the deal closes.

While the Lotus unit will offer Geely high-end vehicle technologies, it is Proton, with its potential as a gateway to the Southeast Asian market, that the Chinese company sees as the main prize, analysts said.

"The only thing attracting Geely is access to the Asean market," said Yale Zhang, managing director of Shanghai-based Automotive Foresight, referring to the Association of Southeast Asian Nations. "Geely is not eyeing any of Proton's technology—current Geely models are much more advanced than Proton's."

Proton will provide Geely access to right-hand-drive markets around the world, including Malaysia, Britain, India and Australia, said the company's executive vice president and chief financial officer, Daniel Donghui Li.

Aside from the capital injection, Proton will benefit from the planned deployment of Geely's sport-utility-vehicle technology, Mr. Li said.

Geely, which acquired Volvo in 2010, last year rolled out its Lynk & Co. brand aimed at competing with foreign marques at home and abroad. The Geely group sold a combined 1.3 million vehicles in 2016 and is aiming to more than double that figure by 2020.

Chinese car makers have been looking to expand into the Southeast Asian market, home to more than 630 million people. Cars built in the 10 Asean member countries can be sold within the bloc tariff-free.

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## TECHNOLOGY

WSJ.com/Tech

# In Cyberwar, Spies Can Become Targets

Ex-intelligence officials fear hackers are exposing identities of team working for NSA

By ROBERT McMILLAN AND SHANE HARRIS

The mysterious hacking group that supplied a critical component of the WannaCry "ransomware" software attack that spread across the globe in mid-May has been releasing alleged National Security Agency secrets for the past eight months.

Former intelligence officials now fear that the hackers, who go by the name Shadow Brokers, are taking a new tack: exposing the identities of the NSA's computer-hacking team. That potentially could subject these government experts to charges when traveling abroad.

The Shadow Brokers on April 14 posted on a Russian computer file-sharing site what they said were NSA files containing previously unknown attack tools and details of an alleged NSA hack affecting Middle Eastern and Panamanian financial institutions.

But something went largely



**Alleged National Security Agency secrets have been released.**

unnoticed outside the intelligence community: Buried in the files' "metadata"—a hidden area that typically lists a file's creators and editors—were four names. It isn't clear whether the names were published intentionally or whether the files were doctored. At least one person named in the metadata worked for the NSA, a person familiar with the matter said.

Additionally, the hacking group in April sent several public tweets that seemingly

threatened to expose the activities of a fifth person, former NSA employee Jake Williams, who had written a blog post speculating the group has ties to Russia.

The U.S. government hasn't commented on the authenticity of the Shadow Brokers' releases. Security experts who have examined the documents believe they contain legitimate information, including code that can be used in hacks, as well as the names of the files' creators and

editors. An NSA spokesman declined to say whether the names, documents and tools released by the Shadow Brokers came from the agency.

For people who work in the intelligence community, having their identities or the work they have done outed is a significant concern, said Robert M. Lee, chief executive of cybersecurity firm Dragos Inc. and a former member of the intelligence community.

Because nation-state hackers might run afoul of other countries' laws while discharging their duties, they could, if identified, face charges when outside their country. So, to keep their own people safe, governments for decades have abided by a "gentleman's agreement" that allows government-backed hackers to operate in anonymity, former intelligence officials say.

The Shadow Brokers "made this personal," Mr. Lee said. He believes the group left names in the metadata either because the group doesn't care about redacting sensitive information or because they wanted the names public.

Attempts to contact the Shadow Brokers weren't suc-

cessful. In blog posts, the group has denied any government affiliation, presenting themselves as anarchic hackers cut in the mold of the Anonymous collective. They first appeared in August of last year, releasing purported NSA

documents.

Some former intelligence officials suggested the U.S. prompted the outing of state-sponsored hackers when it indicted five Chinese military hackers by name in 2014, and more recently brought charges against two officers with Russia's Federal Security Service over a 2014 Yahoo Inc. breach.

By exposing cyberagents, the Shadow Brokers appear to be taking a page from the U.S. playbook, said Mr. Williams, who worked for the NSA's Tailored Access Operations hacking group until 2013. An NSA spokesman said the agency doesn't comment about "most individuals' possible current, past or future employment with the agency."

"We've fired first," Mr. Williams said, referring to the U.S. charging the alleged Chinese hackers by name. "This is us taking flak."

Current and former Justice

Department officials said the 2014 indictment and a 2015 cyber pact between the U.S. and China were meant to serve as a line in the sand to deter nation-state hackers from breaking into U.S. companies for economic gain. The point was to say "this type of behavior was not and should not be condoned," said Marc Raimondi, a U.S. Justice Department spokesman.

Government investigators are treating the Shadow Brokers documents as authentic, according to people familiar with the matter. Earlier this month, Microsoft Corp.'s chief lawyer, Brad Smith, asserted the computer code used in the WannaCry worm, a ransomware attack that held hundreds of thousands of computer files hostage, was "stolen from the National Security Agency."

While the Shadow Brokers claim to be anarchic hackers, many intelligence experts, including Mr. Williams and NSA leaker Edward Snowden, believe they are backed by Russia. A spokesman for the Russian Embassy declined to comment on the allegation. Russia previously said allegations that it has hacked the U.S. government are false.

## Value of Startup Unity Keeps Growing

By ROLFE WINKLER

Unity Technologies is putting the finishing touches on a \$400 million round of financing that values the videogame-technology company at about \$2.8 billion, according to people familiar with the matter.

Private-equity firm Silver Lake is leading the round as a new investor, these people said. Previous investors include venture firms such as Sequoia Capital and Draper Fisher Jurveston.

The 12-year-old San Francisco company, which makes software tools for videogame developers, raised capital last summer at a \$1.5 billion valuation.

**\$2.8**

Unity's value, in billions, as implied by its new funding round

Half of the new investment was earmarked for shares held by employees and existing investors, said people familiar with the deal. The other half would go to the company, an amount that puts the valuation at about \$2.8 billion.

Unity provides a game-development "engine," essentially software that developers use to build their digital worlds and publish on multiple platforms. It has invested heavily in virtual reality, hoping to support a wave of development for new VR gaming platforms.

The company says about one-third of the current 1,000 top-grossing free-to-play games, including last year's sensation, "Pokémon Go," were built using Unity software.

The company's revenue is growing quickly, powered in part by advertising it sells and places inside games. Unity is expected to make about \$300 million in revenue this year, up about 40% from roughly \$210 million last year, according to people familiar with its financial targets.

Unity's gross-profit margin is around 90%, these people said. The company has been profitable in the past, according one of these people, but isn't currently while it makes investments in virtual-reality technology.

Unity was founded in 2004 by game makers in Denmark. The company's chief executive is now John Riccitiello, the former head of console-games maker Electronic Arts Inc.

## GE Says Profit Goal Entails More Cost Cuts

By THOMAS GRYTA

Jeff Immelt, **General Electric** Co.'s chief, said the conglomerate would likely need additional cost cuts to reach a closely watched 2018 profit target, given current struggles in global oil and gas markets.

Wall Street has speculated on whether the industrial bellwether would walk back from the \$2-a-share earnings target it set three years ago, and many are doubtful the company will make it. Analysts currently expect \$1.89 a share, according to Thomson Reuters.

At an investor conference Wednesday, Mr. Immelt shared a PowerPoint slide that

showed the \$2-per-share profit target but noted it would be at the high end of expectations given current market conditions.

Reaching the goal would likely require additional cost savings, he said.

"If we wanted to take it off the page, we would have taken it off the page," Mr. Immelt told the audience. "And we didn't want to."

GE's shares were off 1.7% at \$27.81 in afternoon trading. The shares, which have attracted activist investor Trian Fund Management, have fallen 12% so far this year.

Since the setting of the 2018 profit goal, the oil-and-

gas market has been "much tougher" than expected but GE has countered the setback with cost cuts and capital-spending decisions, Mr. Immelt said.

**CEO Jeff Immelt said the energy market has been 'much tougher' than expected.**

Plans to remove \$1 billion in annual expenses from its core industrials business for both 2017 and 2018 remain

on track, he added. The cost-cutting was stepped up in March following discussions with Trian, which has been frustrated by GE missing its profit goals.

Despite the wider doubts about the goal among analysts, Trian's chief investment officer, Ed Garden, said publicly in April that GE earnings could reach as much as \$2.33 a share in 2018, in part because of the cost-cutting commitments. Barclays analysts recently said the 2018 performance postulated by Trian may not be attainable by the current management team.

Mr. Immelt said GE expects to have about \$8 billion to \$12

### BUSINESS WATCH



A Safran jet engine. The company reduced its price for Zodiac Aerospace by 15% to \$8.2 billion.

SAFRAN

#### Aerospace Supplier Cuts Bid for Zodiac

French aerospace supplier **Safran** SA on Wednesday said it

cut its bid price for **Zodiac Aerospace** SA about 15% to €7.3 billion (\$8.2 billion) after renewed profit headwinds came to light at the beleaguered plane cabin-interior specialist.

Safran in January announced a plan to buy Zodiac Aerospace to become the world's No. 3 aerospace supplier to **Boeing** Co. and **Airbus SE** behind **United Technologies** Corp. and **General Electric** Co.

The deal quickly drew fire from hedge fund TCI Fund Management, which said Safran was overpaying. TCI urged Safran to abandon the deal.

Safran on Wednesday said it would pay €25 a share for 100% of Zodiac shares. Safran originally had said it would pay €29.47 a share for Zodiac in a tender offer. It also adjusted other elements of the deal.

The deal's completion is in

part contingent on 50% of Zodiac shares with voting rights being tendered. To placate investors such as TCI who were looking for Safran to return more capital to shareholders, Safran

said if the deal goes through it would undertake a €2.3 billion share buyback over two years.

—Robert Wall and Ben Dummett

NOBLE GROUP

#### Company Continues To Explore Options

**Noble Group** Ltd. said

Wednesday it continues to explore selling more of its assets and is in talks with "various potential strategic parties" for a stake sale.

The company has appointed **Morgan Stanley** and **Moelis & Co.** to review its strategic alternatives, the embattled commodities trader said in its response to a query from **Singapore Exchange** on unusual price movement in shares on Tuesday, after shares plunged 28% to their lowest in 16 years.

Noble said it can't assure if any of the continuing discussions would result in a transaction.

—Gaurav Raghuvanshi

DONG ENERGY

#### Utility Plans to Sell Upstream Business

Danish utility **Dong Energy**,

partly owned by **Goldman Sachs Group** Inc., said Wednesday that it was selling its upstream oil and gas business to INEOS for as much as \$1.3 billion as it transitions to a pure play renewable energy company.

Dong Chief Executive Henrik Poulsen said the sale was a "major milestone" in the company's transition from a fossil-fuel provider to a "pure play renewables company."

"It's a transformation," Mr. Poulsen said in an interview.

The unit was earmarked for sale last year as Dong Energy switched its strategy to focus on building a portfolio of offshore wind, bioenergy and green distribution businesses and has been using its oil and gas business for cash to fund its renewable drive.

Mr. Poulsen credited the recovery in oil prices in recent months for making the sale finally happen.

The closing is expected to take place in the third quarter of 2017, when 440 employees will transfer to employment with the INEOS group.

**J.P. Morgan Chase & Co.** acted as exclusive financial adviser to Dong Energy in connection with the transaction.

—Dominic Chopping

### BUSINESS NEWS

## Dow-DuPont Plan Displeases Activist

By DAVID BENOIT

Tensions between activist investor Dan Loeb and **Dow Chemical** Co. are spilling back into the open.

After a year of peace, Mr. Loeb plans to publicly push for changes to the complicated combination and breakup of Dow Chemical and **DuPont** Co., according to a presentation reviewed by The Wall Street Journal.

The two chemical companies announced the megadeal in late 2015, saying they would briefly combine their sprawling businesses before splitting the merged operation into three public companies focused on agriculture, materials and specialty products. But this month Dow and DuPont said they were reviewing that plan following shareholder pressure to alter the makeup of the three new companies.

Mr. Loeb's presentation essentially says the current plan to split up the businesses doesn't go far enough to break apart Dow, echoing other investors and analysts. He first took a stake in Dow in 2014 and pressed for it to break up.

The companies said they "are fully aligned regarding the objective of the review, and we continually solicit and welcome input from our owners."

Mr. Loeb's **Third Point LLC** is pushing the companies to shift businesses between the

planned materials company, known as Dow 2.0, and the specialty-chemicals company, according to the presentation. The hedge fund wants the specialty company to be formed by four units that themselves could be separated or sold off, the presentation says.

Third Point's plan would shift businesses that generate \$3.7 billion in earnings before interest, taxes, depreciation and amortization, or Ebitda, to the specialty business, while a smaller set of businesses with some \$300 million in Ebitda would move from specialty to materials.

The presentation estimates Mr. Loeb's plan would create some \$20 billion in additional stock-market value and lead to additional cost cuts.

Mr. Loeb's decision to go public after the companies said they were reviewing the postmerger plan signals he remains concerned about Dow's decision making.

After the merger was struck in 2015, Mr. Loeb publicly called for Dow Chief Executive Andrew Liveris to step down. The two sides brokered a compromise that Mr. Liveris would depart this year after the deal closes. With the deal delayed by regulatory matters, Dow said this month that Mr. Liveris would stay through April 1 of next year. Mr. Loeb's relationship with Mr. Liveris has improved in the past year, people familiar with both sides said.



Dow Chemical and DuPont plan a complex merger and breakup.

## FINANCE &amp; MARKETS

# Treasurys Regain Foreign Appeal

Weaker dollar helps fuel the turnaround as overseas central banks add to their holdings

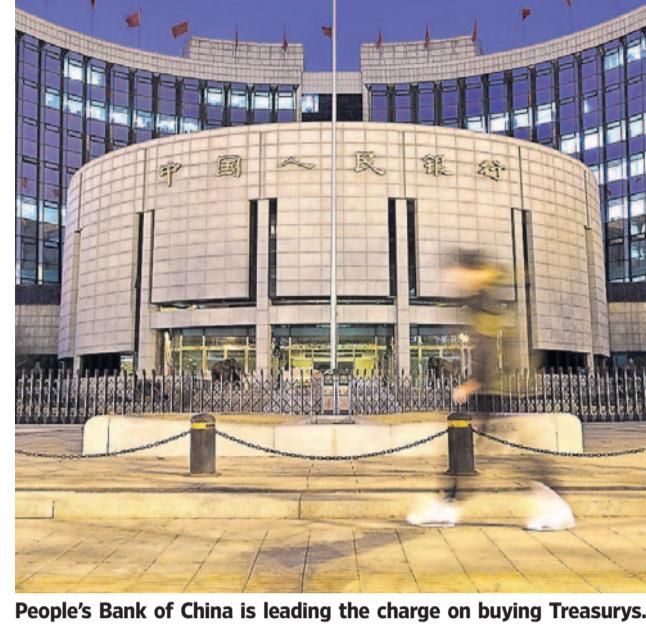
BY MIN ZENG

Foreign central banks are scooping up U.S. government bonds again after paring their holdings in 2016. And the biggest buyer this year? China.

Last year, U.S. Treasurys held by foreign central banks via the Federal Reserve's custody accounts declined by \$140 billion, sparking alarm over whether a wave of Treasury selling by central banks overseas was coming.

This year, the debt holdings have climbed by \$61 billion to \$2.92 trillion, the highest level since June 2016, according to the latest data from the week ended May 17.

There has been a similar shift by China, the second-largest foreign holder of Treasurys after Japan. In 2016, the country slashed its Treasury holdings by \$187.7 billion. But in the first quarter of 2017, China increased its holdings by \$29 billion to \$1.088 trillion, the most recent such Treasury data released on May 15 show.



**People's Bank of China is leading the charge on buying Treasurys.**

"The tide is shifting subtly," said Brad Setser, a senior fellow at the Council on Foreign Relations. "The pressure for China to sell Treasurys has eased off, given the relative stability of its foreign reserves and the Chinese yuan."

China's foreign reserves slid more than \$500 billion between August 2015—when China shocked the world with a one-time devaluation of the

yuan—and December 2016. The reserves have since rebounded from \$3.01 trillion in December to \$3.03 trillion in April.

A reversal in the U.S. dollar has helped fuel central-bank buying of Treasurys. A strengthening U.S. currency from mid-2014 to the end of last year created a negative feedback loop in emerging markets, with capital leaving developing economies, which

caused local currencies to fall.

This year, a steadily weakening dollar has helped stabilize local currencies and reduced the need for central banks to sell Treasurys and use the proceeds to intervene in the currency market.

The dollar has fallen 1.4% this year against the Chinese yuan freely traded in the offshore markets, after a 6% rally in 2016. The Chinese currency was little changed Wednesday after Moody's Investors Service cut China's sovereign credit rating, citing expectations that the country's financial strength will deteriorate.

Analysts tracking the capital-flows data have warned that they provide an incomplete picture of China's Treasury investments because the country can park its holdings in a third destination. For instance, a popular proxy to gauge China's investments has been Belgium, where Treasury holdings fell \$11.5 billion in the first three months of the year.

Still, U.S. Treasury bonds also continue to offer more attractive yields compared with their peers in Germany, Japan and the U.K. At \$13.9 trillion, the Treasury market is also still the world's biggest bond market and the most liquid, a draw

to central banks seeking a safe place to keep large cash piles.

The yield on the benchmark 10-year Treasury note was 2.266% in late New York trading Wednesday, down from 2.446% at the end of 2016. Yields fall as bond prices rise.

Purchases from foreign central banks contributed to declines in Treasury yields this year after a big rise in late 2016. That in turn has caused money managers to exit or pare back bets that bond yields would extend a climb.

During the first quarter, Saudi Arabia's Treasury holdings rose by \$11.6 billion. Russia's holdings rose by \$13.7 billion, Korea's was up by \$4.2 billion and Singapore's was up by \$2.5 billion.

But should the dollar resume its appreciation, pressure may mount for central banks to sell Treasurys.

"The wild card is the dollar," said Alejandra Grindal, senior international economist at Ned Davis Research.

"Whether the stabilization will continue depends on if the dollar strengthens significantly and how well China manages its outflows and its communication about yuan policy."

—Lingling Wei  
contributed to this article.

# Bank Is Pressed On Links To Russia

BY JENNY STRASBURG

U.S. Democratic lawmakers have asked Deutsche Bank AG to provide details about its internal reviews into Russian trades and clients, as well as loans made to President Donald Trump, according to a letter made public on Wednesday.

Rep. Maxine Waters of California, the ranking Democrat on the House Financial Services Committee, and four other Democrats in a letter dated Tuesday asked Deutsche Bank Chief Executive John Cryan to disclose materials related to any internal reviews into Mr. Trump's accounts and any connections between those accounts and Russia.

The lawmakers asked for details of any Deutsche Bank reviews of whether loans to Mr. Trump "were backed by guarantees from the Russian government, or were in any way connected to Russia."

The lawmakers also asked for due-diligence documentation and details of assets and guarantees backing the loans to Mr. Trump.

**U.S. lawmakers also asked Deutsche Bank about loans it made to Donald Trump.**

# OPEC Chief Builds Bridges

BY BENOIT FAUCON

VIENNA—During a turbulent year for oil prices, the Organization of the Petroleum Exporting Countries' top official, Mohammad Barkindo, has embraced a role as the global energy industry's chief diplomat.

Since taking over as secretary-general almost a year ago, the wisecracking 58-year-old Nigerian with a closet full of Nehru jackets has reached beyond OPEC in a way few of the cloistered cartel's officials have in the past.

Mr. Barkindo was a main architect of the agreement last year bringing together the fractious 13-nation cartel and almost a dozen other heavyweight producers for the first coordinated crude-oil supply cuts in eight years.

He served as an important channel between OPEC-member rivals Saudi Arabia and Iran, shuttling between the two countries when they didn't have diplomatic relations last year and brokering an oil-policy detente that cleared the way for a deal.

Mr. Barkindo traveled to Houston to meet U.S. shale producers this year and hosted meetings with oil traders in London and New York.

He has made a point of inviting big non-OPEC producers such as Azerbaijan to Vienna for talks.

His latest mission is to keep OPEC's fragile coalition alive



**Mohammad Barkindo is 'a diplomat rather than an expert, and that helps to get everyone in the room to get on,' one observer says.**

at this week's meeting in Vienna of OPEC members and nonmembers that have joined cuts, such as Russia, Mexico and Kazakhstan.

The group is expected to renew its pledges to withhold almost 2% of global oil supply and continue with efforts to drain a vast oversupply that has weighed down crude prices.

If it fails, analysts have said oil prices would plummet.

Helima Croft, chief commodities strategist at RBC Capital Markets and longtime observer of OPEC, said Mr. Barkindo is the modern oil industry's version of Klemens Metternich, the 19th-century Austrian Empire diplomat who helped reorient Europe's political system during the rise and fall of Napoleon.

"He is a diplomat rather than an expert, and that helps to get everyone in the room to get on," said Bhushan Bahree, a senior director on oil at U.S. consultancy IHS and a long-time OPEC watcher.

Since taking over as OPEC secretary-general last August, Mr. Barkindo has transformed a role once seen as little more than the cartel's top bureaucrat with no real role in decision making into an important ambassadorship—serving as an emissary both inside and outside the fractious group.

Mr. Barkindo plays down any efforts to elevate the role and says he is simply following his own experience through five oil-cycle downturns to get the cartel through "challenging times."

Ed Morse, the Citigroup oil

analyst who counts Mr. Barkindo as a friend, says the OPEC chief "has a mission to make OPEC relevant and to make it more professional."

But when OPEC didn't achieve Mr. Barkindo's goal of reducing vast oil supplies as quickly as some thought possible, prices slipped late last month and early this month.

Mr. Barkindo was part of the decision to frame OPEC's production cuts as a way to bring oil storage—a proxy for a global oversupply—down to a five-year average.

Mr. Barkindo's first trip after being appointed secretary-general in July was to Mecca, where he met Saudi King Salman and talked about the importance of taking action to boost oil prices.

Two months later, he flew

to Tehran, where Iranian officials had been reluctant to support production cuts because they were trying to ramp up output following the end of years of Western sanctions.

Mr. Barkindo said he got personal assurances from President Hassan Rouhani that Iran could support a production cut for OPEC. By the end of September, the framework for the OPEC cuts was agreed upon.

"He knows that when there is a block, he needs to reach out to the highest level," says Robert McNally, president of Washington-based energy consultancy Rapidan Group and a former White House energy adviser.

—Michael Amon  
contributed to this article

## FINANCE WATCH

### BANKING

#### Profits Rise Strongly At U.S. Institutions

The U.S. banking industry posted strong profits in the first quarter of 2017, though loan growth slowed during the economy's eighth year of expansion after the recession.

The Federal Deposit Insurance Corp. pegged the industry's first-quarter profits at \$44 billion, 13% higher than a year earlier. Return on equity, a measure of banks' profitability, rose slightly to 9.37%, still below the 10% figure many investors desire.

The loan-growth slowdown that began in the fourth quarter of 2016 continued. Total annual loan growth slowed to 4%.

—Gabriel T. Rubin

### CME GROUP

#### CEO Suffers A Collapsed Lung

CME Group Inc. Chairman and Chief Executive Terrence A. Duffy has suffered a collapsed lung and is recuperating at

home, the company said.

Mr. Duffy, 58 years old, underwent a procedure on his lung last week, a spokeswoman for the Chicago-based futures exchange operator said in an email.

He is "expected to make a full recovery" and return to work in about two weeks, she said.

The news emerged as the company held its annual shareholder meeting on Wednesday.

CME is the world's largest exchange operator, with a market capitalization of \$40 billion.

—Alexander Osipovich

### SIMON PROPERTY GROUP

#### Mall Landlord To Fund Upgrades

Shopping-mall landlord Simon Property Group Inc. plans to invest an additional \$1 billion to redevelop its properties for the modern retail age.

The Indianapolis-based real-estate investment trust has been renovating its malls across the U.S. It had spent \$5 billion over the past five years on the enhancements.

—Esther Fung

# Can Trump Fire This Consumer Regulator?

BY YUKA HAYASHI

WASHINGTON—A federal appeals court on Wednesday began considering whether the consumer watchdog created after the 2008 financial crisis is constitutional, and whether the president has the authority to fire its director at will.

The oral argument presented an opportunity for the Trump administration to lay out its case for curtailing the power of the Consumer Financial Protection Bureau, an independent agency fighting to keep its current structure headed by a single director.

The hearing by the full bench of the U.S. Court of Appeals for the District of Columbia Circuit came after a three-judge panel of the same court ruled in October that the bureau's structure was unconstitutional and gave the president the power to fire its director for any reason. After a request from the CFPB, the appeals court vacated the panel's ruling and scheduled a hearing by more judges.

Currently, the CFPB chief

can be removed only for "inefficiency, neglect of duty, or malfeasance."

Legal experts say the makeup of the appeals court suggests that it could rule in favor of the CFPB, although judges' nomination backgrounds don't necessarily point to how they might rule in a particular case. Six of the panel's 11 judges were nominated by Democratic presidents, while the three judges on the initial panel were Republican nominees.

A decision in favor of the CFPB would make it difficult for President Donald Trump to fire bureau Director Richard Cordray before Mr. Cordray's term ends in July 2018.

The president's authority over agency leaders has been in the spotlight following Mr. Trump's abrupt firing of James Comey as head of the Federal Bureau of Investigation. Unlike with the CFPB director, the president can remove the FBI chief at will.

"I think the Comey affair is an anecdote that provides some reasons why Congress

has chosen to insulate certain agencies from at-will removal by the president," said Leah Litman, assistant professor at the University of California, Irvine School of Law.

"To simultaneously argue that the president needs more authority to remove federal officials at will but also its constitutionality."

On Wednesday, the two parties were joined by the Trump Justice Department, which in March sided with PHH and asked the court to order a restructuring of the agency. The department argued the CFPB's structure violates the Constitution's separation-of-powers clause.

Deutsche Bank, which has previously faced similar requests for information, declined to comment through a spokesman.

More broadly, U.S. investigators, including the Federal Bureau of Investigation and congressional committees, are looking into any ties between Russian financial institutions, Mr. Trump and anyone in his orbit. Russia has denied interfering in the 2016 election. Mr. Trump has repeatedly denied any collusion between his campaign and Russia.

Deutsche Bank has faced months of scrutiny over controls around its Russia operations, including roughly \$10 billion in equity trades that are a matter of a continuing U.S. Justice Department investigation, and for its ties to Mr. Trump.

The bank lent more than \$300 million to Mr. Trump-affiliated entities, disclosures show.

Democratic lawmakers in March called for a hearing to examine Deutsche Bank's ties to Mr. Trump, in part to explore any potential conflicts of interest in government investigations. The Democratic lawmakers alone have lacked Republican support to demand documents. No hearing has been scheduled.

The letter sent Tuesday asks for a response and documentation by June 2.



**Consumer Financial Protection Bureau Director Richard Cordray**

gaged insurers and fined the company \$109 million. PHH responded by challenging not only the bureau's interpretation of the decades-old law but also its constitutionality.

On Wednesday, the two parties were joined by the Trump Justice Department, which in March sided with PHH and asked the court to order a restructuring of the agency. The department argued the CFPB's structure violates the Constitution's separation-of-powers clause.

## MARKETS DIGEST

**Nikkei 225 Index**

19742.98 ▲ 129.70, or 0.66%

High, low, open and close for each trading day of the past three months.

Year-to-date  
52-wk high/low  
All-time high

19961.55 14952.02  
38915.87 12/29/89

**STOXX 600 Index**

392.37 ▲ 0.35, or 0.09%

High, low, open and close for each trading day of the past three months.

Bars measure the point change from session's open

Year-to-date  
52-wk high/low  
All-time high

3.29%  
19961.55 14952.02  
38915.87 12/29/89

**S&P 500 Index**

2404.39 ▲ 5.97, or 0.25%

High, low, open and close for each trading day of the past three months.

Data as of 4 p.m. New York time  
Last Year ago  
Trailing P/E ratio 23.44 23.49  
P/E estimate \* 18.41 17.51  
Dividend yield 1.98 2.20  
All-time high: 2404.39, 05/24/17

Weekly P/E data based on as-reported earnings from Birinyi Associates Inc.

**International Stock Indexes**

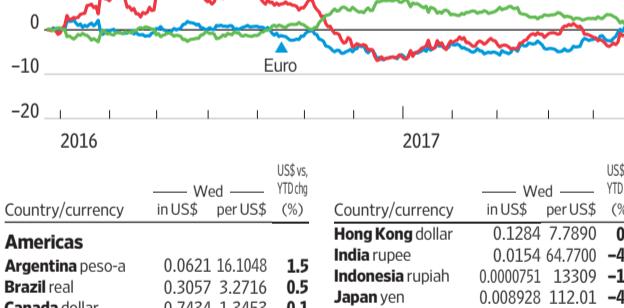
Data as of 4 p.m. New York time

Region/Country	Index	Close	NetChg	% chg	52-Week Range	Low	Close	High	YTD % chg
<b>World</b>	<b>The Global Dow</b>	2768.69	3.25	0.12	2193.75	2769.38	9.5		
	<b>MSCI EAFE</b>	1893.44	1.01	0.05	1471.88	1956.39	10.3		
	<b>MSCI EM USD</b>	1006.35	1.88	0.19	691.21	1044.05	26.7		
<b>Americas</b>	<b>DJ Americas</b>	577.60	1.51	0.26	480.90	578.17	6.9		
Brazil	<b>Sao Paulo Bovespa</b>	63452.38	789.90	1.26	48066.67	69487.58	5.4		
Canada	<b>S&amp;P/TSX Comp</b>	15418.70	-58.24	-0.38	13609.58	15943.09	0.9		
Mexico	<b>IPC All-Share</b>	49500.00	457.48	0.93	43902.25	50154.33	8.5		
Chile	<b>Santiago IPSA</b>	3696.98	22.13	0.60	2998.64	3786.05	14.7		
<b>U.S.</b>	<b>DJIA</b>	21012.42	74.51	0.36	17063.08	21169.11	6.3		
	<b>Nasdaq Composite</b>	6163.02	24.31	0.40	4574.25	6170.16	14.5		
	<b>S&amp;P 500</b>	2404.39	5.97	0.25	1991.68	2405.77	7.4		
	<b>CBOE Volatility</b>	9.92	-0.80	-7.46	9.56		26.72	-29.3	
<b>EMEA</b>	<b>Stoxx Europe 600</b>	392.37	0.35	0.09	308.75	396.45	8.6		
	<b>Stoxx Europe 50</b>	3237.51	0.42	0.01	2626.52	3279.71	7.5		
Austria	<b>ATX</b>	3204.30	21.17	0.67	1981.93	3204.49	22.4		
Belgium	<b>Bel-20</b>	3902.71	-12.11	-0.31	3127.94	4055.96	8.2		
France	<b>CAC 40</b>	5341.34	-6.82	-0.13	3955.98	5442.10	9.9		
Germany	<b>DAX</b>	12642.87	-16.28	-0.13	9214.10	12841.66	10.1		
Greece	<b>ATG</b>	766.03	-17.00	-2.17	517.10	800.08	19.0		
Hungary	<b>BUX</b>	34251.21	-479.73	-1.38	25126.36	34975.81	7.0		
Israel	<b>Tel Aviv</b>	1418.55	-0.63	-0.04	1372.23	1490.23	-3.6		
Italy	<b>FTSE MIB</b>	21369.73	-46.01	-0.21	15017.42	21828.77	11.1		
Netherlands	<b>AEX</b>	527.87	-0.30	-0.06	409.23	537.84	9.3		
Poland	<b>WIG</b>	60812.49	404.79	0.67	42812.99	62666.49	17.5		
Russia	<b>RTS Index</b>	1087.59	-9.24	-0.84	874.88	1196.99	-5.6		
Spain	<b>IBEX 35</b>	10907.40	-8.90	-0.08	7579.80	11184.40	16.6		
Sweden	<b>SX All Share</b>	586.90	0.23	0.04	443.66	593.34	9.8		
Switzerland	<b>Swiss Market</b>	9035.09	-26.67	-0.29	7475.54	9136.95	9.9		
South Africa	<b>Johannesburg All Share</b>	54308.67	-240.24	-0.44	48935.90	54716.53	7.2		
Turkey	<b>BIST 100</b>	98313.77	596.29	0.61	70426.16	98749.90	25.8		
U.K.	<b>FTSE 100</b>	7514.90	29.61	0.40	5788.74	7533.70	5.2		
<b>Asia-Pacific</b>	<b>DJ Asia-Pacific TSM</b>	1599.69	3.33	0.21	1308.52	1603.06	12.4		
Australia	<b>S&amp;P/ASX 200</b>	5769.00	8.80	0.15	5103.30	5956.50	1.8		
China	<b>Shanghai Composite</b>	3064.08	2.13	0.07	2815.09	3288.97	-1.3		
Hong Kong	<b>Hang Seng</b>	25428.50	25.35	0.10	20038.42	25428.50	15.6		
India	<b>S&amp;P BSE Sensex</b>	30301.64	-63.61	-0.21	25765.14	30658.77	13.8		
Japan	<b>Nikkei Stock Avg</b>	19742.98	129.70	0.66	14952.02	19961.55	3.3		
Singapore	<b>Straits Times</b>	3231.24	8.55	0.27	2729.85	3271.11	12.2		
South Korea	<b>Kospi</b>	2317.34	5.60	0.24	1925.24	2317.34	14.4		
Taiwan	<b>Weighted</b>	10044.42	36.58	0.37	8394.12	10044.42	8.5		

Source: SIX Financial Information/WSJ Market Data Group

**Currencies**

Yen, euro vs. dollar; dollar vs. major U.S. trading partners



London close on May 24

US\$ vs. Country/currency Wed YTD chg

Country/currency in US\$ per US\$ (%)

Europe

Bulgaria leva 0.5713 1.7505 -5.8

Croatia kuna 0.1505 6.644 -7.4

Euro zone euro 1.1179 0.8946 -5.9

Czech Rep. koruna-b 0.0422 23.673 -7.8

Denmark krone 0.1502 6.6565 -5.8

Hungary forint 0.003629 275.58 -6.4

Iceland krona 0.009912 100.89 -10.7

Norway krone 0.1192 8.3886 -3.0

Poland zloty 0.2673 3.7417 -10.6

Russia ruble-d 0.01768 56.549 -7.7

Sweden krona 0.1148 8.7095 -4.4

Switzerland franc 1.0239 0.9767 -4.1

Turkey lira 0.2798 3.5734 1.4

Ukraine hryvnia 0.0381 26.2625 -3.0

U.K. pound 1.2938 0.7729 -4.6

Middle East/Africa

Bahrain dinar 2.6522 0.3771 -0.03

Egypt pound-a 0.0552 18.1160 -0.1

Israel shekel 0.2786 3.5900 -6.7

Kuwait dinar 3.2946 0.3035 -0.7

Oman rial 2.5976 0.3850 0.003

Qatar rial 0.2746 3.642 0.04

Saudi Arabia riyal 0.2666 3.7506 -0.003

South Africa rand 0.0772 12.9604 -5.4

Sri Lanka rupee 0.0414 152.75 2.9

Taiwan dollar 0.03313 30.183 -7.0

Thailand baht 0.02909 34.380 -4.0

Corn (cents/bu.) CBOT 370.50 1.00 0.27% 393.75 360.75

Soybeans (cents/bu.) CBOT 947.75 -0.50 -0.05% 1,092.50 941.25

Wheat (cents/bu.) CBOT 431.50 2.00 0.47 488.75 416.00

Live cattle (cents/lb.) CME 120.175 -1.150 -0.95 127.500 99.400

Cocoa (\$/ton) ICE-US 1,885 -136 -6.73 2,270 1,756

Coffee (cents/lb.) ICE-US 128.55 -1.70 -1.31 161.55 128.00

Sugar (cents/lb.) ICE-US 15.60 -0.27 -1.70 20.81 15.24

Cotton (cents/lb.) ICE-US 72.92 0.55 0.76 75.72 69.81

Robusta coffee (\$/ton) ICE-EU 190.200 -34.00 -1.76 2,283.00 1,871.00

Copper (\$/lb.) COMEX 2,587.5 -0.0085 -0.33 2,8400 2,4725

## FINANCE &amp; MARKETS

# Legitimacy of SEC's Courts Challenged

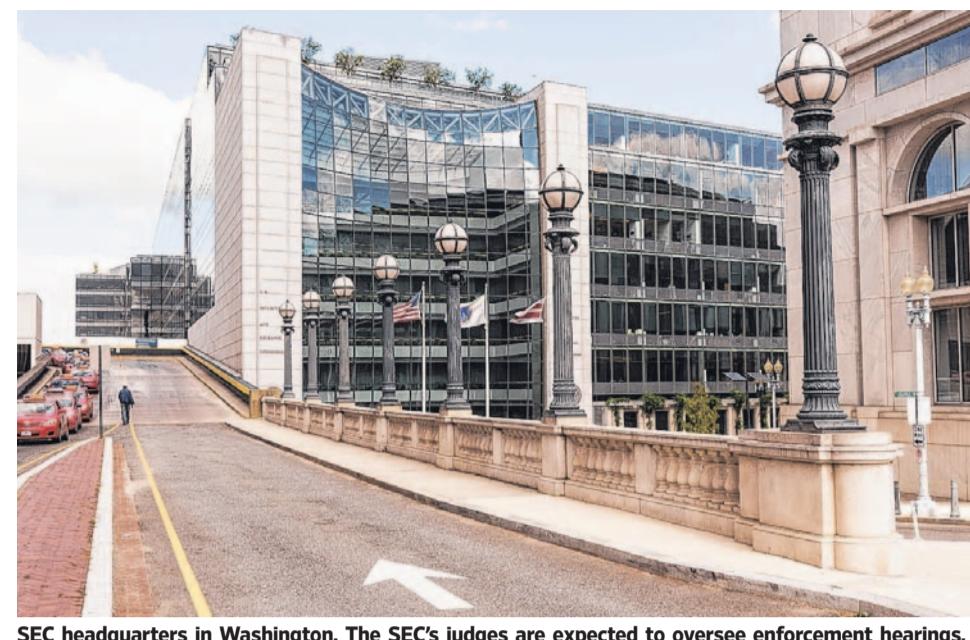
An appeals court considers whether agency vested too much power in courts

BY DAVE MICHAELS

**WASHINGTON**—A federal appeals court on Wednesday sharply questioned the powers of the U.S. Securities and Exchange Commission's in-house courts in a case that could transform how the Wall Street regulator carries out its enforcement authority.

The SEC tribunals are run by officers who have career appointments, such as U.S. district judges, but are employees of the agency. The SEC's administrative judges conduct trials and are expected to independently oversee hearings, although their decisions must be confirmed by the agency's commissioners to take effect.

Judges on the U.S. Court of Appeals for the District of Columbia Circuit probed whether the SEC's judges exercise enough power to qualify as officers who should be appointed by a presidential appointee, such as the SEC's



**SEC headquarters in Washington.** The SEC's judges are expected to oversee enforcement hearings.

commissioners. The challengers to the SEC's system say it is a fatal flaw that its judges were hired by a human-resources office. The arrangement violates a constitutional clause governing which officials must be appointed by the president or his officers, they argue.

The SEC argues its system

for hiring judges is legitimate because the decisions aren't final without the commission's involvement. But several judges on the appeals court on Wednesday questioned that principle, suggesting the SEC's judges have significant authority, including the power to decide what evidence to allow.

The person behind the ap-

peal is Raymond Lucia, a California financial adviser and radio personality who was sued by the SEC in 2012. The regulator accused Mr. Lucia of misleading investors through a strategy he called "Buckets of Money."

An administrative judge who heard Mr. Lucia's case barred him in 2013 from work-

ing as a broker or investment adviser, and fined Mr. Lucia and his company \$300,000. He appealed the ruling and, like defendants in several other SEC cases, complained the judge who sanctioned him wasn't legitimately appointed under the Constitution's appointments clause.

The SEC's in-house courts generated little controversy for decades, but a decision in 2014 to lean more heavily on the tribunals sparked a backlash. Lawyers defending clients challenged how the judges are hired, arguing their sweeping powers mean that presidentially appointed commissioners should appoint them instead of human-resources officials.

The argument is a "constitutional technicality," said Adam Pritchard, a law professor at the University of Michigan who previously worked at the SEC. But if the appeals court rules against the SEC, the opinion could disrupt the use of administrative courts at other government agencies such as the Social Security Administration.

"There is potential spillover to other administrative agen-

cies depending on how the D.C. Circuit resolves the constitutional question," said Matthew Solomon, a partner at Cleary Gottlieb Steen & Hamilton LLP who previously led the SEC's litigation unit.

That question came up during Wednesday's arguments. Mark A. Perry, an attorney for Mr. Lucia, provided a smaller number of judges who could be affected if the D.C. Circuit ruled against the SEC. Mr. Perry said there are only 142 administrative judges working for federal agencies whose powers and duties are similar to those of the SEC's judges.

"We need to think about whether that affects every administrative law judge that works for a government agency," said Judge David Tatel.

The SEC already faces pressure to change how the judges are appointed because other courts, including the U.S. Court of Appeals for the 10th Circuit, have ruled the system doesn't meet constitutional requirements.

If the SEC loses the case before the D.C. Circuit, it would likely appeal the case to the Supreme Court.

## U.S. Stocks Push Higher as Fed Hints at Rate Rise

BY CHRISTOPHER WHITTALL AND RIVA GOLD

Gains in real-estate and utilities shares pushed U.S. stocks slightly higher Wednesday as minutes from the Federal Reserve signaled interest rates could rise in June.

The Dow Jones Industrial Average rose 75 points, or 0.4%, to 21012. The S&P 500 gained 0.3% and the Nasdaq Composite added 0.4%.

In Europe, the Stoxx Europe 600 rose less than 0.1% to 392.37, with gains in travel and leisure shares largely off-

setting declines in the auto sector. Shares of **Daimler** declined 1.6% after German authorities turned up the heat in an investigation into alleged diesel-emissions fraud.

Real-estate and utilities stocks in the S&P 500 rose 0.7% and 0.5%, respectively, by late afternoon. Those sectors are often considered bondlike, because they typically pay relatively high dividends and investors tend to buy them when they are nervous about other parts of the market.

Shares of basic-materials producers in the S&P 500 rose 0.6%. Dow component **DuPont** gained 1.2% by late afternoon. U.S. stocks have climbed in

recent sessions as corporate earnings growth helped outweigh concerns over the ability of the Trump administration to push through its policy agenda, including tax cuts.

Many investors are now focusing on central-bank policy ahead of pivotal meetings next month for the Federal Reserve and the European Central Bank. Wednesday's minutes from the Fed's meeting earlier this month showed officials expected that it would "soon be appropriate" to raise short-term rates again, a signal the central bank could act in June.

The Fed's stimulus policies have helped buoy stocks and bond markets in recent years.

But many investors view rate increases as a vote of confidence in the U.S. economy that shouldn't derail financial markets, particularly if the Fed

**Higher interest rates tend to boost the profitability of certain companies.**

continues to move at a gradual pace. Higher interest rates also tend to boost the profitability of certain companies such as banks.

"You've got a lot of things stuck in a range because the forces are pretty balanced," said Russ Koesterich, co-portfolio manager of BlackRock's Global Allocation Fund. "The economy's doing OK, but not taking off. The Fed's hiking, but doing it gently. And investors are nervous about high valuations and low volatility, but there are few other places to go."

The WSJ Dollar Index, which measures the dollar against a basket of 16 other currencies, slipped 0.2%. The yield on the benchmark 10-year U.S. Treasury note fell to 2.266%, according to Tradeweb, from 2.285% Tuesday. Yields fall as prices rise.

Treasury yields and the dollar are sensitive to Federal Reserve policy, with both tending to gain when expectations of rate increases grow.

In Asia, Chinese stocks pared initial losses to end higher after Moody's Investors Service lowered the country's credit rating for the first time since 1989. The Shanghai Composite Index notched a gain of less than 0.1%.

Japan's Nikkei Stock Average gained 0.7%, while Australian stocks rose 0.2%.

In commodities, U.S. crude-oil prices slipped 0.2% to \$51.36 a barrel.

—Aaron Kurilloff contributed to this article.



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TECHNOLOGY COLUMNISTS

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## MARKETS

# Blackstone's Bridge and Tunnel Man

Sean Klimczak hustles infrastructure projects as firm raises money for public works

By RYAN DEZEMBER

When Blackstone Group LP was competing for the chance to finance a natural-gas export terminal, Sean Klimczak dropped his weekend plans and raced across the country for a meeting with the energy company's CEO. He didn't have a suit in hand, but no matter, he bought one when he arrived.

Blackstone's rival for the \$1.5 billion deal was a group of smaller investment outfits. Blackstone won the deal, and Cheniere Energy Inc.'s facility was built and became the first to ship U.S. shale gas abroad. For Mr. Klimczak, one key to victory was the advantage of being able to write a big check quickly without wrangling with partners.

Now Mr. Klimczak is ascending to a position in which he should be able to write many more 10-figure checks. Blackstone has tapped the 40-year-old to lead its new infrastructure business, which is aiming to raise \$40 billion in a fund focused on building and buying U.S. public works.

Blackstone said that it expects the fund to have buying power of about \$100 billion once debt is added to the mix, and that it will have a broad mandate to invest in assets ranging from power plants and pipelines to water systems, roads, bridges, airports and hospitals.

The firm's plans were unveiled Saturday after officials with Saudi Arabia's Public Investment Fund disclosed in Riyadh as part of President Donald Trump's visit that they had agreed to seed the fund with \$20 billion.

The Saudi commitment alone would be the largest pri-



Mr. Klimczak is attempting to raise \$40 billion for a fund dedicated to assets such as power plants, pipelines, airports and hospitals.

vate infrastructure fund ever raised, eclipsing the \$15.8 billion raised by Global Infrastructure Partners this year. It is the most ambitious launch of a business line, by initial size, in the 32-year history of Blackstone, which is a leader in its four other segments: real estate, private equity, hedge funds and credit.

"We already have government agencies calling with infrastructure proposals that require billion-dollar-plus equity checks," Blackstone President Hamilton "Tony" James said in an interview.

The plans have also piqued Wall Street's interest. Blackstone's shares have risen 8.7% since the announcement, to their highest point in nearly two years.

Jefferies LLC analysts estimate that once all the \$40 billion is raised, the business could annually generate \$300 million in management fees alone for Blackstone.

The new fund is what is called a permanent capital fund, meaning it has no deadlines to cash out of investments. Mr. Klimczak said he expects the ability to hold investments for potentially decades will help persuade government officials to work with the firm.

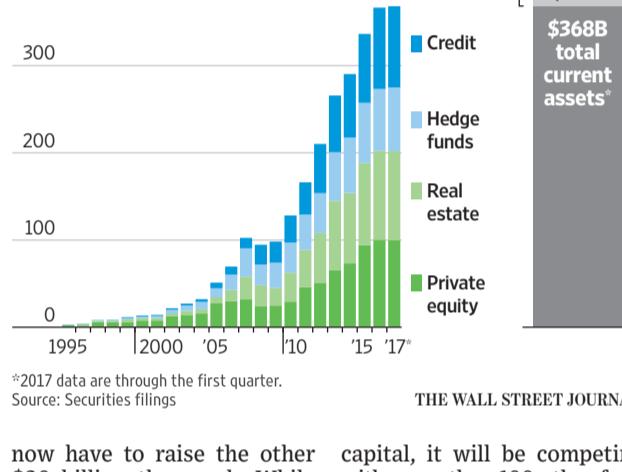
"Why is Warren Buffett welcomed in the utility sector? It is because he has long duration capital. Having the ability to tell a utility commission that you don't ever have to sell is quite powerful," he said.

Still, it is unclear how profitable the venture can be. Big infrastructure deals come with risks that are uncommon in corporate takeovers, from politicians who change their minds or are voted out of office mid-project to construction and permitting processes that can drag on for years and blow out budgets.

Also, Mr. Klimczak and other Blackstone executives

now have to raise the other \$20 billion they seek. While Blackstone has shown the ability to raise huge amounts of capital, it will be competing with more than 100 other fund managers who are collectively seeking to raise more than

## Blackstone's assets under management



\$100 billion for other infrastructure funds, according to industry tracker Prequin.

A native of Tampa, Fla., Mr. Klimczak was the first in his family to go to college, graduating from the University of Notre Dame. He worked a stint at Morgan Stanley as a mergers and acquisitions banker and briefly at Madison Dearborn Partners LLC, a Chicago based buyout shop, before enrolling at Harvard Business School, where he graduated first in his class in 2005.

He arrived at Blackstone later that year and started out as a generalist in the private-equity group and soon homed in on energy, particularly power and electricity transmission deals.

In that role, he has overseen construction of wind farms in Mexico and Germany, power plants in Canada and the Philippines, and a hydro-power dam on the White Nile that provides roughly half of Uganda's electricity.

Mr. Klimczak began meeting with Saudi officials in April 2016 about an infrastructure fund that would never expire, allowing Blackstone to take on projects that took years to bear fruit and sometimes had lower returns than private-equity fund investors sought. Blackstone executives say strong political support for infrastructure spending from both U.S. political parties during the presidential campaign made it an inviting time to start a dedicated fund, which it had tried and failed to do a decade earlier.

Mr. Klimczak "understands the social mission that is associated with infrastructure," Mr. James said, offering the Uganda power-generating dam as an example. "When we first looked at [it], we couldn't get the numbers to work. Sean said, 'Guys, this is transformational for the country. We have to do this.' So we went back to the drawing board and figured it out."

## HEARD ON THE STREET

FINANCIAL ANALYSIS & COMMENTARY

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## Fannie, Freddie Look to Future

### New Asset Class

Volume of mortgages covered by Fannie Mae's and Freddie Mac's new credit-risk transfers



Sources: Federal Housing Finance Agency; Associated Press (photo)

THE WALL STREET JOURNAL



Fannie Mae headquarters in Washington

for the mortgage market. "If there is a guarantee, we would want to make sure that there is ample credit and real risk in front of that guarantee, so that taxpayers are not at risk," he said.

These comments suggest the Trump administration's thinking is in line with a range of compromise proposals put forward by private think tanks, the Mortgage Bankers Association and others. These plans would dra-

matically restructure Fannie and Freddie, and put in place a federal guarantee on certain mortgage securities. This protection would kick in after private investors have taken initial losses through the new "credit-risk transfer" market.

Under most of these plans Fannie and Freddie would still exist, but with a more limited role, perhaps as utility-like mortgage guarantors.

That may not be the most

profitable outcome for Fannie and Freddie shareholders, but they aren't the only stakeholders in this debate. The new government guarantee would ensure a steady flow of investment into the trillion-dollar mortgage-backed-securities market, keeping mortgage rates low.

Investors willing to take on some repayment risk in exchange for higher returns could do so in the new credit-risk transfer market.

Fannie and Freddie have been unloading credit risk on mortgage pools with securities and reinsurance contracts through this experimental market since 2013.

There remain important questions on compromise plans like these, notably how the system would cope with a pullback of private risk capital during a housing downturn. Housing market participants across the board should look past the weekly Washington battles over Fannie and Freddie, and be encouraged that a long-term solution is now emerging.

—Aaron Back

### OVERHEARD

It is common for journalists to move into public-relations roles late in their careers. Movement in the other direction is less common. And moves involving fishing journalism are rarer still.

But **Jon Diat** will prove to be an exception. Mr. Diat is preparing to retire after a nearly five-year stint as the head of external communications at **American International Group**.

He is a true industry veteran, having previously worked at Citigroup through the 2008 financial crisis, and before that in various media relations roles at **J.P. Morgan Chase, Morgan Stanley, Standard & Poor's** and more.

Mr. Diat will now start writing a weekly column on commercial and recreational fishing for the East Hampton Star in New York state. His first column comes out on Thursday.

Representing financial companies during their tough times will help Mr. Diat with the most important trait of a good fisherman, patience.

### Glencore's Bunge Jump Needs Work

Having repaired its balance sheet and watched global-growth optimism push its share price skyward, **Glencore** is back to its deal-making ways. That won't be a bad thing if it chooses its targets wisely. An informal approach to U.S. trading giant **Bunge**, now worth \$10 billion, looks like a good start, but sealing a deal is unlikely to prove easy.

A move into the U.S. soy-and corn-trading business makes sense given cheap valuations: While Glencore's main metals and mining business has benefited from copper and coal prices being 25% and 50% higher than a year ago, respectively, corn prices are almost 10% lower after last year's bumper harvest. That divergence is reflected in corporate valuations: Bunge's stock was pummeled after its first-quarter net income fell 80% year over year.

Glencore's relative advantage might not last. China's economy, which consumes about half the world's copper supply, is slowing, while hopes for a big U.S. infrastructure boost have faded.

Glencore's problem is that Bunge is likely to conclude that it shouldn't do a deal when the cycle is poised to turn in its favor. Indeed, Bunge has said it isn't engaged in formal talks with Glencore, although the stock jumped nearly 20% after news of the overture broke.

Glencore has long wanted a bigger footprint in the agricultural-trading world, to break the stranglehold of the so-called ABCD firms: Bunge, along with **Archer Daniels Midland, Cargill and Louis Dreyfus**. It may yet get its way, but for Bunge, the price would need to be very right.

—Nathaniel Taplin

## Investors' Faith in Michelin Is Looking Overinflated

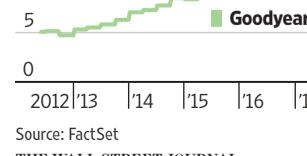
Tire companies are coming under pressure. **Michelin** in particular could default.

Margins at the storied French group have ballooned since the financial crisis, from a trough of 5.6% in 2008 to about 13% last year. It has been helped by both a strong car market and falling commodity prices.

These tailwinds are now turning into headwinds. The price of natural rubber, which accounts for a quarter of Michelin's raw-material costs, bounced back in the second half of last year, following OPEC-style export cuts by a cartel of East Asian producers. Although the price has fallen back again since Febru-

### Tire Fatigue?

Operating margins, past 12 months



ary, it remains about 45% above last year's nadir. Synthetic rubber—another quarter of Michelin's input costs—is a derivative of oil, which is also getting more expensive.

Meanwhile, the car market is showing signs of peaking after years of strong sales growth. New vehicles accounted for only 12% of Michelin's sales last year—it makes more money replacing tires on old cars—but its car margins have historically tracked industry sales. The downturn is clearest in the U.S., where the company makes 30% of its revenue: Seasonally adjusted vehicle sales for the year through April totaled 17.2 million, down from 18.7 million in December. Europe, the company's other key market, remains robust overall, but with the U.K. now weakening, a downturn seems likely

within a couple of years.

Michelin points to its experience in 2011 and early 2012, when rubber prices also surged, as evidence it can pass raw-material costs to its customers. But the U.S. car market was strong in those years, while the European one was bottoming out after the sovereign-debt crisis.

Investors won't have to wait long to find out. Retailers bought lots of tires in the first quarter in anticipation of price increases, which Michelin says were up to 8%, effective April 1. Figures for the rest of the year are likely to be much weaker as this inventory buildup unwinds. In April, marketwide tire

sales were down 4% in North America and 15% in Europe.

Higher prices may also push consumers toward the slightly cheaper tires made by increasingly established East Asian manufacturers like Hankook, Nexen and Cheng Shin.

The biggest problem is that there is little hint of these risks in Michelin's share price, which is close to a record both in absolute terms and relative to profits.

The current price/earnings ratio of 12 compares with just seven for U.S. peer **Goodyear**. As tougher times approach, investors' faith in Michelin looks overblown.

—Stephen Wilmot