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The new world disorder

A SPECIAL REPORT

The world this week

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Brazil reported a record 35,000 new cases of **covid-19** in a day. Even that grim figure is widely regarded as an undercount. India is now recording tens of thousands of new infections each week. In America, Florida, Texas and Arizona set daily records for new cases. Although many places are easing lockdowns, Anthony Fauci, the leading adviser to the White House on infectious diseases, warned that the pandemic is far from over: "The numbers speak for themselves." See article.

Beijing went into "wartime mode" to battle an outbreak of covid-19, the first in the Chinese capital after eight weeks with no cases reported of local transmission. Many of the cases are linked to a wholesale food market. See article.

A court in **China** sentenced the country's former insurance regulator, Xiang Junbo, to 11 years in prison for accepting 18m yuan ($2.5m) in bribes. Mr

Xiang had also served as deputy governor of the central bank.

At least 20 **Indian** troops were killed in a fight with **Chinese** soldiers in the Galwan valley, the first combat deaths on the disputed Sino-Indian border in 45 years. China did not say how many of its soldiers died. The brawl involved nail-studded clubs and stones rather than guns. Tensions have increased since April, when the Chinese army encroached on Indian-claimed territory. See article.

North Korea blew up the building used for meetings between its officials and those from **South Korea**. It said the explosion was retaliation for unflattering leaflets about its supreme leader, sent over the border via balloons by defectors, whom North Korea called “rubbish-like mongrel dogs”. See article.

A court in the **Philippines** found Maria Ressa guilty of libel for alleging links between a businessman and a judge. Ms Ressa is the boss of Rappler, a news website that is critical of the country’s strongman president, Rodrigo Duterte. Her lawyer said the message to other journalists was “Keep quiet, or you’ll be next.”

Steven Mnuchin, America’s treasury secretary, said his government will nominate Mauricio Claver-Carone, a staff member of Donald Trump’s National Security Council, to lead the **Inter-American Development Bank**. All the bank’s four presidents since its founding in 1959 have been from Latin America. The US has 30% of the bank’s shares, the largest stake of any country. See article.

Venezuela’s Supreme Court removed the leaders of two opposition parties, Justice First and Democratic Action. It replaced them with men whom the parties had previously expelled for being stooges of Nicolás Maduro, the country’s dictator.

America’s Supreme Court ruled that the 1964 Civil Rights Act makes it illegal to fire workers for being **gay or transgender**. More than half the states allowed such discrimination. The 6-3 majority decision was written by Neil Gorsuch, a Trump appointee. See article.

The White House tried to stop publication of a book by **John Bolton**, a former national security adviser, claiming that it contained classified information. The book says that Donald Trump tried to persuade Xi Jinping, China's president, to buy American farm goods to help his re-election campaign. It also alleges that in a meeting with Mr Xi, Mr Trump said he approved of China's policy of putting Uighur Muslims in internment camps. On June 17th Mr Trump signed a bill that imposes sanctions on Chinese officials who were responsible for the Uighurs' internment. See article.

A white policeman in **Atlanta** who shot dead a black man when he took the officer's Taser weapon was charged with murder. Republicans in the Senate unveiled their own set of police reforms. These are less radical than those put forward by Democrats but support the creation of a database to track police officers with a record of misconduct.

Boris Johnson, Britain's prime minister, announced that **Britain's** Department for International Development would be folded back into the Foreign Office. British aid will now focus less on ending poverty and more on advancing British foreign-policy goals. See article.

Yousef al-Otaiba, a diplomat from the **United Arab Emirates**, wrote in an **Israeli** newspaper that any unilateral annexation of West Bank territory would harm Israel's relations with Arab countries. It is thought to be the first-ever opinion piece written by an official from the Gulf for an Israeli newspaper.

America imposed new sanctions on **Syria** that target any person, company or institution—Syrian or foreign—that does business with or provides support to the regime of President Bashar al-Assad. See article.

There were more demonstrations in **Lebanon**. The government began injecting more American dollars into the market in an effort to support the local currency. Early talks with the IMF over a bail-out package have been shaken by concerns that the government is not serious about reform.

A judge overseeing a corruption trial in the **Democratic Republic of Congo** was murdered. Police initially said that the judge had had a heart attack, but an autopsy showed he had died from brain injuries after being stabbed in the head.

Coronavirus briefs

A randomised trial conducted by scientists at Oxford found that **dexamethasone**, a cheap steroid drug found in many countries, reduced the death rates for patients on ventilators by 35% and by 20% for those needing oxygen. See article.

The president of **Honduras**, Juan Orlando Hernández, said he and his wife have covid-19.

The remaining lockdown restrictions were lifted in **France**, enabling bars and restaurants to reopen fully. In **England** all shops were allowed to open their doors to customers again.

Next year's **Oscars** ceremony was postponed by two months until April 25th. It is not yet clear whether the event will be held in a theatre or virtually.

The **English Premier League** resumed its season, three months after it was suspended. The football matches are being played behind closed doors.

Business this week

Jun 20th 2020 |

The **Federal Reserve** clarified its new bond-buying strategy, announcing that it would acquire individual corporate bonds on the secondary market. This comes on top of its purchases in exchange-traded funds, which include some junk-rated funds that track debt. But the central bank's latest move comes almost three months after it first announced emergency measures to shore up markets. Questions have been raised about the length of time it has taken to roll out some of its programmes. See article.

Stockmarkets rallied in response to the news from the Fed, making up for some of the heavy losses they racked up in the week ending June 12th, which was the worst for the S&P 500 and Dow Jones Industrial Average since mid-March.

The Trump administration said it would let American tech firms work with **Huawei** on creating international standards for 5G. The decision represents a long-expected easing of the sanctions placed on the Chinese provider of telecoms networks and equipment over national-security concerns. America did not have much choice. Huawei's size and expertise makes it one of the companies integral to setting the rules on international networks.

America's Justice Department put forward proposals that roll back the immunity of **social-media firms** for content posted on their platforms. Donald Trump signed an executive order recently rescinding the protections after he got into a spat with Twitter, but it is unlikely to be upheld once it is challenged in court.

Robert Lighthizer, the US trade representative, confirmed that America had pulled out of talks with the EU that had sought to find common ground on **taxing tech companies**. America argues that such levies will disproportionately hit its global giants, such as Apple and Google, and has threatened to retaliate with sanctions if European countries impose their own digital tax.

Facebook launched a payment service on its WhatsApp platform in Brazil. Brazilians can link their credit or debit cards to **WhatsApp Pay** to send money to each other or buy goods from small firms. Facebook had hoped India would be the first country to use the facility nationwide, but became bogged down in regulatory objections there.

Shop till you drop

The Economist

Retail sales in America surged last month by 17.7% over April, more than double the amount that had been expected. That followed a 14.7% decline in April. Sales were still down by 6.1% compared with May last year. It is thought that the government's stimulus measures to households helped fuel the shopping spree, and that consumers might not spend so much when the money runs out.

In America's biggest IPO so far this year, **Royalty Pharma** raised $2.2bn when it listed on the Nasdaq exchange. The company invests in the rights to royalties on future drug sales across the life sciences, combining scientific expertise with capital investment for the industry. Royalty's share price leapt by more than half on the first day of trading.

Acknowledging that demand for energy will remain weak in the aftermath of covid-19 and that governments "will accelerate the pace of transition to a lower carbon economy", **BP** said it would write down the value of its oil and gas assets in the second quarter by between $13bn and $17.5bn. To buttress its balance-sheet the energy giant reportedly raised $12bn through a sale of hybrid bonds.

In its first forecast for 2021, the International Energy Agency said that **demand for oil** would increase by 5.7m barrels a day next year to 97.4m. That is still below the average for 2019, mostly because the aviation industry will still struggle in 2021. However, China's "strong exit from lockdown" saw its demand for oil in April rebound back almost to the level it was at a year ago.

In a rare admission of corporate wrongdoing on homicide-related charges, **PG&E** pleaded guilty to 84 counts of involuntary manslaughter in relation to the Camp Fire disaster in California two years ago. The electric utility's faulty equipment sparked the inferno. Its chief executive (who was not in charge at the time of the fire) pled guilty to each one of the deaths of the 84 victims of the fire as their names were read out alphabetically. The company is soon to exit bankruptcy protection.

Everybody Hertz

Hertz postponed a sale of new shares after the Securities and Exchange Commission raised objections. A judge had earlier allowed the sale to proceed, an unprecedented ruling for a company that has filed for bankruptcy protection. The car-hire company had warned potential buyers of the stock that they stand to lose their shirts unless there is a significant and "currently unanticipated improvement" in its business, which has been hammered by the pandemic.

KAL’s cartoon

Jun 20th 2020 |

Economist.com Kal

Leaders

Politics and the pandemic

Britain has the wrong government for the covid crisis

It has played a bad hand badly

Jun 18th 2020 |

THERE WAS a lot going on in Britain in early March. London staged an England-Wales rugby match on March 7th, which the prime minister attended along with a crowd of 81,000; on March 11th Liverpool played Atletico Madrid, in front of a crowd of 52,000 fans, including 3,000 from Spain; 252,000 punters went to the Cheltenham Festival, one of the country's poshest steeplechase meetings, which ended on March 13th.

As Britons were getting together to amuse themselves and infect each other, Europe was shutting down. Borders were closing, public gatherings being banned. Italy went into full lockdown on March 9th, Denmark on March

11th, Spain on March 14th and France on March 17th. Britain followed only on March 23rd.

Putting in place sweeping restrictions on everyday life was a difficult decision, fraught with uncertainty. Yet the delay is just one example of the government's tardiness. Britain has been slow to increase testing, identify a contact-tracing app, stop visits to care homes, ban big public events, provide its health workers with personal protective equipment (PPE), and require people to wear face coverings on public transport. As this wave of the disease ebbs, Britons are wondering how they came to have the highest overall death rate of any country in the rich world, and why leaving lockdown is proving so difficult.

The evidence so far suggests that the British government played a bad hand badly. The country was always going to struggle. The virus took off in London, an international hub. Britain has a high proportion of ethnic-minority people, who are especially vulnerable to the disease. And Britons are somewhat overweight, which exacerbates the impact of the infection.

Britain has got some things right. Its researchers have been in the forefront of the race to find drugs and create vaccines against the disease. On June 16th a trial by Oxford University, the first to identify a life-saving medicine, showed that a cheap steroid can reduce mortality among the sickest patients by a third. A swift reorganisation of the National Health Service put paid to fears that it would be overwhelmed. But the government has wasted the most precious commodity in a crisis: time. In a federal system, like America's, the central government's failings can be mitigated by state and local authorities. In a centralised system, they cannot.

Hindsight is a fine thing, and offers a clarity that is absent in the blizzard of events. Yet it is now plain that Britain's scientists initially argued for the wrong approach: accepting that the disease would spread through the population, while protecting the vulnerable and the health service. Neil Ferguson, an epidemiologist at Imperial College London, estimates that had Britain locked down a week earlier, at least half of the 50,000-or-so lives that have been lost would have been saved. This is more Britons than have died in any event since the second world war.

In retrospect, the government should have probed the scientists' advice more deeply. Some of it was questionable. The received wisdom that people would tire of social distancing, and that shutting down early would mean loosening early too, was just a hunch. Even after the evidence changed, and it became clear the country was heading for catastrophe, the government was slow to impose the sort of lockdown seen across Europe.

Yet you do not need hindsight to identify other mistakes. Delays in fixing PPE supply chains, promoting face coverings and increasing testing capacity were clearly errors at the time. Despite the urging of the country's scientists and the World Health Organisation, by the middle of April Britain was still carrying out just 12,000 tests a day, compared with 44,000 in Italy and 51,000 in Germany. Because most testing was reserved for hospitals, care homes struggled to find out which of their residents and staff were infected. Competition for PPE was fierce, so they also struggled to get the kit they needed to protect their workers.

The government is not solely to blame. The pandemic made new demands on the system. Some crucial bits of machinery did not work. The publicly owned company which supplies the health service with PPE failed. Public Health England, which was responsible for testing and tracing, failed. But there was a failure of leadership, too. When systems break it is the government's job to mend them; when the evidence argues for drastic measures ministers need to take them.

Britain is still living with the consequences. The spread of the virus and the devastation it has wrought have made leaving lockdown difficult, as shown by the halting return of pupils to school. Only five year-groups have gone back, many parents are choosing to keep their children at home, and the government has abandoned an earlier ambition to get more in. The "world-beating" contact-tracing system still lacks its app, which is not due to arrive until winter. Slow progress at suppressing the virus will have grave economic consequences, too.

These shortcomings have claimed many victims. Among them is public trust. Britain went into this crisis with a powerful sense of unity and goodwill towards the government. Now Britons think worse of their government's performance during the crisis than do the citizens of any of

22 countries polled by YouGov, aside from Mexico. That reflects the government's mistakes and its hypocrisy, after the prime minister's main adviser broke its own rules about when to travel—and kept his job. While the world waits for a vaccine this lack of trust will make managing the disease a lot harder.

The painful conclusion is that Britain has the wrong sort of government for a pandemic—and, in Boris Johnson, the wrong sort of prime minister. Elected in December with the slogan of "Get Brexit Done", he did not pay covid-19 enough attention. Ministers were chosen on ideological grounds; talented candidates with the wrong views were left out in the cold. Mr Johnson got the top job because he is a brilliant campaigner and a charismatic entertainer with whom the Conservative Party fell in love. Beating the coronavirus calls for attention to detail, consistency and implementation, but they are not his forte.

The pandemic has many lessons for the government, which the inevitable public inquiry will surely clarify. Here is one for voters: when choosing a person or party to vote for, do not underestimate the importance of ordinary, decent competence. ■

Geopolitics

The new world disorder

If America pulls back from global institutions, other powers must step forward

Jun 18th 2020 |

Seventy-five years ago in San Francisco 50 countries signed the charter that created the United Nations—they left a blank space for Poland, which became the 51st founding member a few months later. In some ways the UN has exceeded expectations. Unlike the League of Nations, set up after the first world war, it has survived. Thanks largely to decolonisation, its membership has grown to 193. There has been no third world war.

And yet the UN is struggling, as are many of the structures, like the World Trade Organisation (WTO) and the Nuclear Non-Proliferation Treaty (NPT), designed to help create order out of chaos. This system, with the UN at its apex, is beset by internal problems, by the global struggle to cope with the rise of China, and most of all by the neglect—antipathy even—of the country that was its chief architect and sponsor, the United States.

The threat to the global order weighs on everyone, including America. But if the United States pulls back, then everyone must step forward, and none more so than the middling powers like Japan and Germany, and the rising ones like India and Indonesia, which have all become accustomed to America doing the heavy lifting. If they hesitate, they will risk a great unravelling—much like the nightmare in the 1920s and 1930s that first impelled the allies to create the UN and its siblings.

The UN is bureaucratic and infuriating. Its agencies fall prey to showboating and hypocrisy, as when despots on its Human Rights Council censure Israel yet again. The Security Council gives vetoes to Britain and France, much diminished powers since 1945, but no permanent membership to Japan, India, Brazil, Germany or any African country. Alas, it looks virtually unreformable.

Nonetheless, the global order is worth saving. As Dag Hammarskjold, a celebrated secretary-general, said, the UN "was not created to take mankind to heaven, but to save humanity from hell." Our special report this week explains how the UN does that essential job, as do many other multilateral institutions. Its peacekeepers protect 125m people on a budget only a bit bigger than New York City Police Department's. It says it is helping provide life-saving assistance to 103m. For all the Security Council's flaws, it would be missed.

That is because, left to themselves, countries drift into antagonism. Witness the fatal clash of Indian and Chinese forces this week over a border dispute both sides are too proud to defuse (see article). Multilateral endeavours like the UN, NATO and the NPT cannot ensure peace, but they do make war less likely and more limited. France and its allies are helping contain the conflict spreading across the Sahel.

Without a multilateral effort, old problems are likely to deepen—even Syria, after nine bloody years, will one day be ready for the UN envoy's plans for peace. Meanwhile new problems are more likely to go unsolved. The pandemic is an example. The virus not only calls for global solutions, like treatments and vaccines, but it also aggravates local insecurity (see article). It is the same with climate change and organised crime.

Protecting the system from the forces of disorder is easier said than done. One threat is antagonism between America and China, which could create gridlock in global bodies, exacerbated by competing parallel financial and security arrangements. Another is that America may continue its careless treatment of multilateral institutions—especially if President Donald Trump behaves as badly in a second term as a devastating new book by John Bolton, his former national security adviser, says he has in his first (see article). Mr Trump has undermined the World Health Organisation and the WTO, and this month said that he would pull out a third of the American troops stationed in Germany, enfeebling NATO and limiting America's scope to project power from Europe into Africa.

Happily, the world has not yet reached the point of no return. For decades the middling powers have depended on America for the system's routine maintenance. Today they need to take on more of the work themselves. France and Germany have created an alliance for multilateralism, an initiative that is open to other countries. Another idea is for nine democracies, including Japan, Germany, Australia and Canada, which together generate a third of world GDP, to form a "committee to save the world order".

Although America is dominant, other countries can still get things done—with or without help from the White House. Sometimes the aim is to bind in America. After a chemical-weapons attack on Sergei Skripal, a Russian ex-spy living in Britain, Western countries' imposition of sanctions on the Kremlin swept up America, too. The Quad is an emerging coalition between India, Australia, Japan and America, which are all alarmed at Chinese expansion, including in the South China Sea (see article).

Sometimes, however, the world must work without America even if that is second-best. After Mr Trump walked away from the Trans-Pacific Partnership, a huge trade deal, the other members went ahead on their own. Stymied at the WTO, countries are instead forming regional and bilateral trade arrangements, such as one between Japan and the European Union and another between 28 countries in Africa.

Defending the international order is necessary, too. China's stature is growing along with its contributions—it now pays 12% of the UN budget compared with 1% in 2000. Its diplomats head four of the UN's 15 specialised agencies, and America just one. If other countries do not act, the system will come to reflect China's expansive views of national sovereignty and resistance to intervention, even in the face of gross human-rights violations.

Some think the job of middling powers is triage, to keep the system going until America returns to the party under a different president. It is more than that. Although polls suggest that most Americans would like to play a bigger global role, there is no going back to the "unipolar moment" after the Soviet collapse, when America ran the show single-handed. Not only did that provoke a backlash abroad, exploited by Russia and China, but it also stirred up resentment at home.

At the time, President Barack Obama responded by asking like-minded countries to help America make the world safe. They shrugged. They must not make the same mistake again. ■

Elephant v dragon

How to end the perilous Indo-Chinese border spat

To avoid escalation, both sides should agree on the "Line of Actual Control"

Jun 18th 2020 |

In the ancient Chinese game of Go, clever players ignore little battles in favour of strategic plays. Leaving local disputes unresolved means that later, when the game tightens and the enemy is off-guard, you can snatch prizes at lower cost. In the 69 years since China truly became India's neighbour by grabbing Tibet, the world's two most populous countries have played a similar game. Even as their leaders summited and trade thrived, the Asian giants left a mess of territorial disputes to fester.

Mostly these claims, over some 130,000 square kilometres on either side of their 3,488km-long border, have not mattered much. Despite a Chinese "lesson-teaching" invasion in 1962, rare armed skirmishes and less rare fisticuffs between patrols, the border zone has remained relatively calm. Much of it is too rugged and empty to fight over. So long as neither side shifts the status quo, what difference does it make if there are no proper markers on long stretches of border, but instead just a fuzzy “Line of Actual Control”?

A brutal clash on June 15th provided a loud and ugly answer (see article). Details remain sketchy. At least 20 Indian soldiers died, many after tumbling into an icy river. India says the Chinese also suffered casualties. China says little (see article). The death toll is the worst in any clash between the two since 1967, and the first loss of life since 1975.

Even worse, the skirmish cannot be explained away as an isolated incident. This spring China deployed far heavier forces than usual. It has pushed them forward not at one point but at many, say Indian sources, in effect seizing as much as 60 square kilometres of land that India views as lying on its own side of the line. A particular concern is China’s westward extension along the Galwan river, threatening a strategic road that runs parallel to the border and forms the main link to India’s northernmost outposts. Not surprisingly, this is where the deadly clash erupted.

Why would China change the status quo, angering a big nuclear-armed trading partner? Because, say Indian cynics, India is distracted just now by a swelling pandemic and shrinking economy, and saddled with a government better at chest-thumping than at strengthening its army or building alliances. Nonsense, say India’s critics. It is India that has changed the status quo, quietly expanding infrastructure in contested regions even as, after stripping its part of Kashmir of statehood last August, its leaders boasted of soon “regaining” other parts, including a chunk that Pakistan gave to China in 1963.

China may also see an interest in teaching India that, should it continue to flirt with closer ties to America, it will pay a price. To their credit, officials on both sides have avoided whipping up popular anger, stressing instead the importance of implementing an earlier deal to pull forces back. Such gentlemen’s agreements have calmed tempers in previous clashes.

Yet whatever the efficacy of generals meeting in windblown tents, it is a reckless way to fix problems between two rising nuclear powers that are home to a third of humanity. India has previously suggested that, as a second-best to a formal agreement over where the border lies, the two sides should at least present maps showing their view of where the line of control runs in practice. China, perhaps thinking itself the more astute Go player, has always refused to do so. This allows it to claim that any Indian move is a violation of its own understanding.

It is time to stop playing games. China looks stronger just now but India, if pushed, will find ways to cause it pain. And the last thing the wider world needs is an escalating slugfest between a dragon and an elephant over a lofty patch of frozen earth.■

The trouble with climate finance

Green investing has shortcomings

The financial system and climate change

Jun 18th 2020 |

THE FINANCIAL industry reflects society, but it can change society, too. One question is the role it might play in decarbonising the economy. Judged by today's fundraising bonanza and the solemn pronouncements by institutional investors, bankers and regulators, you might think that the industry is about to save the planet. Some 500 environmental, social and governance (ESG) funds were launched last year, and many asset managers say they will force companies to cut their emissions and finance new projects. Yet, as we report this week (see article), green finance suffers from woolly thinking, marketing guff and bad data. Finance does have a crucial role in fighting climate change but a far more rigorous approach is needed, and soon.

One of the shortcomings of green finance might be called “materiality”. Some fee-hungry fund managers make hyperbolic claims about their influence, even as big-business bashers pin most of the blame for pollution on companies. The reality is more prosaic. Fund managers have some influence over a big slice of the economy, but many emissions occur outside the firms they control. Estimates by *The Economist* suggest that publicly listed firms, excluding state-controlled ones, account for 14-32% of the world’s total emissions, depending on the measure you use. Global fund managers cannot directly influence the bosses of state-controlled Chinese coal-fired power plants or Middle Eastern oil and gas producers.

Some European bank regulators hope to cut emissions indirectly, by imposing climate-stress tests on lenders and insurers that penalise their exposures to dirty or vulnerable projects. But the evidence so far suggests that this will not make much difference (assuming there is no change in rules on carbon emissions). The effect on these firms’ solvency is small, because only a fraction of their assets are invested in fossil fuels or in projects whose value is sensitive to physical risks, such as flooding, after being discounted over 10-15 years. Meanwhile, despite all the fundraising, the sums being invested in renewable energy and infrastructure are only about half what would be needed to keep temperatures within 2°C of pre-industrial levels.

Another problem is measurement. Ideally, a fund manager with a portfolio, or a bank boss with a loan book, could gauge its total net carbon footprint, including the supply chains companies use and the emissions their products release—and do so without double-counting. That way you could objectively track both its carbon and financial performance and compare one portfolio with another. Unfortunately, corporate disclosure is so bad that this is impossible, at least for now. Instead, fund managers resort to using dubious ESG ratings, created by external advisers, that make subprime credit scores look like the gospel truth. Their opaque methodologies bamboozle clients and bosses. Indices and portfolios which claim to be climate-friendly often contain the securities of firms that are big polluters.

The final problem is motivation. Suppose shareholders can influence a firm and measure its emissions properly. Even then they may not have a strong financial incentive either to force it to shut down its lucrative oilfields, say, or to increase its investment in experimental energy and costly electrical grids. That is because the externalities of greenhouse-gas emissions are not accurately priced into the cost of energy. Dedicated green investors might still call for climate-friendly decisions, but they might not carry enough weight to determine how firms behave.

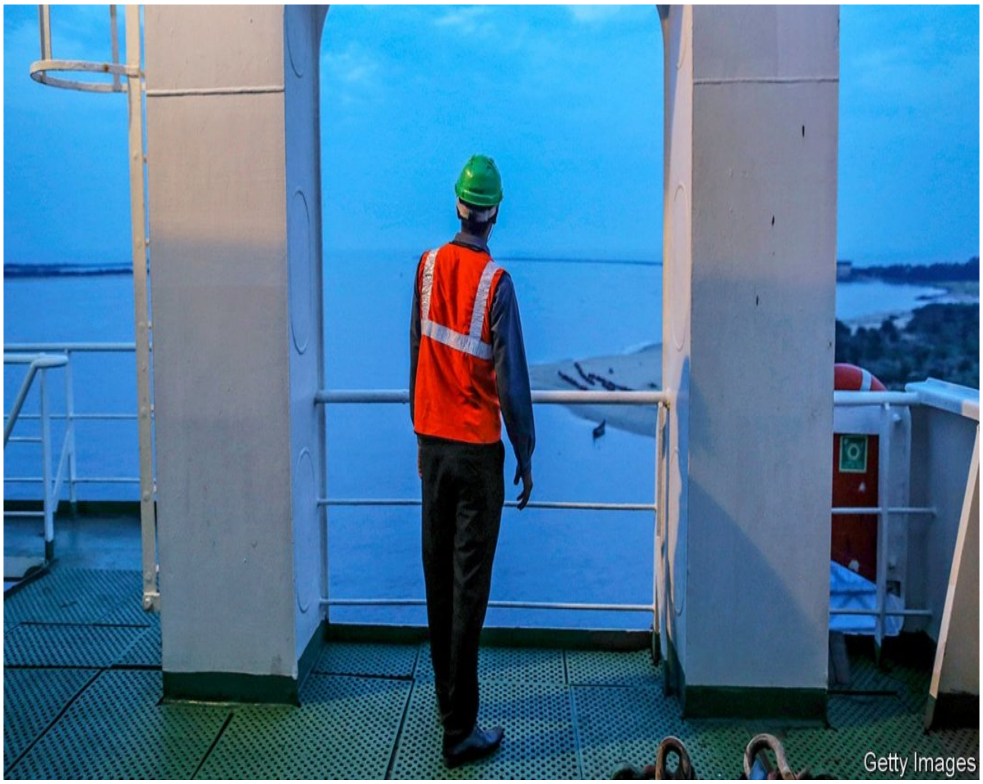
What to do? Governments need to force firms to improve their disclosure. Asset managers need to drop the gimmicks and set coherent and measurable objectives. Most important, widespread carbon taxes would unlock the power of finance, giving investors and banks a strong motive to shift capital away from dirty industries to clean ones and to develop instruments that allow firms to hedge and trade the price of carbon. Climate finance is still in its infancy. There is a lot of room for improvement.■

Sailors are stranded at sea

Cargo ship crews are stuck at sea

A crewing crisis

Jun 20th 2020 |



As you read this, over 60,000 cargo ships are on the high seas, laden with iPhones from China, dresses from Bangladesh, beef from Argentina, oil from the Gulf and much, much more. The industry likes to say that it is responsible for “90% of everything”. Indeed, its ships are the circulatory system of global commerce and their 1.2m merchant seamen its lifeblood. They enable nations to turn their comparative advantage into wealth. If they were to stop, much of humanity would soon begin to starve or freeze.

Throughout the covid-19 pandemic merchant seamen have kept working (see article). But they have been stuck on board. In a normal week around 50,000 finish their contracts and are relieved. The virus has cut that number to almost nothing. Over 250,000 mariners are stranded at sea, even though they are at least a month past the end of contracts that typically last three to nine months. Each day that total rises, and an essential job starts to look more like indentured labour.

Most merchant seamen are from developing countries, in particular India, Indonesia and the Philippines. They start and end their contracts in whatever port a shipping schedule stipulates. The ship-management firms that organise rosters and contracts for shipowners fly them out and back again. But most commercial flights have been grounded for months. Managers would have used charter planes, but many countries are refusing entry to non-citizens. Some are turning citizens away, too. Sailors are forbidden to disembark, and their reliefs are barred from entry.

The situation is unjust to sailors both on board and onshore. The first lot do not know when they will see their families again; the second do not know when they will next be able to earn a wage. It is also dangerous. Fatigue makes it hard to concentrate, and cargo ships are high-pressure, high-risk places. Forcing sailors to work endlessly is a recipe for accidents.

In the pandemic's early days, governments could perhaps have been forgiven for their neglect. There was much else to worry about. But their confinement has dragged on and sailors now have every right to feel bitter. After being locked down for months, seeing nobody but the odd pilot or port official, they are some of the world's least likely virus-spreaders. They know that they are being ignored simply because they can be. Lorry-drivers, whose goods cannot cross borders without them, were quickly classed as essential workers. Sailors, unfortunately for them, can stay on board while their cargoes are loaded and unloaded.

On June 16th an industry-wide agreement allowing emergency extensions to labour contracts expired. Unless crew-changes restart, insurance contracts could lapse—a headache for the entire industry.

But it is governments, not shipowners and managers, who must solve the problem. Last month the International Maritime Organisation, an arm of the UN, published a protocol for safe crew-changes in the pandemic. Almost no country has yet got round to implementing it. The most important step is to classify merchant seamen as essential workers, thus enabling them to cross borders and travel to and from ports during lockdowns. Ports and airports need holding facilities and accommodation for testing and quarantine for sailors. In ordinary times, all this might seem onerous. But the covid-19 world is one where hairdressers sterilise their scissors between cuts and offices allocate desks on a rota to maintain social distancing. Shipping needs to adapt to these new realities, too.

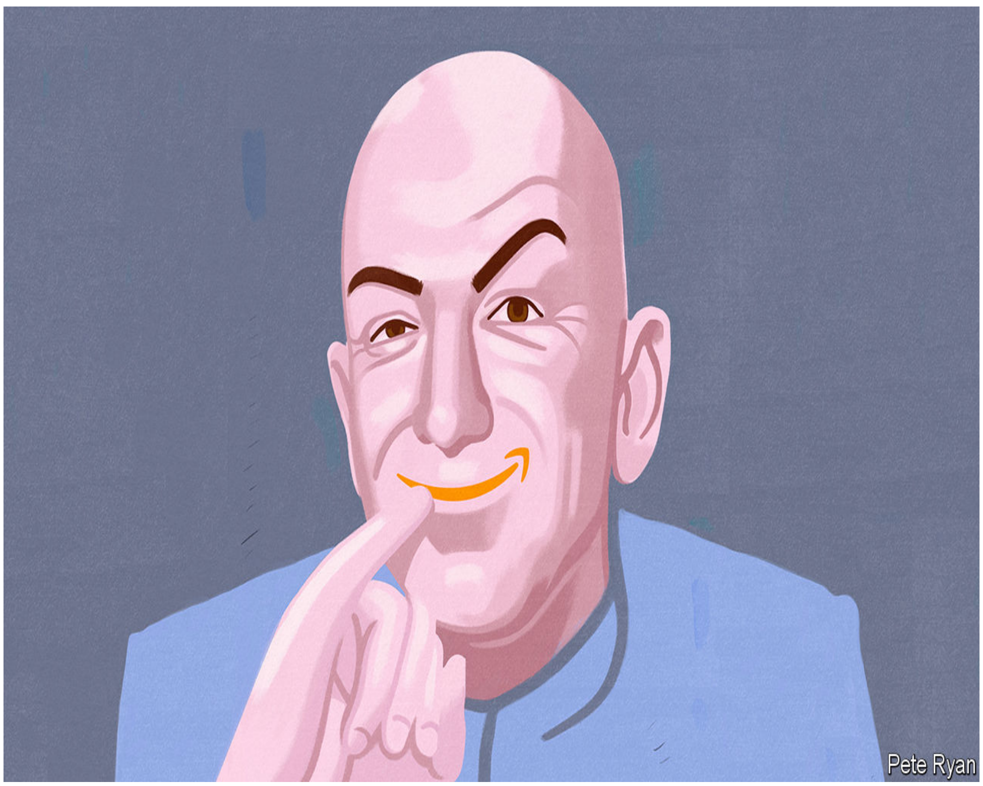
Global trade's invisible hands must not be forgotten. When their work is done, they deserve to go home. ■

The genius of Amazon

The pandemic has shown that Amazon is essential—but vulnerable

Jeff Bezos's vision of a world shopping online is coming true faster than ever. But the job of running Amazon hasn't got any easier

Jun 18th 2020 |



In the summer of 1995 Jeff Bezos was a skinny obsessive working in a basement alongside his wife, packing paperbacks into boxes. Today, 25 years on, he is perhaps the 21st century's most important tycoon: a muscle-ripped divorcé who finances space missions and newspapers for fun, and who receives adulation from Warren Buffett and abuse from Donald Trump. Amazon, his firm, is no longer just a bookseller but a digital conglomerate worth $1.3trn that consumers love, politicians love to hate, and investors and rivals have learned never to bet against. Now the pandemic has fuelled a digital surge that shows how important Amazon is to ordinary life in America and

Europe, because of its crucial role in e-commerce, logistics and cloud computing (see [article](#)). In response to the crisis, Mr Bezos has put aside his side-hustles and returned to day-to-day management. Superficially it could not be a better time, but the world's fourth-most-valuable firm faces problems: a fraying social contract, financial bloating and re-energised competition.

The digital surge began with online "pantry-loading" as consumers bulk-ordered toilet rolls and pasta. Amazon's first-quarter sales rose by 26% year on year. When stimulus cheques arrived in mid-April Americans let rip on a broader range of goods. Two rivals, eBay and Costco, say online activity accelerated in May. There has been a scramble to meet demand, with Mr Bezos doing daily inventory checks once again. Amazon has hired 175,000 staff, equipped its people with 34m gloves, and leased 12 new cargo aircraft, bringing its fleet to 82. Undergirding the e-commerce surge is an infrastructure of cloud computing and payments systems. Amazon owns a chunk of that, too, through AWS, its cloud arm, which saw first-quarter sales rise by 33%.

One question is whether the digital surge will subside. Shops are reopening, even if customers have to pay at tills shielded by Perspex. Yet the signs are that some of the boom will last, because it has involved not just the same people doing more of the same. A new cohort has taken to shopping online. In America "silver" customers in their 60s have set up digital-payment accounts. Many physical retailers have suffered fatal damage. Dozens have defaulted or are on the brink, including J Crew and Neiman Marcus. In the past year the shares of warehousing firms, which thrive on e-commerce, have outperformed those of shopping-mall landlords by 48 percentage points.

All this might appear to fit the script Mr Bezos has written over the years in his letters to shareholders, which are now pored over by investors as meticulously as those of Mr Buffett. He argues that Amazon is in a perpetual virtuous circle in which it spends money to win market share and expands into adjacent industries. From books it leapt to e-commerce, then opened its cloud and logistics arms to third-party retailers, making them vast new businesses in their own right. Customers are kept loyal by perks such as Prime, a subscription service, and Alexa, a voice-assistant. By this account, the new digital surge confirms Amazon's inexorable rise. That is the view on Wall Street, where Amazon's shares reached an all-time high on June 17th.

Yet from his ranch in west Texas, Mr Bezos has to wrestle with those tricky problems. Start with the fraying social contract. Some common criticisms of Amazon are simply misguided. Unlike, say, Google in search, it is not a monopoly. Last year Amazon had a 40% share of American e-commerce and 6% of all retail sales. There is little evidence that it kills jobs. Studies of the "Amazon effect" suggest that new warehouse and delivery jobs offset the decline in shop assistants, and the firm's minimum hourly wage of $15 in America is above the median for the retail trade.

But Amazon's strategy does imply huge creative disruption in the jobs market even as the economy reels. In addition, viral outbreaks at its warehouses have reignited fears about working conditions: 13 American state attorneys-general have voiced concern. And Amazon's role as a digital jack-of-all-trades creates conflicts of interest. Does its platform, for example, treat third-party sellers on equal terms with its own products? Congress and the EU are investigating this. And how comfortable should other firms be about giving their sensitive data to AWS given that it is part of a larger conglomerate which competes with them?

Amazon's second problem is bloating. As Mr Bezos has expanded into industry after industry, his firm has gone from being asset-light to having a balance-sheet heavier than a Soviet tractor factory. Today it has $104bn of plant, including leased assets, not far off the $119bn of its old-economy rival, Walmart. As a result, returns excluding AWS are puny and the pandemic is squeezing margins in e-commerce further. Mr Bezos says the firm can become more than the sum of its parts by harvesting data and selling ads and subscriptions. So far investors have taken this on trust. But the weak e-commerce margins make it harder for Amazon to spin off AWS. This would get regulators off its back and liberate AWS, but would deprive Amazon of the money-machine that funds everything else.

Mr Bezos's last worry is competition. He has long said that he watches customers, not competitors, but he must have noticed how his rivals have been energised by the pandemic. Digital sales at Walmart, Target and Costco probably doubled or more in April, year on year. Independent digital firms are thriving. If you create a stockmarket clone of Amazon lookalikes, including Shopify, Netflix and UPS, it has outperformed Amazon this year. In much of the world regional competitors rule, not Amazon; among them are MercadoLibre in Latin America, Jio in India and Shopee in South-East Asia. China is dominated by Alibaba, JD.com and brash new contenders like Pinduoduo.

Imitation is the sincerest form of capitalism

The world's most admired business is thus left having to solve several puzzles. If Amazon raises wages to placate politicians in a populist era, it will lose its low-cost edge. If it spins off AWS to please regulators, the rump will be financially fragile. And if it raises prices to satisfy shareholders its new competitors will win market share. Twenty-five years on, Mr Bezos's vision of a world that shops, watches and reads online is coming true faster than ever. But the job of running Amazon has become no easier, even if it no longer involves packing boxes.■

Letters

- **Letters to the editor: On prosecutors, the media, mercenaries, Greek, carbon pricing, the Bible, Andrew Johnson**

On prosecutors, the media, mercenaries, Greek, carbon pricing, the Bible, Andrew Johnson

Letters to the editor

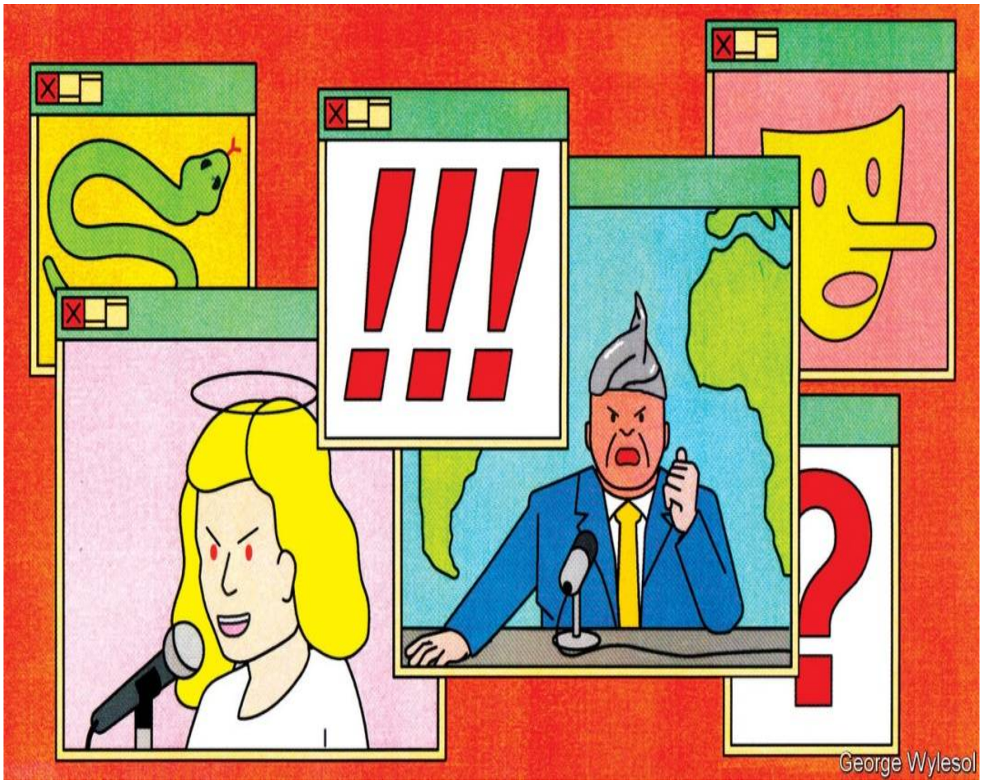
A selection of correspondence

Jun 20th 2020 |

In defence of prosecutors

As a former prosecutor, with more than a decade of experience in Miami, I take issue with your statement alleging that prosecutors are not inclined to bring charges against police because we'd rather secure convictions to advance our careers ("Order above the law", June 6th). The "elaborate culture" described in your article of turning a blind-eye to police misconduct is an academic chimera. I have never met a prosecutor who engaged in that kind of unethical calculus and am confident that it would not have been tolerated by our fellow prosecutors or our managers. That being said, I'm sure that racism exists at all levels of government. But speciously suggesting that there is an unspoken quid pro quo between police and prosecutors is false and does nothing to advance the rights of victims of police brutality.

J.P. NIXON
Westport, Connecticut



One rule for some

There is another reason for the popularity of fake news on the political right ("Return of the paranoid style", June 6th). It is the double standards found in most of the media's reporting. This conservative complaint is not entirely a myth. Take covid-19. Widespread demonstrations in early May by right-wing anti-lockdown protesters were depicted by the media as selfish and menacing acts that would result in the virus being spread. Yet the protests that erupted over George Floyd's horrific death just a few weeks later were praised by the same media. The same Democratic governors who supported lockdown and prevented businesses from reopening even participated in the marches.

One group of experts on infectious diseases, whom I presume supported the lockdowns, penned a letter with over 1,200 signatures stating that the protests were necessary to fight “white supremacy”. It is hard to imagine that these experts would support street demonstrations by conservatives in the middle of a pandemic. Commentators on the right had a field day pointing out the hypocrisy. A politicised scientific and medical community is deeply worrying because it boosts the argument on the far right that supposedly unbiased science and scholarship are a sham.

ARVIN BAHL
New York

Soldiers for hire

The trend in Africa towards using mercenaries, who work for private military companies, has been observed elsewhere (“Are mercenaries no longer taboo?”, May 30th). Left unabated, the privatisation of warfare will increase the risk of human-rights abuses and worsen humanitarian problems, especially where conflict persists and governance is weak.

This is why governments, civil-society organisations and private-security companies set up the International Code of Conduct Association for private security-service providers, based in Geneva. All those who use private contractors for legitimate security purposes, including governments, businesses, international organisations and NGOs, should exercise greater responsibility and due diligence. The UN now requires its own private-security providers to be members of the association, opening up their operations to continual monitoring and oversight by it. Nevertheless, more must be done to reel in rogue private contractors and to strengthen accountability.

JAMIE WILLIAMSON
International Code of Conduct Association
Geneva

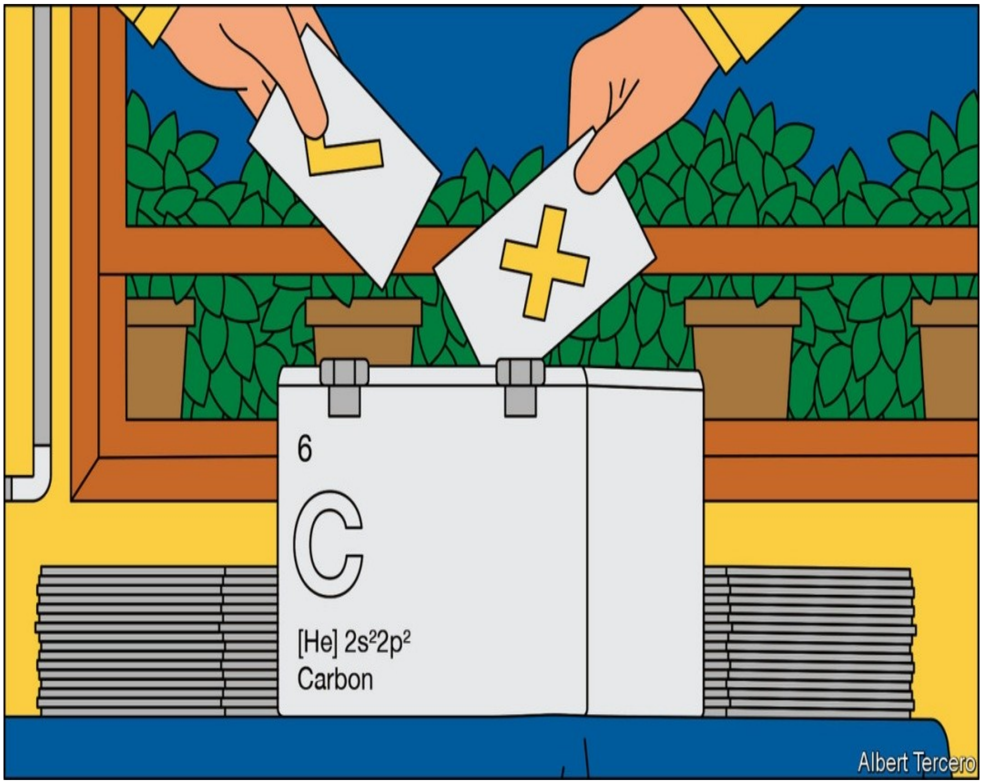
The rise of mercenaries in the 21st century is indeed a striking, if not worrying, phenomenon. However, the term “mercenary” may be misleading because it refers to soldiers who serve any state for pay, as A.E. Housman famously put it in verse. Yet most contracted soldiers are actually employed by their own government, in whose armed forces they have served, or by its local allies. In each case, they are advancing national policy. These mercenaries might be better defined as privatised state forces, rather than dogs of war. They are closer to Francis Drake than John Hawkwood.

ANTHONY KING
Chair of war studies
Warwick University
Coventry

Greek lesson

An article referred to the hooligan fish's genus name, *Thaleichthys*, as Latin for rich fish ("Alaska welcomes hooligans", June 6th). The word *thaleichthys* does not stem from Latin but comes from ancient Greek, a merger of the words *thalein* (to flourish) and *ichthys* (fish).

HARRY CORDATOS
Colchester, Connecticut



Pricing emissions

Your briefing on carbon pricing argued that "there's got to be something better" than border carbon adjustments, in effect tariffs on countries that are not members of the carbon-pricing scheme ("The contentious and correct option", May 23rd). But you did not propose any realistic alternatives. The European Union's system of freely allocating emissions-trading allowances to placate concerns over carbon leakage for energy-intensive, trade-exposed industries (EITEs) is becoming unsustainable, now that the number of allowances in the EU's carbon market must shrink to meet tighter climate goals. A global carbon market involving billions of euros in wealth transfers between Europe, America and China is Utopian.

Thus, the EU is left with two options: either introducing border adjustments or low-carbon product standards, while progressively diminishing the use of free allocation. Both are complicated, but such standards have been proven to work in other contexts, such as the Montreal protocol.

EITE products account for less than 2% of global GDP but 20% of carbon-dioxide emissions. Without a sustainable system to manage international differences in climate-policy ambition, they will not be decarbonised.

OLIVER SARTOR
Agora Energiewende
Berlin

We all stumble in many ways

It was apparently too obvious that the scriptural basis for old-fashioned Christians' fondness for old-fashioned communal worship could only come from the Old Testament to bother checking the quote "Don't forsake the gathering of the brethren" ("Your own personal Jesus", June 6th.) The reference is in fact found in the letter to the Hebrews in the New Testament. This old-fashioned priest would like respectfully to remind *The Economist* that the internet allows Bible references to be checked in a matter of seconds.

FR PHILIP-THOMAS EDWARDS
London

Drunk on power

Lexington compared Donald Trump to one of his most hapless and divisive predecessors, Andrew Johnson (June 6th). In addition to being an unreconstructed shire supremacist and notoriously thin-skinned, Johnson was one of mid-19th century Washington's heaviest drinkers, to the point of arriving at his own vice-presidential inauguration in 1865 drunk and slurring his words.

Some of Johnson's more erratic acts, such as comparing himself to Jesus Christ, could be chalked up to his extreme alcoholism. Trump, a life-long teetotaller, has no such excuse.

SCOTT PLATTON
Princeton, New Jersey

Briefing

And on the second day...

Can Amazon keep growing like a youthful startup?

Investors certainly seem to think so

Jun 18th 2020 |

NEXT MONTH Amazon will turn 9,500 days old. But for Jeff Bezos, the company's founder and chief executive, it is always "Day 1". Amazon, he has insisted since its founding in 1994, must forever behave like a feisty startup: innovate aggressively and expand relentlessly.

Adherence to this rule has made Amazon as convenient to consumers as it is feared by businesses which stand in its way. Today roughly $11,000-worth of goods change hands on Amazon's e-commerce platform every second. The company delivered 3.5bn packages last year, one for every two human beings on Earth. Amazon Web Services (AWS), its cloud-computing division, enables more than 100m people to make Zoom calls during the day and a similar number to watch Netflix at night. In all, Amazon generated $280bn in revenues last year.

This year Amazon has become not just convenient, but essential. The smiling brown package left at the threshold as the neon-vested delivery worker backs swiftly away has become the hallmark of the locked-down pandemic. Shopless and officeless life would be unimaginable without deliveries and cloud-based work—and insufferable without distractions like video-streaming. Investors see this as an acceleration of a long-term trend towards life online from which the world will not turn back. “The explosive demand created by covid-19 catapults Amazon straight into 2025,” says Michael Moritz of Sequoia Capital, a venture-capital firm.

Amazon’s market capitalisation doubled to $734bn between 2016 and 2018. Since then it has close to doubled again. Its shares trade at 118 times earnings, compared with 25-35 times for Apple and Microsoft, the other members of the trillion-dollar-company club. Up and down Wall Street, brokers tell clients to hold Amazon shares if they have them, or buy them if they don’t.

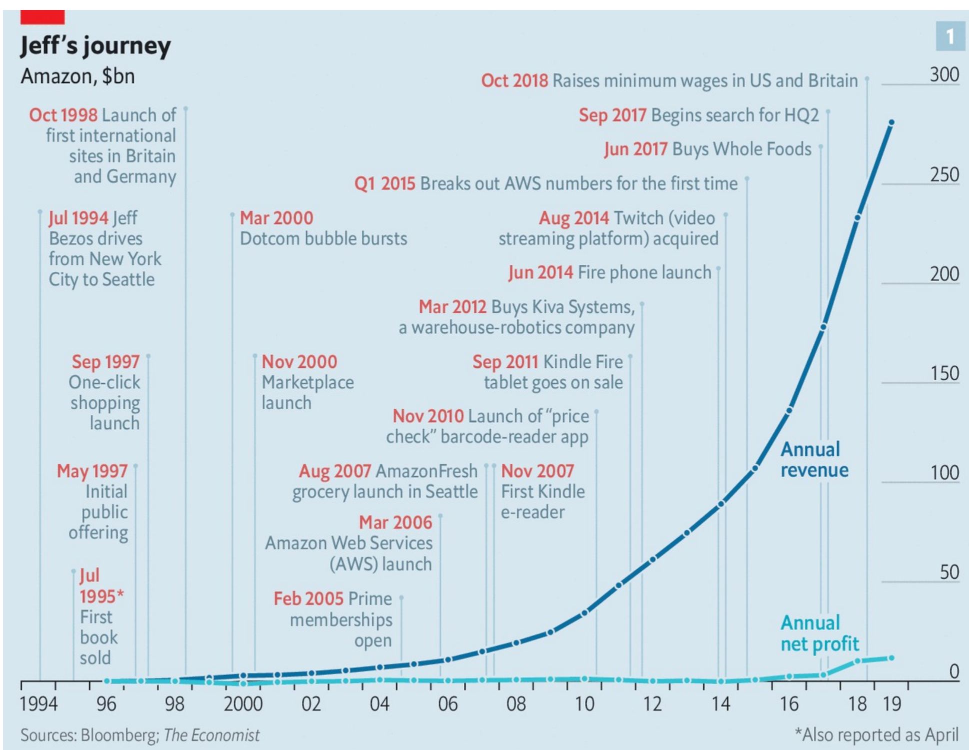
But Amazon is not without problems. Rivals have emerged in both e-commerce and the cloud. Questions are being raised about its treatment of workers and independent merchants on its platform. Politicians in many capitals would like to see it broken up. So would some investors, on the basis that they would see higher returns that way. “Day 2”, which Mr Bezos characterises as “Stasis. Followed by irrelevance. Followed by excruciating, painful decline”, has not yet dawned. But it is well past noon on Day 1.

Prime position

No firm bestrides the physical and digital worlds in the way Amazon does. In the physical world, it has a logistics system second to none. The 150m customers who subscribe to its Prime service get all their purchases delivered promptly—as well as perks like free streaming of videos and films—for a flat fee, with same-day delivery in some places. The convenience leads them to shop more. The logistics system is also used to fulfil orders for other companies. In 2018 "third-party" sales accounted for 58% of sales through the platform.

The scale of its retail operation gives Amazon an unparalleled collection of data on the desires and decision-making of hundreds of millions of shoppers—the sort of data that advertisers love. Amazon's advertising revenues are now $11bn; its 7% share of the global online-ad market is larger than any save Google's (38%) and Facebook's (22%).

In the digital world Amazon dominates the cloud-computing business. In 2003 two engineers suggested that Amazon's in-house IT infrastructure could be provided as a service to other companies, as space on its website and use of its logistics system were. That intrigued Andy Jassy, Mr Bezos's technical adviser at the time. Today Mr Jassy is AWS's chief executive. The division has established the company's credentials as a developer of serious technology on a very large scale, rather than just a user of it. It also provides lots of cash. Last year AWS contributed $35bn to Amazon's sales—and a fat $9.2bn in operating profits.



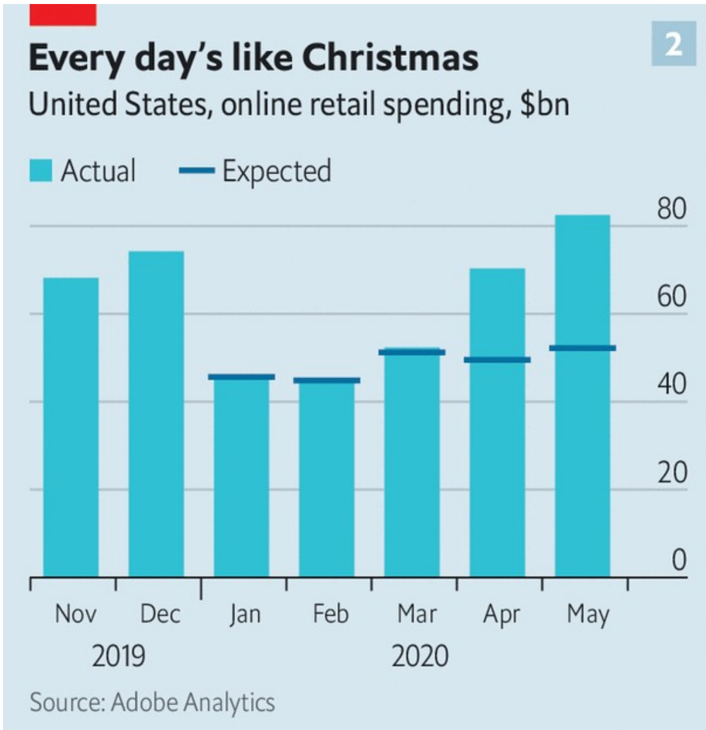
The Economist

The AWS piggy bank has supported both expansion in retail—in 2017 Amazon paid $14bn for Whole Foods, an upscale supermarket chain—and new projects which the company's engineers cook up at a prodigious rate. One of the whizziest is Project Kuiper, a satellite-broadband venture; another is Haven Healthcare, a not-for-profit aimed at reducing health-care costs, created with JPMorgan Chase, a bank, and Berkshire Hathaway, a conglomerate.

Amazon is still growing briskly, especially so for a set of multi-billion-dollar businesses. But growth is no longer accelerating in a day-one-ish way. Start with retail. Between 2016 and 2019 growth in global sales of goods, Amazon's own and third parties', on its websites slowed from an annual rate of 27% to 18%, calculates Sanford C. Bernstein, a broker. The effects of covid-19 might drive it back up to 23% for 2020 as a whole, but the long-term trend is not expected to change.

And the coronaviral sales boost has come at a cost. The company is hiring 175,000 new workers in America to cope with surging demand; it has invested heavily in covid-proofing its operations; and it has sacrificed earnings by prioritising the delivery of essential items, which tend to have lower margins, while barring many lucrative non-essentials from warehouses and removing ads for them to tamp down demand. Even as sales rose by 26% between January and March, profits fell by 29% compared with the previous year.

With its range narrowed and shipping slowed, Amazon could not keep up with soaring online demand (see chart 2). In America and elsewhere shoppers turned to rivals, often on a "click and collect" basis. According to data from Rakuten Intelligence, an independent subsidiary of a Japanese e-commerce firm, Amazon's share of online spending in America was 34% in mid-April, down from 42% before covid-19. For years Amazon has led the way as an e-commerce pioneer, says Mark Shmulik of Bernstein; now every big retailer will turn to the web as never before. Long-established retailers like Target and Walmart are already making hay.



The Economist

Big resurgent rivals are not Amazon's only competition. Shopify, a Canadian firm, offers retailers a way to sell online—and obsesses over the experience it provides to the companies which use it just as much as Amazon obsesses over its customers. It has gone from nowhere a few years ago to 5.9% of America's online-retail market, second only to Amazon. It is now to become the back-end for Facebook Shops, the social networking giant's new e-commerce venture. Taking a lead from Alibaba, China's dominant online retailer, Facebook hopes to provide a setting where people will browse and socialise in a way that no one does on Amazon.

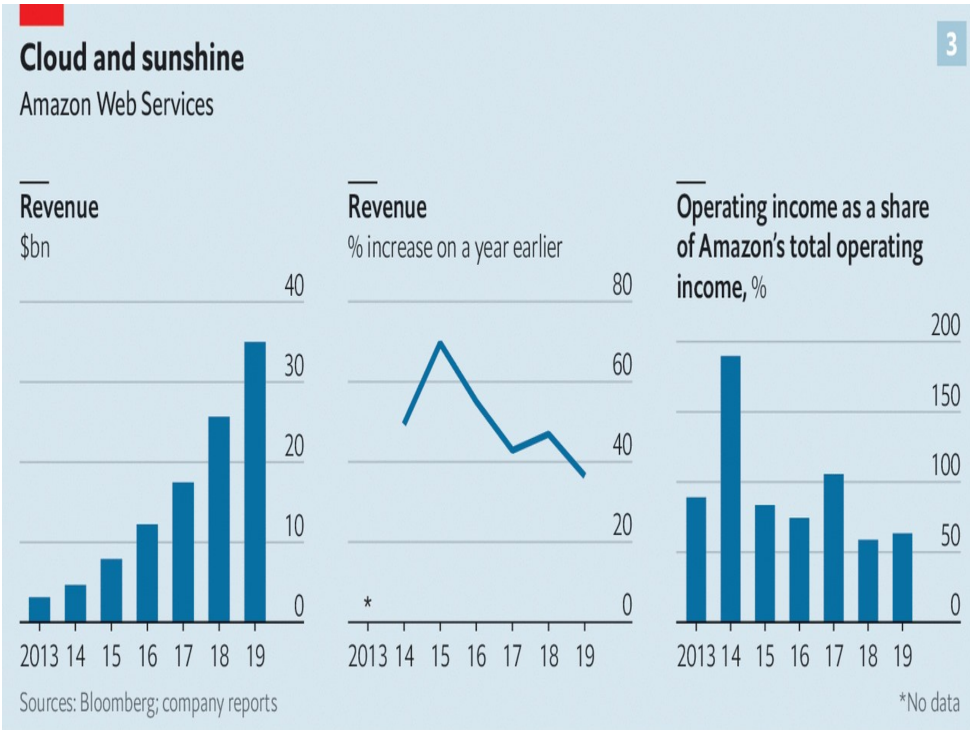
Amazon can no longer count on Prime to fuel prodigious growth at home; most American households that can afford the $120 fee are already members. Future retail growth will therefore depend on markets elsewhere. These currently account for 29% of the company's total non-AWS revenues. In western Europe, Amazon is entrenched and has been doing well. But an ageing, economically sluggish continent is not exactly a long-term growth and profits motor. Many of the region's consumers tend to browse online then buy offline. Meanwhile, things in emerging markets are not going to plan.

A year ago, after 15 years of trying, Amazon gave up on China. In 2012 it had managed to win an e-commerce market share of 7% there, but Alibaba and the other local success story, JD.com, squeezed it out, poaching customers with screaming deals and promotions. Had Amazon fought harder it might still have lost; it is possible, even likely, that the Communist Party would not long have tolerated a big American retail presence. But it does bear some blame: it failed to recruit talented locals, and made too many decisions in Seattle.

Failing to deliver

Elsewhere in the emerging world Amazon is still burning billions with no returns in sight. Its $6.5bn investment in India looks troubled. The nationalist government of Narendra Modi is making life hard for foreign firms—and easier for its local champion, Reliance Jio (in which Facebook is investing $5.7bn). In Latin America Amazon's 3% share of online retail is barely one-fifth that of MercadoLibre, an Argentine firm better at dealing with bad roads, banditry and other local pitfalls. Because profits from western Europe are not enough to offset losses in the developing world, Amazon's international division has been losing money for years.

Investors have mostly shrugged off Amazon's global retail slowdown. The reason is simple—AWS. Its operating income usually adds up to well over half of Amazon's total—in the most recent quarter it accounted for 77%. Bernstein estimates that Amazon's retail business had an operating margin of -1% in 2019, and AWS 26%. But the cloud is getting crowded. Alibaba, Google and Microsoft have expanded their cloud offerings (though Alibaba Cloud still earns almost all its revenue in China). Globally, AWS's share of cloud-computing declined from 53.7% to 47.8% between 2016 and 2018, according to Gartner, a research firm, while Microsoft's nearly doubled to 15.5%. Revenue growth at AWS has slowed sharply, from 49% in the second quarter of 2018, year on year, to 33% in the first quarter of 2020 (see chart 3).



The Economist

The AWS cloud is considered superior to the others in terms of reliability and speed. Azure experiences more service outages, for example. AWS also allows its customers to do more sophisticated things. But the rivals are good enough for most purposes, and improving. Large firms may prefer to deal with Microsoft because they have been dealing with it as a software provider for decades. George Gilbert of TechAlpha Partners, a consultancy, says that whereas AWS offers a wide range of platform services that suit the most technology-centric customers, Microsoft concentrates on integrating its servicesin order to make them accessible to mainstream customers.

AWS has the resources to defend its market-leading position. But in the cloud wars any handicap could cost it dearly. Its parent may be becoming one such drag. For years being part of Amazon was a huge advantage for AWS, says Heath Terry of Goldman Sachs, a bank. It needed cash from the rest of the group, as well as technology and data. But Mr Bezos's habit of moving into new industries means that there are now ever more rivals leery of giving their data to it. Potential customers worry that buying services from AWS is tantamount to paying a land-grabber to invade your ranch. Walmart has told its tech suppliers to steer clear of AWS. Boards of firms in industries which Amazon may eye next have directed their IT departments “to avoid the use of AWS where possible”, according to Gartner.

This has fuelled talk that AWS might be better off pursuing its future as a separate company. In addition to putting a healthy distance between itself and the Amazon expansion machine, AWS would no longer need to cross-subsidise the firm’s less lucrative ventures. The transparency that would be offered into the financials of each business by a break-up would allow fund managers a better insight into how the new firms fulfil their investing criteria. In financial markets, a separation has been expected for the past year or so, according to the head of global internet banking at a leading financial institution.

Mr Jassy says that AWS was always designed to be separable from the rest of Amazon. If things get to the point where being inside Amazon is more disadvantage than advantage, says Mr Terry, AWS could go its own way.

Not that AWS gets nothing from being part of Amazon, however. Some data-driven technologies work better at scale. Data from Alexa, the virtual assistant Amazon makes available through its Echo smart speakers, helps feed Amazon’s voice-recognition algorithms, which can then be sold as a service to AWS customers, as well as back to shoppers. More shoppers and more data mean better algorithms, and so on. Yet such benefits could easily be set aside if AWS’s position inside Amazon continues to give powerful rivals such as Microsoft and Google a winning sales pitch.

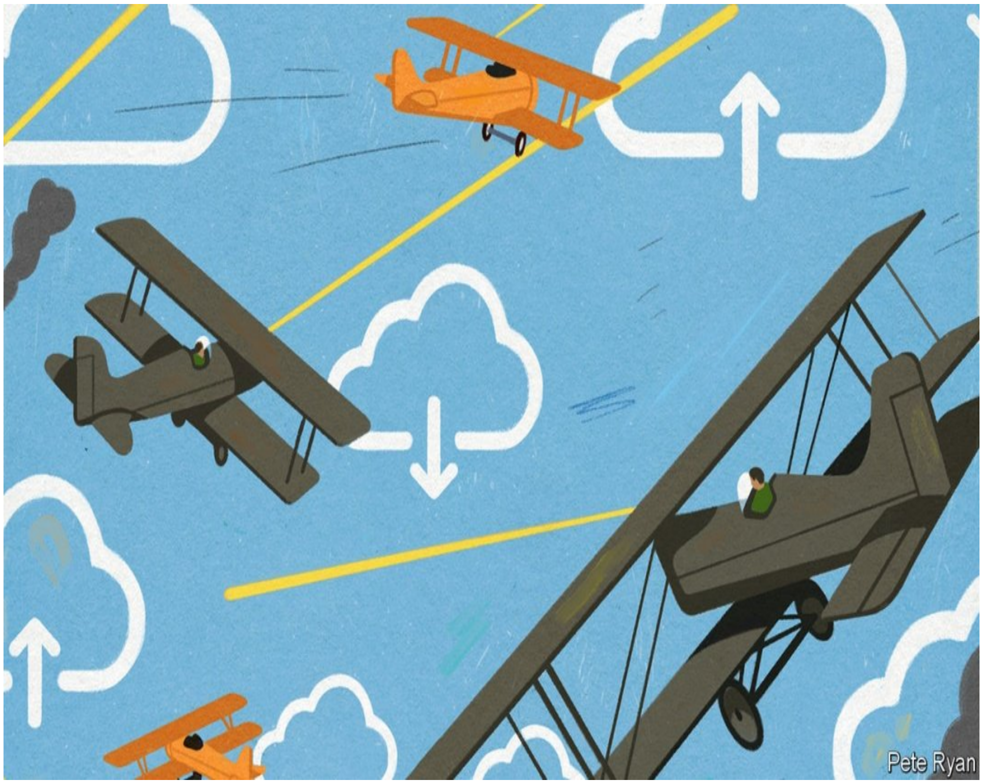
Letting go of AWS would mark by far the most dramatic reorganisation in Amazon’s unremittingly accretive history. Analysts reckon the unit accounts for a third or more of Amazon’s value. A plausible valuation of $500bn would see it start out as one of America’s ten most valuable firms. And despite slowing growth it is still expanding twice as fast as the retail bit. If it grew at 20-30% a year for a decade—which is more slowly than in the past—while maintaining its margins, it could turn into the world’s biggest profit-generator.

The great migration

There is no historical precedent for a half-a-trillion-dollar firm growing that fast for that long. But the notion is not entirely outlandish. Less than 10% of the estimated $4trn in annual global IT spending has so far migrated to the cloud. Mr Jassy is not alone in arguing that "the overwhelming majority" of computing is going to end up there one day. A company focused entirely on making that happen could become vast.

How would Amazon fare without AWS? In some ways, the change might be salutary: some close to Amazon feel that it has grown too big. Elements of unproductive bureaucracy and politicking are creeping in, they report. A lot of high-level Amazon meetings these days are about lobbying for promotion rather than innovation or operational excellence, says a former executive. A slimmed-down and refocused company might be on a better footing.

It would, though, also be one with much less cash to back its further growth. As well as helping pay for the purchase of Whole Foods, AWS money has paid for international expansion and heavy investment in "last-mile" delivery, among other things. If the e-commerce rump were to inherit a hefty chunk of the company's $59bn cash pile it might be able to keep spending—but not for long, at its recent rates. An Amazon without AWS "might not be one I would want to own", says a representative of a big institutional shareholder in Amazon.



Mr Bezos's views on a break-up are unknown (he declined to be interviewed for this article). He may believe that AWS and the rest of the group are symbiotic and would both suffer if separated. Even if he does not, though, it is a fair bet that he would be reluctant to let go of a cash-cow that enables Amazon to pursue new ventures. In time, the ad business might grow to fill that role. Last year it boasted an operating margin of 49%, and it is standing up to the current collapse of the advertising market better than its larger online rivals. But it is still small compared with AWS.

Whatever Mr Bezos's views are, though, they will not be the final word that once they would have been. For a few years Seattle tech insiders have reckoned that Mr Bezos has been preparing to give up the top job to become executive chairman. He has already shed some of the management burden. In 2016, when Mr Jassy became chief executive of AWS, he named Jeff Wilke as "chief executive worldwide consumer".

Though the pandemic has now brought Mr Bezos back into day-to-day involvement in the e-commerce operation, in recent years he has mostly confined himself to new projects such as Amazon Go, a till-less supermarket, and, earlier, Alexa. He has also been devoting a fifth of his working week to Blue Origin, his private rocket company, which is currently working on satellite launchers to compete with those of SpaceX and a Moon lander for NASA.

There is also the matter of his private life. In January last year Mr Bezos tweeted a bombshell: he and his wife, MacKenzie, were getting divorced. Days later the *National Enquirer* published details of an extramarital affair. The news shook the tight group of executives who run the company alongside him. Amazon's meritocratic culture depends on "truth-seeking", says a former senior executive. But it only works "if people at the top behave accordingly", he adds. "Jeff's episode put a dent in the company's values." Investors, for their part, fretted that Mr Bezos's eventful personal life had become a distraction.

If Amazon fissions, Mr Jassy and Mr Wilke will be the obvious candidates to run the two firms—if, that is, one or other of them does not leave before then (they are both high on every recruiter's wish list). Mr Bezos might stay on to oversee both companies as executive chairman. Amazon's board will want to hang on to his magic touch for as long as possible, says a headhunter who knows the firm well.

But over time his influence may dwindle. He remains the company's biggest shareholder—and thus the richest man in the world. His divorce settlement cut his economic stake from 16% to 12% (though he kept the voting rights of the portion he gave up). Still, every year he sells a slug of stock to fund Blue Origin, so in some years' time he may come to own less than a tenth of his creation. Excluding the big three passive fund managers, the four largest institutional investors in Amazon already control 10% of the stock. And unlike many technology firms, Amazon has no dual-class shares that would let Mr Bezos control the board regardless of the size of his stake.

There might be other attractions to new leadership. While on Wall Street and in Seattle investors and insiders talk of one way of splitting up the company, in Washington, DC, they talk of another. A growing chorus of politicians, accompanied by an ensemble of antitrust experts, accuse Amazon of abusing the market power its size and reach provide.

Elizabeth Warren, a Democratic senator and scourge of big tech, has proposed sundering Amazon's private-label business—which produces goods for sale on the site—from that of third-party sellers on its platform. The company would also have to sell Whole Foods and Zappos, an e-commerce rival it bought over a decade ago. Two Republican senators, Ted Cruz and Josh Hawley, also speak of breaking up big tech, for different reasons. Donald Trump reserves especial spite for Mr Bezos on the basis that he owns the *Washington Post*, a newspaper critical of the president.

Soul-searching in Seattle

Anti-Amazon feeling grew stronger in April, after the *Wall Street Journal* reported that Amazon employees used data on third-party sellers to pinch ideas for the private-label business. Amazon has launched an internal inquiry into the incident, which violated the company's own guidelines. But lawmakers who had been investigating Amazon, Alphabet (Google's parent), Facebook and Apple for antitrust violations, still threatened to subpoena Mr Bezos if he did not voluntarily appear at an upcoming hearing. (In June Amazon signalled it was ready to send Mr Bezos.) The European Commission is reportedly preparing to file formal antitrust charges against Amazon over its treatment of third-party sellers in the coming weeks.

In America Amazon's market share is nearly two-fifths in e-commerce, but only 6% in all of retail. The firm's low prices and high-quality service certainly do consumers no harm. But even Amazon insiders say accusations of stealing small firms' ideas are becoming harder to brush off.

So are criticisms with respect to Amazon's treatment of its workers, a large proportion of whom are African-American or Hispanic. During the pandemic a number of warehouse employees have been publicising safety shortcomings to activists and the media. According to a tally by an Amazon worker, there have been 1,079 coronavirus cases among American warehouse workers. Amazon has said that the firm's rates of infection and quarantine are never higher than those of the communities in which its facilities are located, and sometimes lower. In May a group of 13 state attorneys-general asked Amazon to hand over data on covid-related infections and deaths at its warehouses.

In May a furore erupted after Amazon fired two tech employees who worked on user-experience design, after they organised a live-stream for warehouse workers to explain their pandemic safety fears. Democratic senators have demanded more information from Amazon on the dismissals. So have a handful of shareholders.

The incident prompted the resignation of Tim Bray, a respected senior vice-president at AWS (and co-inventor of XML, an internet data-description language). The sackings, and those of other activists at the firm, Mr Bray wrote, were evidence of a "vein of toxicity" running through Amazon's culture. A leading engineer inside Amazon's Grand Challenge team, a secretive skunk-works unit working on ambitious projects, says morale is rock-bottom. He plans to leave.

The risk of Amazon's labour practices inviting more regulatory scrutiny—and, possibly worse, alienating brainboxes—is not lost on investors. The firm needs to be "very, very careful", says the institutional shareholder's representative. Amazon raised workers' wages by $2 an hour from mid-March until June 1st and allowed warehouse employees worried about infection to go on unpaid leave without the risk of being sacked. It made 150 changes to the way its warehouses function to ensure social distancing and more cleaning.

Still, says the shareholder rep, rather than leading by example on labour Amazon "seems to be playing catch-up". Mr Bezos, who has added $54bn to his net worth thanks to his company's buoyant share price while low-paid warehouse workers toil through the pandemic, "needs to lean over backwards to make sure workers are properly treated", cautions a leading Silicon Valley venture capitalist.

The antitrust cudgel may in fact be an attempt to force Amazon to spruce up its labour track record. How far regulators are willing to go will depend on the public mood. Americans' reliance on the company and the goodwill it has generated with consumers may help it, says an antitrust expert close to Congress. An AWS spin-off, if it occurred, might obviate the need for drastic antitrust action.

Mr Bezos has managed to keep Amazon from ageing beyond Day 1 for longer than most companies can dream of. But not even the best magician can stop the passage of time. One day, Day 2 will come. ■

Hotting up

How much can financiers do about climate change?

The role that green investing can play must not be misunderstood or overstated

Jun 20th 2020 |

IN THE MAYFAIR office of Chris Hohn, the boss of TCI, a hedge fund, an enormous photograph of a melting iceberg hangs on one wall. Robert Gibbins, the founder of Autonomy Capital, another London hedge fund, says his desk is adorned with the deformed remains of a car bumper, melted by an Australian wildfire. An interest in modish office decor is a long-standing feature of high finance. An interest in climate change, though, was until recently rare; the preserve of boutique investment houses and pokey back offices in the large asset managers. Now it is all the rage.

One reason for this is the realisation that extreme weather events pose threats to businesses seeking investment. Last year PG&E, a Californian utility, was forced into bankruptcy for its role in sparking wildfires. Another reason is that governments are taking steps to limit the emission of greenhouse gases that could have real impacts on firms' future revenues. A third is pressure from clients. Large asset owners, including Japan's Government Pension Investment Fund, the world's biggest, are badgering the companies which manage their money to attend more to the environmental, social and governance (ESG) bona fides of the companies they put money into. A fourth factor is that asset managers are facing shrinking margins. By offering their clients various sorts of greenery they can also charge higher fees.

Hungry planet

The greening trend could be a force for good in the fight to reduce climate change. But the role that financial services can play must not be misunderstood or overstated. The sector is responding to changes in government and broader circles of opinion, not driving change itself. And there is a limit as to how much it can do. Calculations by *The Economist* suggest that the amount of direct control over carbon emissions exerted by companies in which investors hold sway is lower than is often thought. Less than a quarter of industrial emissions come from companies that can be influenced by investors in stockmarkets. And when one gets away from the key sectors of energy and natural resources, the amount that can be done by green investment may not be very much at all.

In 2019 the greenhouse emissions from human activity—mostly carbon dioxide, but with contributions from methane, nitrous oxide and other gases too—had the warming effect you would get from 55bn tonnes of carbon dioxide. The carbon dioxide from fossil-fuel emissions and industrial processes accounted for 37bn tonnes.

In order to see how much of this might be amenable to investor-led action *The Economist* analysed emissions disclosures from over 5,000 publicly listed companies which between them account for about 90% of the value of the world's stockmarkets. The number of companies making such disclosures has been rising steadily in America (from 53% of the companies in the S&P 500 five years ago to 67% today); over the same time it has shot up in

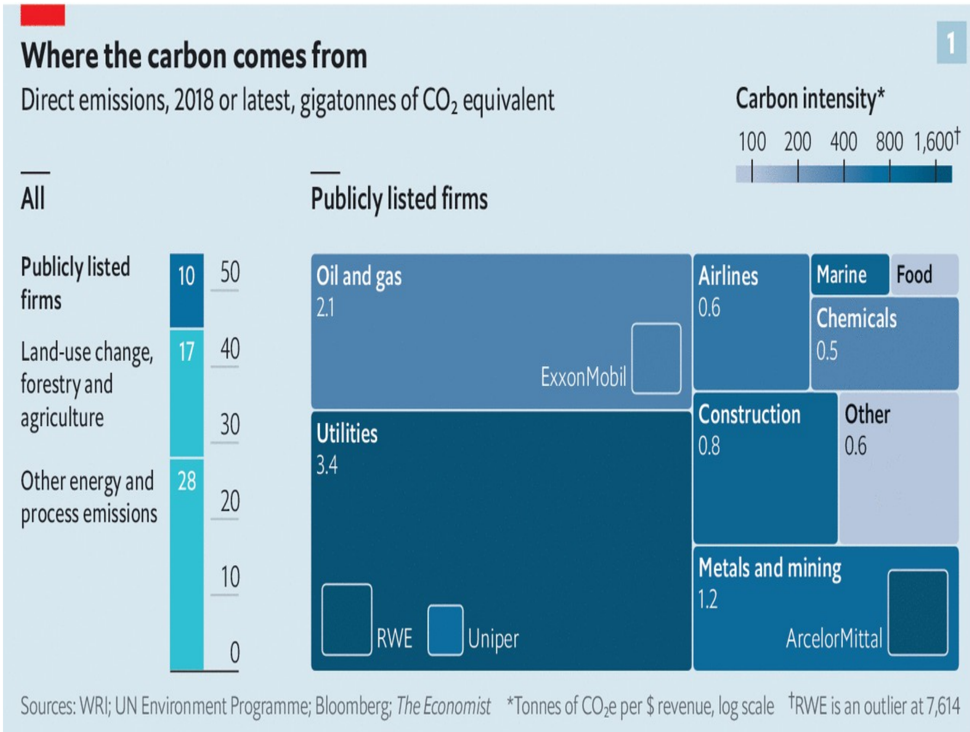
Europe and Japan, from 40% to 79% of companies in the Euro Stoxx 600 and from 13% to 46% on the Nikkei 225.

Those disclosures differentiate between the emissions that companies make directly (which the Greenhouse Gas Protocol, widely used for such reporting, calls “scope-one” emissions) and “scope-two” emissions which are produced by the companies which provide them with energy, mostly in the form of electricity. The scope-two number is vital to assessing the emissions caused by a company’s activities, but in order to look at the total emissions we considered only scope one, since adding in scope two leads to double-counting.

As you would expect, the largest emissions come from companies which burn fossil fuels in the normal course of their business: those that run fossil-fuel power stations, or fleets of aircraft or steelworks. In Europe ArcelorMittal is the biggest emitter because steelmaking requires the burning of coal. In America the biggest operational emitter is ExxonMobil, which unlike many large companies produces much of the electricity and heat that it uses itself.

Using the emissions disclosed by these companies, we estimated emissions for non-disclosing firms on the basis of those disclosed by similar firms in the same sector with comparable revenues. Given that a firm’s decision whether to disclose and its emissions intensity may not be independent, this step could introduce error.

Totting everything up reveals that each year publicly traded companies emit greenhouse gases equivalent to 10bn tonnes of carbon dioxide from their operations (see chart 1). Perhaps a quarter of those are produced by listed firms that are majority owned by governments. That leaves eight gigatonnes of emissions that stock markets can influence directly. That is 14% of the world’s total emissions, or 19% of the emissions related to energy use and industrial processes. (Those estimates undercount oil emissions. If you add the emissions from the oil sold by institutionally controlled energy firms, part of what is called “scope three” emissions, then it increases to 23% and 32%, respectively.)



The Economist

Where are the rest of the emissions coming from? In large part from consumers of those companies' wares. An oil company's scope-one emissions include all the carbon dioxide and methane it gives off in its operations, but not the carbon dioxide given off when its wares are burned in engines and boilers. Attempts to take this into account are found in the scope-three disclosures, which cover the entire value chain of a business from the extraction of its raw materials through its suppliers and on to its end users.

Only two-fifths of the firms in the S&P 500 and half of those in the Euro Stoxx 600 disclose a figure for their scope-three emissions. The figures are, unavoidably, larger than for scope one. They are biggest for the extractive industries. Of the companies in our dataset that disclosed their scope-three emissions, Royal Dutch Shell topped the list, followed by BHP, a mining firm.

Large scope-three emissions point to business models that depend on either suppliers or customers emitting greenhouse gases in bulk. This makes them hard to change. A company can reduce its scope-one emissions by changing its internal processes, and its scope-two emissions by changing its electricity supplier—for example, choosing one that uses a lot of renewable energy sources or nuclear power plants. To change its scope-three emissions, though, it needs to change either the practices of its suppliers or, harder still, what it sells.

The first may be feasible through investment. The Swedish furniture retailer IKEA has a €200m ($224m) fund to help its suppliers transition to using renewable energy, among other things. Changing what happens downstream, though, may be harder. As long as BHP goes on selling iron ore to steelmakers who use coal to smelt it, BHP will have high scope-three emissions; as long as Royal Dutch Shell sells oil and gas it will, too.

Scope-three emissions are highly concentrated within a small number of firms. When *The Economist* looked at scope-three emissions with the same methodology we used for scope-one emissions, 220 of our 5,000-odd companies, with a value of about $14trn, accounted for 84% of the total carbon footprint. This fits with a separate analysis by the Carbon Disclosure Project (CDP), a group which tracks firms' climate disclosures. In 2015 the CDP looked at 224 fossil fuel firms and totted up scope-one emissions and a subset of scope-three emissions: emissions that come from the use of a firm's products. The CDP found that between them the companies and their wares produced the equivalent of 31bn tonnes of carbon dioxide.

Divided right in two

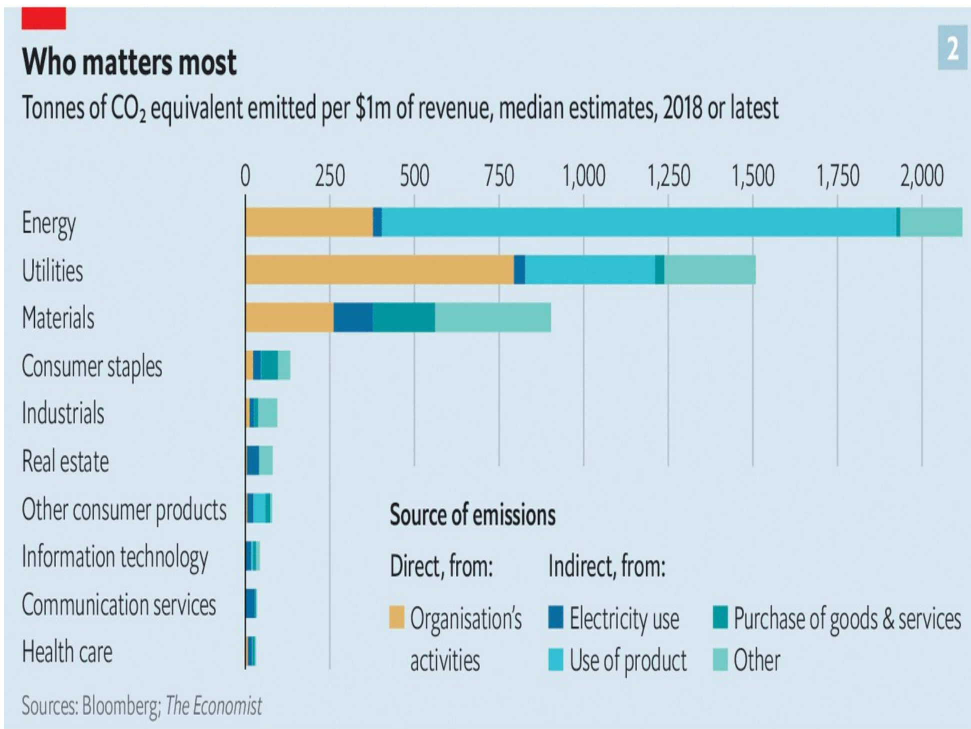
In our analysis 76% of the heavy emitters are majority investor-owned. And this ownership is also highly concentrated. When the stakes that they hold in a company are weighted according to that company's emissions, the biggest 250 financial firms control about 86% of the emissions from the investor-controlled companies with the highest scope-three emissions. The financial firms with the largest holdings by this measure are the biggest asset managers, such as BlackRock (10% of the emissions from the investor-owned, heavy-emitters subgroup), Vanguard (6%) and State Street Capital (3%).

Some of these investors, including BlackRock, are part of Climate Action 100+, a group of institutional investors with over $40trn in assets. They ask firms to set emissions-reduction targets, disclose carbon-footprint data and generally clean up their act. Of the 161 firms targeted by CA100+, 70% have set scope-one emissions targets. But only 9% have set goals that a research group called Transition Pathway Initiative sees as compatible with the target of keeping global warming since the Industrial Revolution below 2°C. A similarly small proportion has made the promise no longer to lobby against green regulation that CA100+ asks for.

Rather than trying to change the actions of the companies at the heart of the climate crisis, most green investment seeks to reward and encourage companies in all sectors which either emit less than they might or help others so to do. JPMorgan, a bank, estimates that at least $3trn of institutional assets are now managed in a way that tracks ESG factors. Though that is a lot, it is only 4% of total assets under management.

Hortense Bioy of Morningstar, a research firm, says that in Europe there are about 400 green funds managing €132bn in assets. Some simply exclude fossil-fuel companies. Others seek out "climate-solution firms" developing technologies that reduce energy demand. One popular green-fund category is "low-carbon". Low-carbon fund managers offer the chance to invest in the companies with the highest revenues per tonne of carbon dioxide emitted, either in a given sector or on a given index. They face the problem, though, that current carbon accounting does not make such comparisons easier. Apple has only a tiny fraction of Samsung's operational emissions; but Samsung makes things, while Apple has others do that for it.

Nevertheless, carbon intensity may be a useful measure (see chart 2). *The Economist* looked at data from firms that disclose their operational emissions in the S&P 500 and Euro Stoxx 600. Calculating carbon intensity on a variety of measures shows that greener firms trade at a premium. Whether that means better returns in the long run, though, remains inconclusive.



The Economist

Perhaps the most obvious avenue for green investing is in firms whose technologies replace those that emit greenhouse gases on a grand scale. Renewable energy is one obvious possibility, but one which does not at the moment offer a wide range of choices to investors. Only three firms in the S&P 500 produce renewable energy, making up less than 1% of the index's market capitalisation. Even among private-equity and venture-capital firms only $11bn were invested in renewables in 2019, according to BloombergNEF, a consultancy.

A study by Mariana Mazzucato of University College London and Gregor Semieniuk of University of Massachusetts Amherst looked at renewable-energy investments from 2004 to 2014. Institutional investors provided 7% of the funding and commercial banks provided 12%.

Another way to reduce emissions by rejigging finance is to make it harder for companies to get money if either climate change or action to avert it poses a particular problem to them. This is the idea behind the "stress tests" that central banks in England, France, the Netherlands and Singapore are forcing on banks and insurers: by modelling a 4°C world, or a $100/tonne carbon price, they seek to discover how badly the banks' lending to their current portfolio of clients endangers them.

So far, these tests are not producing results as worrying as some might have expected. The central bank of the Netherlands found only 3% of banks' loan books were at risk. This may be because much of the data needed for rigorous testing do not exist. Daniel Klier of HSBC, a bank, says only 12% of the companies in the bank's loan portfolio reveal climate data. Insurance firms tend to have a better grasp on which assets are at what physical risks. But neither industry has the complete picture. For now stress tests are a work in progress.

It is also possible that the risks are not, in fact, that catastrophic. There are clearly businesses which will not survive serious action on climate change. For the world to limit warming to 2°C nine-tenths of today's coal reserves will have to stay in the ground, according to JPMorgan. But this hardly means that, in Mr Hohn's words, "Coal is the new subprime." Western banks tend to have little exposure to the energy sector. The biggest ten have between 8-14% of the total credit exposure of all listed energy firms. Their share of exposure to coal will be even smaller.

Chinese banks probably have a much bigger share, though disclosure is patchy at best. One analysis by UBS, a bank, found that between January 2014 and September 2017, 60% of the financing for the world's biggest 120 coal-plant developers came from Chinese banks. The next-biggest lenders were Japanese banks (8%) and Indian ones (7%).

The fact that banks will stay standing if coal companies topple does not mean that efforts to reduce emissions will have no effect on the financial sector. At present only 20% of world emissions are covered by a carbon price. If prices were to increase in both their level and the share of emissions that they cover, banks and investors would need to take notice. Particularly as the pain will be spread unevenly across sectors (see chart 3).

Shake and quake

The IMF thinks that a $75 per tonne price on all emissions might keep warming below 2°C. If you applied such a price to companies' scope-one emissions, pre-tax profit in the S&P500 would fall by 8%, and in the Euro Stoxx 600 firms by 12%. That overstates the damage; the whole idea of carbon prices is that they make sensible reductions in emissions that were not cost effective before. But it gives a sense of the extent of change that companies and those who invest in them would face.

Axel Weber, chairman of UBS, sees that change in truly cosmic terms: "We need to build a new universe, not add some galaxies to the existing one." He envisions a whole new financial system centred on a carbon price and tradable emission permits. Secondary markets in carbon futures and derivatives would allow investors to plan and invest for the long term.

Such calculations hint at a powerful future for finance, not as a driver of climate action, but as its enabler, making it more flexible and better able to tap insights and capital from investors around the world. If that also helps the financial firms doing the legwork, that will be all to the good. And if it shows up some of today's green financing attempts as window dressing and marketing wheezes, that will be good, too. ■

Asia

United States

China

The Americas

Middle East & Africa

Europe

- **France: The call of the wild**

Townies v tractors

French urbanites fuss about rustic noises and smells

Some second-home owners have sued over loud livestock and church bells

Jun 20th 2020 | VAISON-LA-ROMAINE

France's sense of itself has long been rooted in the land, even though three-quarters of French people live in towns. Now, however, having locked down in small airless spaces, many city-dwellers feel the call of the wild. Estate agents report an uptick in searches for homes with gardens. Diehard urbanites talk wistfully of a bucolic existence in *la France profonde*. In a poll, 61% of the French think confinement will encourage people to move to the country or buy a second home. But do today's townsfolk know what rural life really entails?

The question arose late last year, when Pierre Morel-À-L'Huissier, a deputy from the Lozère, a remote rural area, introduced a bill to protect France's "sensory heritage". By this, he meant "the crowing of the cockerel, the noise of cicadas, the odour of manure", and other rural sounds and smells. Some of his fellow citizens, it turned out, had judged these intrusions into their romanticised idyll a form of intolerable pollution.

Last year second-home owners on the Ile d'Oléron, off the west coast, brought a case against a cockerel for crowing too early. The court ruled against them, rescuing Maurice, the unfortunate bird, from banishment or worse. In Soustons, in the south-west, a case was brought against the owner of 50 ducks and geese which made a din. Near the Pyrenees, a new resident in Foix filed a complaint against the village because the church bells were too noisy.

Rural people are pushing back against this nonsense. The mayor of Saint-André-de-Valborgne, in southern France, has put up a sign outside his village warning visitors that they are entering a risk zone. Church bells ring often. Tractors make a racket. All because "farmers are working to give you what you eat." These noises are "not a nuisance but intrinsic and authentic characteristics" of rural life, said Mr Morel-À-L'Huissier. And on its first reading, the National Assembly unanimously backed his bill.

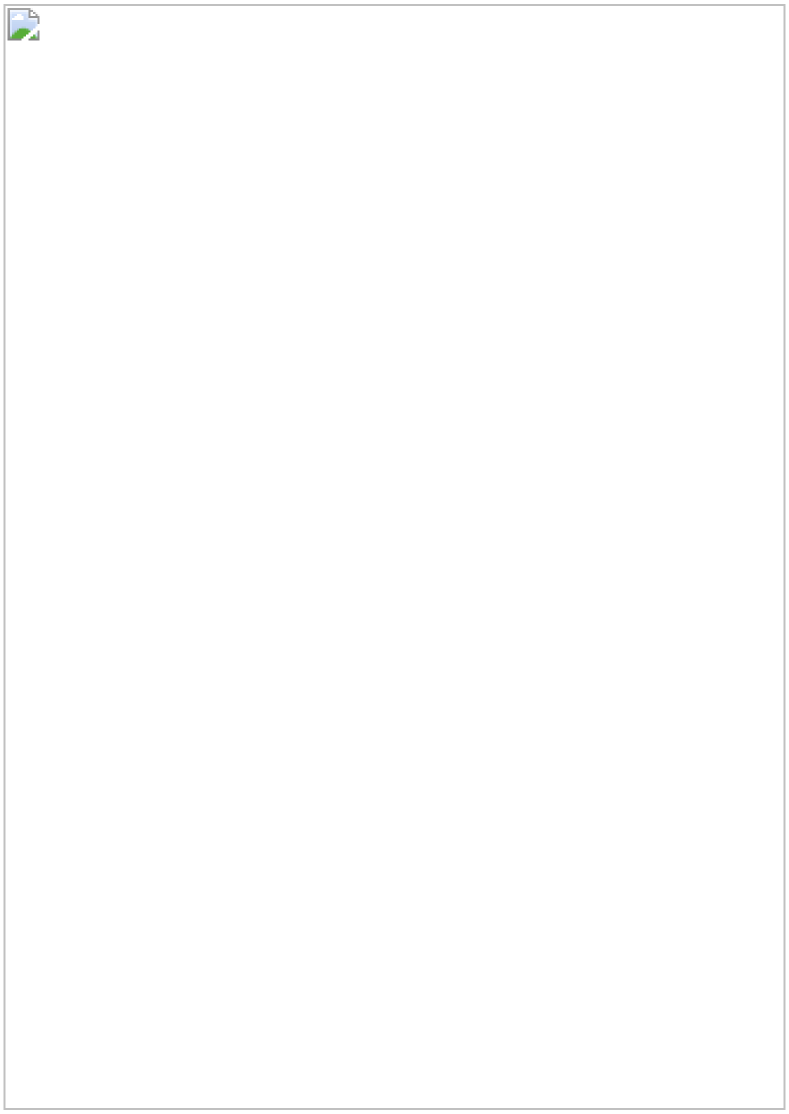
Britain

An unfortunate case study

The British state shows how not to respond to a pandemic

It faced difficult circumstances. And has so far failed to rise to them

Jun 18th 2020 |

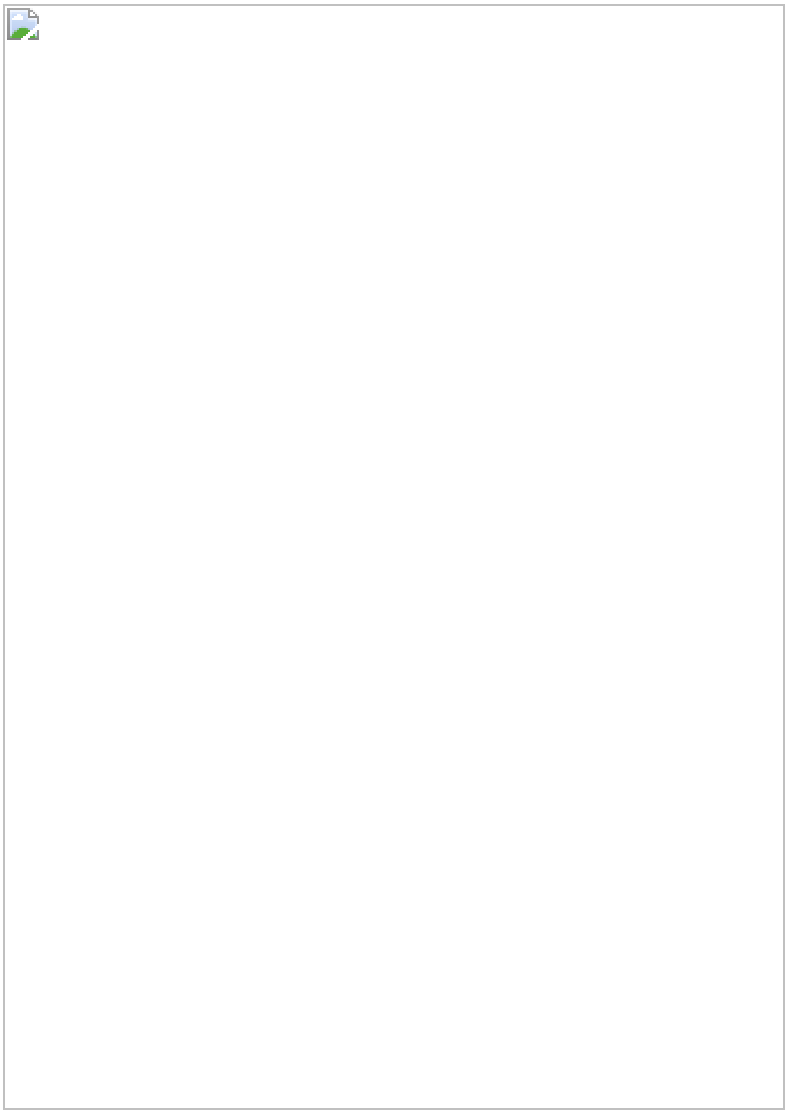


Covid-19 was sweeping Europe. Images of overwhelmed hospitals in Lombardy played on television every night. Governments were beginning to put in place restrictions that would last for months. And Mike Padgham, the owner of four care homes in Scarborough and Pickering, in the north-east of England, faced a dilemma. Should he shut his homes to visitors?

If they had been in Alsace or Umbria, the government would have told him to. In Britain, it did not. Despite the lack of national guidance, Mr Padgham nevertheless went for it, closing the homes to all but essential visitors; something which annoyed relatives. “People thought we were jumping the gun,” he recalls. Two days later on March 13th, Public Health England, a government agency, advised those who were unwell to stay away from homes, but also noted the “positive impact” of visits. It took another fortnight for the government to tell care homes to turn visitors away.

Mr Padgham’s foresight was not enough to keep out the virus. There were five deaths in his homes—a small part of a bigger tragedy. Altogether, one in 14 residents in British care homes at the start of the pandemic is thought to have died from the virus. A comparison in May by the International Long-Term Care Policy Network found that a higher proportion of people in care homes in Britain had died than in France, Germany, Canada or Sweden.

Some aspects of the British response to the pandemic have been admirable. Its researchers are leading the search for drugs; an Oxford University trial has found the most promising one yet (see article). The National Health Service has weathered the storm. Sweeping organisational changes—including postponing elective surgeries, discharging inpatients and buying private beds—saved it from being overwhelmed. But measured by the number of deaths over and above those that would normally be expected, Britain nevertheless appears to have the highest death rate in the developed world (see chart 1).



Lots of factors beyond the government's control contributed to this. Care homes are a popular way to look after old folk. Britons are fatter than their fellow Europeans. The large ethnic-minority population is disproportionately likely to suffer from diabetes and heart disease, which increase the risk of severe covid-19. Genomic analysis suggests Britain imported lots of cases from Spain, before it was clear how prevalent the virus was there. One in seven Britons live in London, an international travel hub which prior to the pandemic received nearly 1,500 flights a day.

Yet the government's poor response has contributed. On March 12th, having joked two weeks earlier about shaking hands in a hospital with covid patients, Boris Johnson, the prime minister, turned serious: "families are going to lose loved ones before their time." But the restrictions he announced were light: those with symptoms were told to stay at home for a week; those older than 70 instructed to avoid cruises. Meanwhile, continental Europe was already beginning to lock down.

Given the government's well-publicised suspicion of "experts'" views about Brexit, some worried it would ignore the scientists' advice on dealing with the pandemic. These fears were unfounded. The government's advisory committee (the Scientific Advisory Group on Emergencies, or SAGE) helped shape policy—which was, in early March, to protect the vulnerable, while tailoring restrictions on others to ensure the health service was not overwhelmed. The virus would spread among the general population, which would build immunity to the disease.

At that stage, there was great uncertainty about numbers. Even so, some of SAGE's advice seems questionable. On March 3rd the committee minuted that: "There is currently no evidence that cancelling large events would be effective," on the grounds that those who might have attended would go to the pub instead. But not all would, and if they did, there would have been less risk of the infection spreading across the country, which it did. So large events went ahead, including a football match on March 11th between Liverpool and Atletico Madrid, attended by 3,000 Spanish fans.

Perhaps the government should have questioned the experts more closely. But it "was getting advice it wanted to hear", notes Sir Lawrence Freedman of King's College London, who worked on the inquiry into the Iraq war and has reviewed the government's early response. Boris Johnson was focused on protecting the economy, and his instincts are liberal. "Of course people must make their own decisions," he told a press conference. "I'm a believer, as I say, in freedom." He was unlikely to scrutinise advice that went with his grain.

Then it became clear just how fast the disease was spreading. On March 13th, Neil Ferguson of Imperial College London, whose team has produced the outbreak's most influential modelling, presented analysis to SAGE which showed hospitals would soon be overwhelmed. Policy changed—but not swiftly enough. On March 16th Mr Johnson advised people to avoid all unnecessary contact. On March 18th he announced that schools would close. It was not until March 23rd that he ordered people to stay at home.

As a result of the government's tardiness, Britons were slower to change their behaviour than people in France, Spain or Italy (see chart 2). When the country finally locked down, the virus had spread further than in those countries (see chart 3). Professor Ferguson now estimates that, since the epidemic was doubling in size every three to four days, if the country had locked down on March 16th, the death toll would have been reduced by at least half.

Choosing when to lock down was a difficult decision. The same was not true of building testing and tracing capacity. In the middle of February, SAGE noted that PHE could trace only five new cases a week, and that it might be possible to raise this to 50 cases a week. By the time the virus was spreading fast PHE still only employed a couple of hundred contact tracers. The route that some of the most successful countries, such as Denmark, Germany and Switzerland have followed, of tracing infected people's contacts and containing outbreaks of covid-19 locally, was thus closed to Britain.

The lack of testing was a bigger problem still. Early on, the shortage made it hard for scientists to get a true picture of how far the virus had spread, and SAGE repeatedly emphasised the need to increase capacity, to little avail. Even by the middle of April Britain was testing people at a third Germany's rate. For six weeks, it lagged the rest of Europe (see chart 4).

At the time, PHE had sole responsibility for testing. In contrast to Germany, which used a large number of private and university laboratories, PHE tried to boost its own capacity. "They had shown they couldn't ramp up supply, and that was because they were using homebrewed tests," says an insider. It was only after the government belatedly set out a plan in early April to use university and private-sector facilities to run commercial tests, and passed responsibility for this to the Office for Life Sciences, a smaller, more agile government body, that capacity jumped.

The shortage had particularly grim consequences in care homes. With limited testing available, staff with symptoms were instructed to stay at home, which resulted in a spike in the use of agency workers, who moved from one home to another. Care homes also took lots of those rushed out of hospitals to free up beds, without the ability to test many of the new arrivals. Asymptomatic care-home workers gained access to testing only on April 29th. Scientists at Imperial College London tested staff at three care homes in the capital in April. In two homes, staff tested negative; in one, three of 19 were positive but asymptomatic, meaning they could have been spreading the virus unknowingly.

The decision on whether to make people wear face-coverings ought to have been a simple affair. Many scientists were lobbying for it, on the grounds that they cost nothing, laboratory tests show that even home-made masks can block transmission and countries that adopted them early also succeeded in containing the disease swiftly. On April 14th Sadiq Khan, the mayor of London, asked the government to make such an order. SAGE was ambivalent; on April 21st it said it regarded the evidence for them as "weak" but recommended that they should be worn in crowded public spaces. By June 4th, when the government announced that people should wear face-coverings on public transport, they were worn universally in East Asia and much of Europe had made them compulsory. Britain, along with America, was an outlier.

Why Britain took so long to follow is unclear; most likely it was because of a parochial failure to observe best practice abroad and an Anglo-Saxon fear of appearing nannying. It still does not require them in shops: most of the Britons crowding back into newly reopened retail outlets have their faces uncovered.

Economic life is restarting in Britain, but more slowly than elsewhere. Hospitality remains shuttered. While the best London offers is a takeaway pint from a handful of pubs, in Paris or Berlin one can enjoy a bottle of wine in a restaurant. According to a tracker maintained by the Blavatnik School of Government at the University of Oxford, the cumulative stringency of the government's lockdown is now about 10% higher than the rich-country average.

Britain's economic structure—it is under-represented in the worst-hit businesses, such as transport and hospitality, and has a lot of service jobs that can be done from home—should have insulated it somewhat against the covid-19 shock. But because of the long lockdown, it looks likely to be near the bottom of the global league table for growth in 2020 (see chart 5).

The best performing rich countries, such as South Korea, are those that managed to keep the pandemic under control. The worst hit economically, such as Spain and Italy, are those with much higher death rates. When public opinion will not tolerate elevated death rates, the trade-off between public health and the economy dissolves. A healthy population and a healthy economy go hand in hand.

That the British government has provided its people with neither is reflected in opinion polls (see chart 6). The prime minister himself remains fairly popular, but his ratings are in decline. He won sympathy when he succumbed to the disease, but has lost it in other ways. The revelations that he missed five consecutive meetings of the COBRA emergency committee when the virus was taking hold, and that Dominic Cummings, his chief adviser, broke the lockdown rules he helped design, fuelled suspicions that the government did not take the crisis sufficiently seriously.

The political consequences of this failure are likely to stay with Mr Johnson during his time in power (see article). The man who expected to be defined by his ability to "Get Brexit Done", as his election slogan went, will be remembered for something else altogether. As one of his Conservative predecessors, Harold Macmillan, responded when asked what was most likely to blow a government off course: "Events, dear boy, events."

Those events are far from over. Every day throws up a difficult new decision. It is unclear how to get schools to reopen or persuade parents to take their children back to the classroom. The government is under pressure to reduce the two-metre social-distancing rule, but more than 1,200 new infections a day are being identified in Britain, compared with a few hundred in Italy, France and Germany. Loosening social-distancing rules and reopening the economy under these circumstances is a risk.

Mr Johnson has a knack for getting away with things, and perhaps this gamble will come off. The previous ones he took with the nation's health, however, did not. ■

Editor's note: Some of our covid-19 coverage is free for readers of The Economist Today*, our daily newsletter. For more stories and our pandemic tracker, see our coronavirus hub*

Drug discovery

Dexamethasone cuts covid-19 deaths

A cheap drug can make a big difference

Jun 20th 2020 |

THE GOVERNMENT'S public-health performance may not look good, but Britain's scientists are still top-notch when it comes to inventing and discovering drugs. On June 16th researchers at the University of Oxford announced that they had identified the first drug proven to reduce mortality from covid-19. Dexamethasone, a cheap steroid, reduces deaths by a third among the most severely ill patients. It is set to become the standard of care for the National

Health Service (NHS) across Britain. Doctors around the world will, undoubtedly, follow suit.

The results came from RECOVERY (Randomised Evaluation of COVid-19 thERapY), the world's biggest clinical trial for covid-19 drugs. The trial, run by Oxford and the NHS, is testing a range of drugs on covid-19 patients in 176 hospitals across Britain. Dexamethasone is an anti-inflammatory that is already used to treat a variety of health problems, such as rheumatoid arthritis, eczema, asthma and some cancers. It was included in the covid-19 trial because steroids were tried as a treatment for SARS (severe acute respiratory syndrome), a related lung disease, with mixed results.

As part of the British trial 2,104 patients were randomly assigned to receive dexamethasone and compared with 4,321 patients who received the usual standard of care alone (which includes treatment for dehydration and pre-existing health problems, plus oxygen or a ventilator if needed). Among those who received only the usual care, 41% of patients ill enough to need ventilators died within 28 days; so did 25% of those on only supplemental oxygen and 13% of those who did not need help to breathe. For patients treated with dexamethasone, the 28-day death rate was 28% for those on ventilators and 20% for those on oxygen. There was no benefit from the drug for the rest.

This is big. If doctors in Britain had known from the start what they know now about the effectiveness of dexamethasone, they could have saved as many as 5,000 lives since the country's covid-19 epidemic began. That is roughly 10% of the number of people who have died from the illness in Britain. It is a generic drug that hospital pharmacies usually have on their shelves. A course of treatment costs the NHS about £5 ($6.30). In poor countries it would cost about $1.

Clinical trials of various drugs are going on in many other countries. But Britain has been particularly committed to doing large, rigorous trials while battling a big covid-19 wave. Such trials are easier to do in the NHS than in more fragmented health-care systems, especially when results are needed urgently. As the pandemic gathers speed around the world, dexamethasone can make it a little less deadly.■

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International

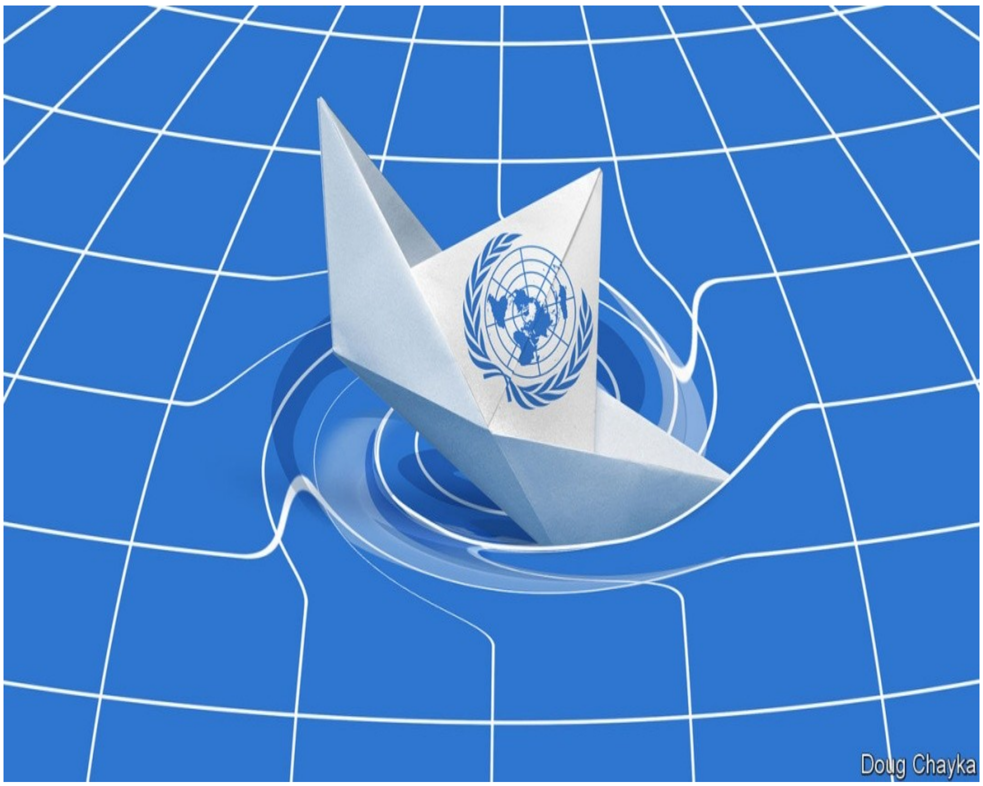
Special report

Time to rediscover statesmanship

Three future scenarios for the UN

Bedlam, bumbling or boldness?

Jun 20th 2020 |



In a speech in January Mr Guterres conjured up "four horsemen" to describe the challenges facing the world. The first represented the worst geostrategic tensions in years, with a real risk of a "great fracture". Next, said the secretary-general, the planet was burning, and an existential crisis was close to a point of no return. His third horseman took the form of rising global mistrust, often spilling into hatred, amid discontent over inequality and the sense among too many that globalisation is not working. Lastly, the dark side of digital technology threatened to invade privacy, disrupt work and unleash lethal autonomous machines in war.

If this was not apocalyptic enough, a fifth horseman is now galloping around the globe. Covid-19 has claimed hundreds of thousands of lives and plunged the world into a recession far deeper than that of 2008-09. Worse could be to come if the virus proceeds to devastate poorer countries before boomeranging back into rich ones. And in response the world has seemed rudderless. National leaders have been too preoccupied fighting the disease in their own countries to have much appetite for international efforts. And at the UN, the Security Council has been a bystander.

The nightmare scenario is a descent into deepening disorder. Imagine that after the covid-19 crisis is over, Mr Guterres's horsemen run rampant. Any hope that the world can summon the will to tackle climate change vanishes. Under pressure, institutions that have sustained a rules-based system buckle. Unrestrained protectionism kills the WTO. America abandons NATO, as its European partners slash defence spending to prioritise economic recovery. Divisions between northern and southern members prove too much for the EU. The UN goes the way of the League of Nations, failing to stop rival powers from provoking each other and, in the end, fighting.

While such bedlam is possible, a likelier scenario is less dramatic: bumbling along. Inertia helps the main multilateral institutions survive, despite their inability to modernise themselves, and second-tier powers keep co-operation alive. Future American presidents restore a degree of confidence in the country's commitment to the international order, although the trauma of transactional Trumpism casts a long shadow. America's return to the Paris agreement lends weight to efforts to tackle climate change.

The tussle between America and China continues. But America makes a more concerted counter-push, working with its European and Asian allies, with a revived championing of universal values. In many parts of the world mistrust of China runs deep. Russia still makes mischief, but less often, since a more coherent West gives it fewer opportunities. The multipolar system becomes less "chaotic" and more contained, settling into an uneasy stalemate. Perhaps this is enough to keep the four horsemen in their stables.

Just possibly, extraordinary times could provide the jolt the world needs to be bolder

Bumbling along in this way would not be the worst outcome. But it would be a waste of a crisis. Just possibly, extraordinary times could provide the jolt the world needs to be bolder, even if for now this seems improbable. Little or no global leadership can be expected from America under Mr Trump. The pandemic has pushed most other issues aside: planned gatherings on big global issues, such as climate change and nuclear non-proliferation, have been postponed. Yet the delay may be a blessing in disguise, giving fresh thinking a chance.

Already, some see opportunities ahead. In Europe Mr Macron is alive to the idea that the time may become ripe for big ideas. Britain's Boris Johnson always welcomes a chance to play Churchill. Ideas for making the post-covid-19 economy greener are sprouting, as are concerns to make it fairer. Perhaps China could be persuaded to take part in a new round of nuclear arms control, which could serve as a start to rebuild relations with Russia.

Global organisations have a shot at change, too. Just as the second world war prompted leaders to create institutions to prevent wars, Bill Gates believes the covid-19 crisis will lead them to build institutions to prevent pandemics and, alongside national and regional bodies, to guard against bioterrorism. Co-operation on viruses could serve as a model for collaboration to strengthen resilience in cyberspace. The shock to the system could even be profound enough to prompt a serious go at reforming the UN Security Council before it grows even less representative of the realities of power in the 21st century. Ample groundwork has been done. What is missing is political will.

Let's go to San Francisco

None of this can happen overnight. A start could come from a P5 summit, with a further push at the 75th-anniversary meeting of the Global Assembly in September. Because of the pandemic, this will be a more limited affair than originally envisaged, perhaps with a mix of physical and virtual presence, but it can still dignify the occasion and show a worldwide wish for closer collaboration. It should also be an opportunity to look ahead, mapping the way to reforms designed to ensure that the UN is still in business at 100.

If the wartime model were followed, the road might even lead to a grand convention, as in San Francisco in 1945. The main actors at that conference were the delegates of the governments involved, especially the big powers. But in all—counting the secretariat workers, the press, interpreters, security personnel and assorted lobbyists and observers—about 5,000 people crowded into town, in a foretaste of the General Assembly that clogs New York every September. "Consultants" representing industries, labour, religions, professions, women and minorities were accredited. They managed to influence the charter on education and human rights, and successfully pushed for an article allowing the UN's Economic and Social Council to consult NGOs. A rethink of the rules ought to be even more inclusive.

Such a prospect looks far-fetched when the world is consumed by the fight against a virus, and when America and two other big powers are waging a new cold war. But in the midst of the second world war it was hard to imagine that institutions would emerge that would keep the peace for three-quarters of a century. The statesmanship that created them is now needed once again.■

Business

Fashion victims

How slow times in the luxury world will separate the bling from the chaff

Posh purveyors are having to rethink their business model in a hurry

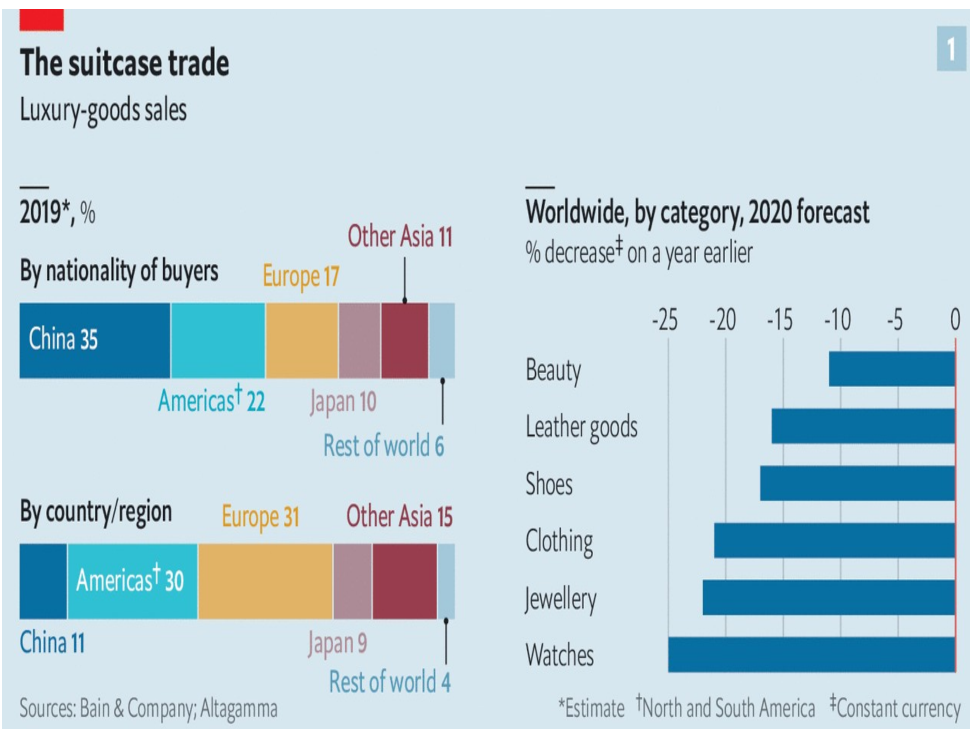
Jun 20th 2020 | PARIS

MILAN, PARIS or New York this time of year would usually be teeming with fashionistas scrambling to get from the Balenciaga show to the Chanel party. Not in 2020. Fashion weeks have been cancelled, repurposed as posh catwalk webinars. Shops selling Hermès ties and Prada pumps are only just reopening, wondering what to do with stock of pre-covid-19 vintage. Instagram influencers normally on hand to feed the hype have nothing to snap.

The world of personal luxury goods—from handbags and haute couture to diamond rings and pricey Swiss watches—has been in hibernation. At the height of the pandemic between March and May sales slumped by 75% or so on a year earlier, according to the Boston Consulting Group. They have slowly picked up as Asia, then Europe and America, started reopening. Even so, the outlook for the luxury world is far from glittering.

The global recession hangs over a sector fuelled by consumer confidence. Beyond that short-term shock, the industry is facing an overhaul in how its baubles are made, where they are sold and to whom. Trends once expected to play out over a decade may unfold in mere quarters. Rapid change has set nerves jangling in a business meant to exude timeless tradition.

Start with who is buying and where. Although most purveyors of luxury are European (with America home to some of the lesser marques), most of their customers come from Asia. Asians bought more than half of the €281bn ($315bn) in bling sold last year. Chinese buyers alone have gone from 1% of purchases in 2000 to 35% last year, according to Bain, another consultancy. But most of that—perhaps 70%—was purchased overseas, often on jaunts to Europe. Just over a tenth of all luxury sales were actually booked in mainland China.



The Economist

Unless intercontinental tourism rebounds faster than expected, new ways will have to be found to get Euro-chic into Chinese hands. Firms hope that shopping sprees will simply move from Paris to Shanghai. In the short run, this might boost margins: the likes of Louis Vuitton (part of LVMH, the biggest luxury group) and Gucci (part of Kering, another French giant) charge a third more in China than in Europe for the same products. Closing a few flagship stores in high-rent tourism hotspots such as Paris or Milan, which usually sell half their stock to tourists, could save firms money in property costs.

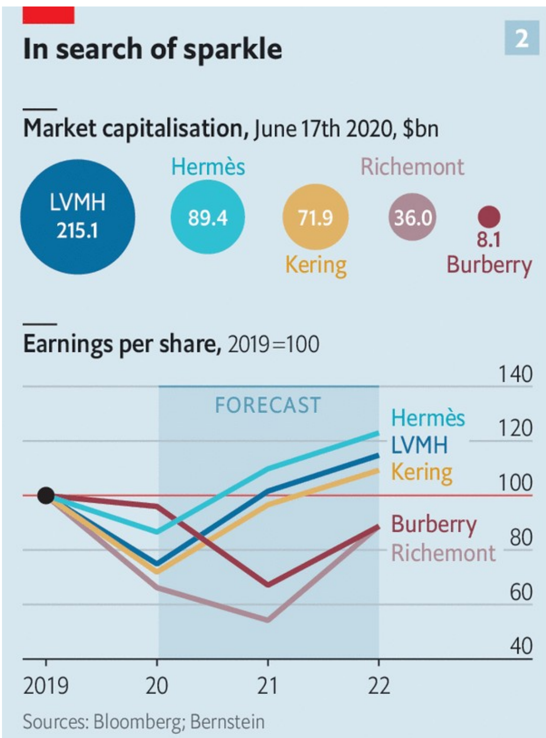
Yet any boost to margins may be short-lived. The difference between European and Chinese prices has narrowed. Those in China have been declining as apps make international price comparisons easier and firms woo shoppers facing ever more restrictions from Chinese authorities on bringing luxury items home from abroad. And more shops on the mainland, in cities they would once have deemed déclassé, may diminish the aura of exclusivity that shopping on Avenue Montaigne in Paris or New York's Fifth Avenue confers. The de facto discounts were aimed at luring buyers to the West precisely for that reason.

The pandemic has accelerated other trends. Online sales of luxury goods, at 7-8% of the total on average, are around half those of mass-market fashion retailers like H&M and Zara. The closure of shops has, predictably, eased some of the reservations brands may have about selling their wares on the internet. LVMH has said online purchases are "significantly higher" as a share of sales than pre-pandemic. Sales through department stores—which are in terrible financial shape, notably in America—are also likely to shrink.

Meanwhile, costs may rise. Though they love to show off in-house "artisans" stitching handbags and the like, even the poshest *maisons* quietly outsource some of their production. Many rely on outsiders for more than half their products. These suppliers are often small family firms in Italy, which went into the pandemic with slim margins and slimmer financial buffers. Luxury groups are now having to assist them financially in a hurry lest they disappear for good.

All this paints a drab financial picture. Sales are forecast to fall by a third in 2020, and recover only by 2022 at the earliest. That will crimp margins, since luxury firms' costs are largely fixed. Rents must still be paid and brands advertised—the poshest ones spend the best part of $1bn a year on marketing—even as sales droop.

In many industries, squished margins and falling sales might lead to a slew of takeovers. Few expect that to happen in luxury. Most of the big players have healthy balance-sheets and are expected to find ways to return to profitability (see chart 2). Many smaller marques are controlled by founders or their families, who are loth to sell in a downturn. If anything, consolidation might slow; all eyes are on whether LVMH will complete its $17bn takeover of Tiffany, an American jeweller, agreed weeks before covid-19 struck.



The Economist

Not all parts of the industry are equally vulnerable. In a crisis, buyers stick to more established brands. "They want the best of the best," says Luca Solca of Bernstein, a broker. Good news, then, for the likes of Louis Vuitton and Chanel, which have in fact pushed up prices in recent months. In contrast, brands hoping for a turnaround in their fortunes—Burberry is a perennial candidate—are less able to gain the attention a relaunch might otherwise garner.

Some segments have also been hit harder than others. Perfumes and cosmetics have held up best: a lockdown is no reason to forgo a skincare regime, apparently. Fashion houses face bigger problems, as cooped-up fashionistas see less need to replenish their wardrobes. Worse, unlike jewellery or handbags, surplus stock of apparel is rapidly going out of style. Overt discounts are frowned upon in luxury for fear of cheapening precious brands. Most at risk are fancy watchmakers like Richemont, which attract sellers at fairs and trade shows that have now been cancelled.

The question is whether amid this shake-up the luxury world can keep its grip on the wallets of the world's big spenders. Fears that consumers would opt for a more ascetic post-pandemic future are dissipating: reports of "revenge shopping" as China emerged from lockdown implies that rich folks' appetite for status symbols remains intact. But these worries are being replaced by those over Chinese shoppers developing a taste for nascent local brands, at the expense of the old-world stalwarts.

The biggest potential changes may concern the designers themselves. By late June the most exalted would normally start displaying autumn and winter collections in shop windows. This year they will make up for lost time by selling their summer season through the summer, as might seem sensible anyway. Giorgio Armani, an Italian veteran, has argued this should become the new norm. What a bold fashion statement that would be.■

Editor's note: Some of our covid-19 coverage is free for readers of The Economist Today*, our daily [newsletter](). For more stories and our pandemic tracker, see our [coronavirus hub]()*

Beyond the pale

Will Silicon Valley face up to its diversity problem?

The tech industry's response to the killing of George Floyd has been stronger even than in other parts of the economy

Jun 20th 2020 | PALO ALTO

To GET A sense of diversity in tech, take a stroll on University Avenue in Palo Alto, a city at the heart of Silicon Valley. Before the pandemic, if you encountered a black person, the chances were they worked in a local shop. African-Americans account for 3% of workers at America's five biggest technology firms (see chart) and probably less at smaller ones. About one in 50 partners at venture-capital (VC) firms is black. The figure among VC-financed entrepreneurs is one in 100. Such dismal numbers, and Silicon Valley's meritocratic pretensions, help explain why tech's response to the killing of George Floyd has been louder even than other industries'. Will outrage lead to lasting change?

Pushed by a left-leaning workforce, big tech now regularly takes an activist stance on important issues, from immigration to the pandemic. Yet even by these standards, the reaction to the Black Lives Matter protests has been remarkable. Firms offered donations to race-related charities, set up funds to finance startups by non-white founders, stopped selling controversial technologies such as facial recognition and vowed to purge their software of racist language. Apple and YouTube (part of Google) each pledged $100m to combat racism with educational schemes and support for black artists. On June 17th Google said it would raise the share of "under-represented groups" in leadership by 30% by 2025.

Yet corporate activism will amount to little if tech firms and their financiers do not change how they operate, says Sydney Sykes, co-founder of BLCK VC, a group on a mission to swell the ranks of black venture capitalists in America. Companies must make more of an effort to promote and retain minority employees. VC firms have to examine why they often reject pitches by minority entrepreneurs; a simple "just can't get excited about this" is no longer enough. They should also broaden their professional networks beyond the usual lily-white crowd, argues Elliott Robinson of Bessemer Venture Partners, a big VC firm.

Since diversity, particularly on gender, became a hot topic in the tech industry a few years ago, progress has been slow. But Ms Sykes believes things will speed up now. Customers and employees want it. And the firms have started to twig that lofty statements and charity do not suffice. Facebook's chief diversity officer, Maxine Williams, now reports directly to Sheryl Sandberg, the firm's number two (though not to its boss, as some would like). At Reddit, a popular discussion website, a white co-founder, Alexis Ohanian, stepped down from the board to make way for a black replacement, Michael Seibel, boss of Y Combinator, a startup school. On June 17th Apple said it would replace its diversity chief.

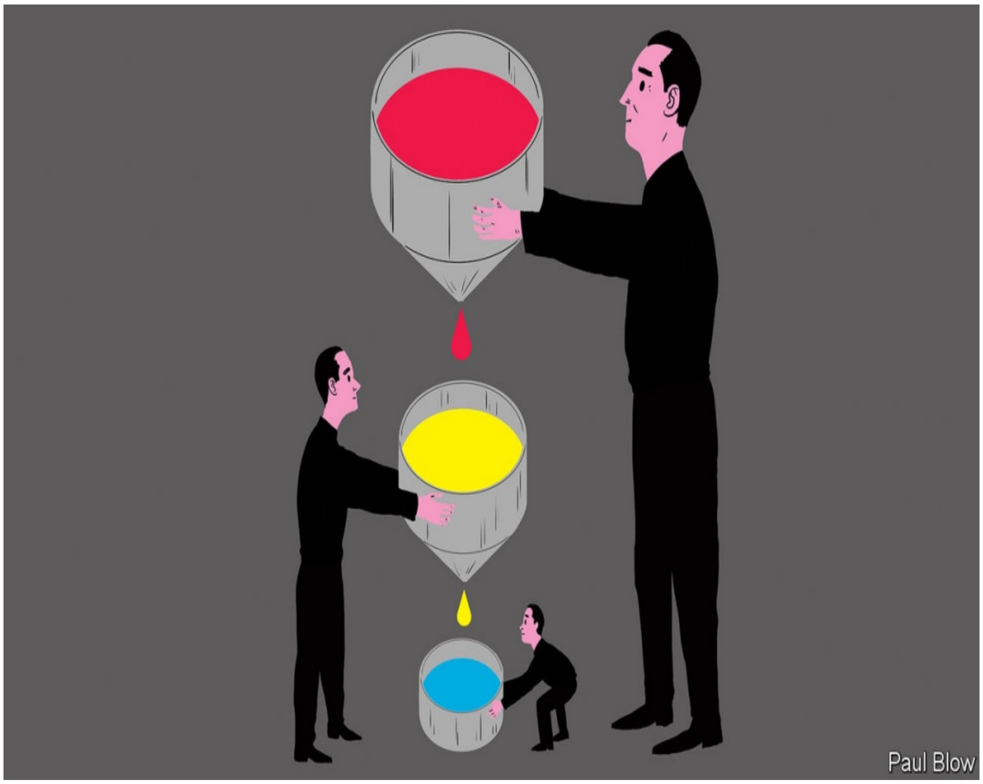
Mr Robinson has long lamented the tech industry's "diversity theatre": grand statements followed by little action. But even he is somewhat hopeful. Thanks to smartphones, he says, whites can see for themselves how black people are treated—and want it to stop. He knows all too well: he has been forcibly restrained by police three times in his life, for no reason other than the colour of his skin. The last time was not far from University Avenue.■

Bartleby

Waging war on recessions

An early analysis of furlough schemes

Jun 20th 2020 |



SINCE THE emergence of the welfare state, adults who want to work have generally found themselves in one of two positions: earning a wage from their job or receiving unemployment benefits. The pandemic has led many people to find themselves in a halfway stage—furlough. This often involves the state paying a large slice of employees' wages so that firms can keep them on the payroll during the lockdown.

How effective is this approach? A new paper* by Morten Bennedsen of INSEAD business school in France and colleagues surveyed 8,781 Danish firms with anywhere between three and 2,000 employees. Around two-thirds of the firms said that the effect of the pandemic on their revenues had been negative, or very negative. Of those companies that had experienced a fall in revenues, the median decline was 35%.

The Danish government offered a variety of financial-aid programmes to firms, including a furlough scheme which paid 75% of salary costs (subject to a cap) to eligible companies. The academics found that 56% of the firms surveyed had taken some form of government aid and this was true of almost all businesses that had suffered a revenue decline of more than 50%. Unsurprisingly, companies in the most distressed industries were most likely to have taken assistance.

The aid seemed to work. Firms that received it laid off fewer workers and furloughed more people than firms which received no aid at all. But, as the authors of the study point out, this definition of success might be subject to a selection bias—firms that wanted to furlough workers may have been likelier to apply for aid.

So they also asked firms a counterfactual question: what decisions would they have taken had they been unable to get aid? On this basis, the researchers estimate that taking the aid increased a firm's furloughed workers as a share of its total workforce by about 20 percentage points, and decreased the share of laid-off workers by almost the same amount.

If these findings are replicated elsewhere, furlough schemes may be adopted in future recessions. Some commentators point to the record of Germany, which suffered a much smaller rise in unemployment than other rich countries during the recession in 2008-09 because of a scheme that subsidised short-term working.

There are two obvious concerns about such support schemes. The first is the cost. The British scheme, which started in March, is expected to cost around £60bn ($75bn) by the scheduled end in October, or a bit less than 3% of GDP. The second problem is that such schemes may prevent the necessary role that recessions play in "creative destruction", whereby resources are reallocated from failing businesses to successful ones (see article). The survival of "zombie" companies may make the next recovery less vigorous.

On cost, the counterargument is that widespread job losses lead to deep recessions and thus sharp declines in government revenues. They can also be bad news for laid-off workers who may take years to find another job. Paying money upfront to reduce the severity of a recession can thus be a good investment in both social and economic terms.

It would be great if governments could save only companies that have a viable long-term future. The analogy might be an old rule of thumb among central bankers that they should lend money in financial crises to banks that have a liquidity problem, not a solvency one. In practice, however, financial crises in recent decades have been so acute that central banks have mostly been unable or unwilling to discriminate. Similarly, while governments have imposed conditions on wage-support schemes in the current crisis, their main priority has been to dole out aid as quickly as possible in order to save jobs.

A lot more research is clearly needed to see whether furlough support schemes will have adverse long-term economic effects. The longer the schemes are in place, the more likely it is that market distortions will occur. But the principle that governments should intervene to support struggling banks and unemployed workers, as a way of reducing the severity of recessions, has long been established. It is conceivable to think that furlough schemes might eventually be viewed in the same light.

* “The impact of public aid programs on distressed firms: Evidence from COVID-19 in Denmark”, by Morten Bennedsen, Birthe Larsen, Ian Schmutte and Daniela Scur■

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Much ado about Samsung

No end in sight for Samsung's legal troubles

South Korea's biggest conglomerate faces more scrutiny from prosecutors—and the public

Jun 20th 2020 | SEOUL

Lee jae-yong has seen a fair share of prison cells. Samsung's de facto boss, and grandson of its founder, spent nearly a year behind bars for bribery before his sentence was suspended in February 2018. Then, on June 4th, prosecutors asked a court to have Mr Lee and two other executives from South Korea's biggest conglomerate arrested ahead of indictments on fresh charges of unfair trading, stock-price manipulation and violating accounting rules, citing concerns that they might destroy evidence.

The judge demurred and declared that Mr Lee could await the start of his latest trial at home, rather than in police custody, arguing that the prosecution had already amassed enough relevant evidence. Although critics spied a certain leniency towards Mr Lee at work in the ruling, it does not mean that his or Samsung's legal troubles are anywhere near over.

The latest allegations by state prosecutors relate to the role Mr Lee allegedly played in manipulating the terms of a merger between two Samsung affiliates, Samsung C&T and Cheil Industries. The tie-up cemented his control over the group in 2015. (Three executives have already been sentenced to prison for hiding or destroying evidence related to the investigation.) The bribery charges that saw him locked up were also related to the merger. Last year South Korea's Supreme Court ordered a retrial in that case. (Samsung and Mr Lee deny any wrongdoing.)

Shortly before prosecutors requested the latest arrest warrant for Mr Lee, Samsung asked them to convene an external committee to opine on whether the charges merited a trial. (The committee is due to issue its non-binding recommendation by July.) Neither case is likely to be resolved before 2021. Both could land Mr Lee behind bars once again.

The heightened legal scrutiny and uncertainty casts a shadow over the group's decent performance in the pandemic. Samsung Electronics, the group's listed crown jewel, reported higher sales and stable profits in the first quarter. In April Samsung Biologics, a biotech arm part-owned by Samsung C&T, signed a $362m deal to make an antibody treatment against covid-19.

The affair may also hurt the group's efforts to get back in South Koreans' good graces. In May Mr Lee apologised to his compatriots, acknowledging that the group had "not always strictly followed laws and ethics". He pledged betterment, including an end to dynastic succession and to the group's hostility towards labour unions. Samsung has also joined the fight against covid-19 by keeping its factories running and donating equipment to hospitals at home and abroad. All the self-flagellation was working: one widely cited analysis of online comments found that public sentiment towards Samsung improved following Mr Lee's apology.

More images of him emerging from courtrooms looking sheepish may reverse that trend. That may be a reason why Samsung has been unusually vocal in defending its boss against the latest charges. On June 7th, three days after the prosecutors requested Mr Lee's arrest, Samsung Electronics sent a statement to reporters reiterating that all activity relating to the merger had been "legal in compliance with relevant regulations and procedures". It pleaded with them to refrain from "immoderate reports" that could damage the firm, and by extension the national economy, at a time of crisis.

Stressing lofty principles such as the national interest over petty concerns like law-abidance is a well-worn argument among South Korean conglomerates that get into trouble. The coming months will show if it is wearing thin.■

Chopped and screwed

Why corporate disputes in China still revolve around rubber stamps

Who controls the chop controls the company

Jun 20th 2020 |

China is in the vanguard of new technology, from facial recognition to 5G networks. Many Chinese firms, though, rely on something from an earlier age: a hard, usually rubber chop with a firm's name engraved on it, to be dipped in crimson ink and stamped on important documents. Chopping is seen as more authoritative than a mere signature. The 2,000-year-old tradition may seem quaint. But in China, who controls the chop controls the company.

Consider three ongoing kerfuffles. On June 4th the board of Arm China, the Chinese joint venture of a chip designer owned by Japan's SoftBank, voted to remove its boss, Allen Wu. Just one snag: Mr Wu refused to go. Because he still holds the chop, he has continued to act in Arm China's name, and threatened legal actions to defend his position. A week later Bitmain, which makes bitcoin-mining computers, announced that it had replaced its old chop with a new one. They looked virtually identical—Bitmain's Chinese name in a red circle around a star—except for a new serial number. But it was enough to indicate that one of the feuding co-founders, Micree Zhan, now has the upper hand.

The oddest recent chop bust-up occurred in April. Li Guoqing, the ousted co-founder of Dangdang, a once-popular e-commerce platform, broke into its headquarters and, in a bid to retake the company, removed dozens of its official chops (besides the main chop, others are used for things like contracts and tax receipts). Dangdang declared the seized chops to be invalid. But on June 13th it was reported that the police had cleared Mr Li of wrongdoing, implying the chops are his for now.

Chops have figured in business fights elsewhere. In 2007 Russian police seized seals from Hermitage, an investment firm owned by Bill Browder, a deported financier, and used them to re-register its companies under others' names. But in 2015 Russia eliminated the need for company seals. In Japan and South Korea, where chops are still used, tussles over them are rare.

In China's sharp-elbowed business world chop rows remain more common—and mostly unreported. Managers sometimes misuse seals to enter side contracts. Lawsuits to reclaim a chop can drag on, says Eric Carlson of Covington & Burling, a law firm, so many cases are resolved out of court. But, he notes, technology is catching up with tradition. China is starting to deploy electronic chops, which are easier to monitor—and to strip from aggrieved wielders.

The Reimann hypothesis

A peek inside JAB Holding

One of Europe's biggest family-owned companies is also among its most taciturn

Jun 20th 2020 | BERLIN

THE REIMANNS are as fabulously rich as they are faceless. On turning 18, each of Albert Reimann's nine children signed a codex, pledging to stay out of Benckiser, the family chemicals business in Ludwigshafen, Germany, and never show their face in public. Reimann died in 1984, leaving each of his offspring with 11.1% of his company. Good luck finding a photograph of any of them, including the five who have sold their stakes in the family concern. Its public face is Peter Harf, a Harvard-educated manager whom Albert hired in 1981 as an adviser. A restless sort, with a sharp mind and a dislike of sharp suits, which he spurns for jeans and colourful shirts, Mr Harf transformed Benckiser from a medium-sized manufacturer typical of

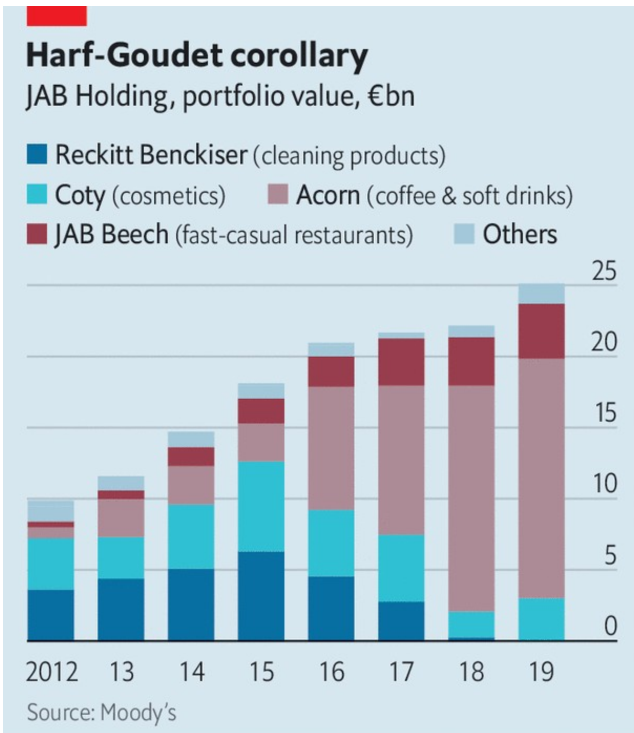
Germany's Mittelstand into an international consumer-goods powerhouse overseeing operating companies worth some $120bn.

JAB Holding, as the Luxembourg-based group was renamed in 2012 in honour of its founder, Johann Adam Benckiser, is as anonymous as its camera-shy owners. Its assets are anything but. Having sold off the last of its stake in Reckitt Benckiser, a London-listed consumer-goods group, in 2019, JAB has focused on three main business lines. The first two revolve around caffeine and carbs. Over the years JAB has snapped up purveyors of coffee (like Keurig and Jacobs) and places to consume it (Peet's Coffee and Pret A Manger, among others), as well as makers of sugary drinks (Dr Pepper) and sellers of snacks (such as Krispy Kreme Doughnuts and Panera Bread). These operations accounted for 85% of JAB Holding's estimated €25bn portfolio in 2019.

Most of the rest sat in beauty. In 1992 Mr Harf orchestrated JAB's purchase of Coty, a maker of perfume, from Pfizer, an American drugmaker, for $440m. Coty was listed in New York in 2013, and in 2016 Mr Harf added to it 41 beauty brands, including Wella (shampoo), Max Factor and Covergirl (make-up), bought from Procter & Gamble (P&G), an American giant, for $12bn.

Alongside JAB Holding, which manages the Reimanns' money (and that of Mr Harf, whom they treat almost like a family member) is a larger sister holding, JAB Consumer Fund (JCF), with investments in the same group of businesses. It was set up in 2014 with cash from other wealthy families, including the Peugeots, a French carmaking clan, and Colombia's Santo Domingo beer dynasty.JCF adds complexity to the federation, which comprises several intermediate holding companies co-owned by JAB and JCF that in turn control underlying operating assets. But it enables the structure to take on more debt, which Mr Harf has used to enlarge the empire with deals like the $19bn purchase of Dr Pepper Snapple in 2018. The two vehicles are run jointly by Mr Harf and Olivier Goudet, a former finance chief at Mars, a huge American confectioner (which is also family-owned). An admirer of Warren Buffett, Mr Harf likes to refer to the JAB-JCF as Benckiser Hathaway.

Like the famed American investor's conglomerate, JAB favours long-term bets on businesses that are easy to understand. What sets it apart from Berkshire Hathaway, and many family offices, is a focus on a few big assets. According to Moody's, a credit-rating agency, 96% of JAB Holding's funds were in the three biggest last year (see chart). Investor AB, another large and complex investment fund, controlled by Sweden's Wallenberg clan, has 37% of its portfolio in its top three assets. Mr Harf wants JAB Holding to own a stake of 30-40% in each portfolio firm, so that even if JCF's backers exit, the Reimanns would retain the ear of the operating firms' CEOs.



The Economist

Such concentration is a boon when things are going well, as they have been with the coffee business, which Mr Goudet envisaged as a rival to Switzerland's Nestlé. Defying the covid-19 pandemic, JAB listed 16.5% of shares in JDE Peet's, the result of a merger between Jacobs Douwe Egberts and Peet's Coffee, at the end of May in Amsterdam. Out of ten "smart investors", nine warned Mr Harf to wait with the IPO, he says. In the event, the offering raised a caffeinated €2.25bn, making it Europe's biggest IPO this year and valuing the firm at €15.6bn. The share price surged by 15% on the first day of trading. The outlook for JAB's other cafés, starved of customers amid pandemic lockdowns, may improve as economies reopen.

The same cannot obviously be said of the cosmetics arm. Mr Harf may have overpaid for P&G's brands and folding them into Coty has proved tricky. Coty's market capitalisation has shrunk by more than 80% since 2016, to $3.7bn. In May KKR injected €750m into the debt-laden business, which will eventually give the private-equity firm a 60% stake in a professional-beauty firm to be hived off from Coty. Mr Harf himself will run the consumer operation. On June 1st he took over as Coty's CEO after it went through four chief executives in five years, to clean up what he calls "the greatest blemish on my vest".

"Overall Mr Harf has done well for the Reimanns," says Jean-Philippe Bertschy at Vontobel, a Swiss bank. Despite Coty's pallid record, JAB investor returns have averaged 15% a year since 2012. But Mr Bertschy cautions JAB against more break-neck acquisitions. Previous ones provoked the departure last year of JAB Holding's chairman, Bart Becht, who reportedly quit after failing to convince the other partners to scale back expansion and focus instead on running the companies under their wings better.

Mr Harf will now try to do just that. The spry 74-year-old plans to overhaul Coty, starting with distribution. That will not be easy. Cosmetics is cut-throat and Coty must find a niche between the two giants of the industry, L'Oréal and Estée Lauder, and trendy "indie" brands. At least Mr Harf has plenty of coffee to keep him going. ■

Schumpeter

Can Zoom be trusted with users' secrets?

Kowtowing to China is a big threat to its business

Jun 20th 2020 |

Brett Ryder

FEW AMERICAN companies have done as well during the covid-19 crisis as Zoom. The lifesaver of lockdown joins a small coterie of tech firms whose product, like Google's, you no longer need to explain to grandmas. Zoom's staggering success was made clear this month when it reported a 169% surge in year-on-year sales during the three months to April 30th. Daily participants ballooned from 10m in December to 300m in April; profits soared alongside. Even analysts, rarely the most expressive of writers, let rip. One report started with "Wow". Another, with "Holy Cow".

Zoom's achievements go beyond mere lucre. Its videoconferencing tools have the intuitive simplicity of an Apple product. It has made working from home feel not clunky, but chic. Moreover, its 50-year-old founder, Eric

Yuan, cuts an intriguing figure. He has ridden an emotional roller-coaster this year as his company faced not just adulation, but scathing criticism for privacy lapses, security issues and Zoom-bombings. Yet the speed with which he acknowledged the setbacks, and rolled out a 90-day plan to fix them, offers a case study of a leader who tries to learn from his mistakes. On June 17th, for instance, Zoom said it was introducing end-to-end encryption for all users.

But Mr Yuan, an American citizen, has a more intractable problem. It concerns his country of birth, China. On June 11th it became clear how vulnerable Zoom was to the long arm of the Communist state when the firm, which prides itself on "the open exchange of ideas", admitted it had temporarily shut down the accounts of three critics of the regime outside China. Investors barely noticed. Four days later Zoom's market capitalisation reached a record high of $67bn. But it showed with devastating clarity how tech firms struggle to bridge the digital chasm between China and America. This poses an acute business risk for Zoom.

Zoom's relationship with China is complex. The American company has meagre sales on the mainland. But 700 of its staff are based there, developing global products. It also has servers in China that it says are geo-fenced to store Chinese data only (though in April it admitted the rule may have been breached, a mistake it says it fixed). It says having its engineers in China helps reduce costs. It also hopes to increase sales to China. But its operations there force it to abide by Chinese law. Hence it suspended Zoom meetings with users in China and beyond commemorating the 31st anniversary of the massacre around Tiananmen Square on June 4th, which the Chinese government, hearing about them on social media, considered illegal. It also temporarily blocked an activist's account in Hong Kong. Zoom admits it went too far, says it is developing tools to tackle the problem and pledges that requests from the Chinese government will no longer affect anyone outside mainland China.

That is a hard promise to keep for any company with operations in China. American values of free speech are at odds with those of a surveillance state. American firms that do business in China are used to treading a fine line. Those with a lot of Chinese customers and operations, such as Apple, seek to obey Chinese rules, but only in China. They argue that their Chinese businesses are ring-fenced from the rest of the world. Free speech and data security elsewhere are not compromised. Firms which, like Facebook, are barred from penetrating the Great Firewall can ignore China's rules completely.

Zoom is different. It cannot easily fence off its Chinese operations from the rest of the world because its Chinese product developers are integral to its global business. Yet its activities in China mean it falls under laws that require companies to co-operate with the state and its intelligence services. That raises security and free-speech concerns not just within China but beyond it, too.

The repercussions have started. Some governments, such as Britain's, have reportedly been warned by spy agencies to avoid secret discussions about China on Zoom. China hawks in America's Congress are demanding that the company answer questions about its relationship with the Chinese government. Academics note that Chinese students at American universities may be particularly at risk if their inability to travel to America for covid-related reasons means they have to attend lectures in China via Zoom. James Millward of Georgetown University says it could chill academic freedom. He called on universities to develop an urgent "Plan B" to Zoom. End-to-end encryption to protect privacy may provide some reassurance. Chinese law, however, makes it hard to guarantee that the state will not seek to intrude.

That leaves Zoom with two unpalatable options. The first is the route that ByteDance, a privately held Chinese tech giant, is taking to ensure its short-video app, TikTok, is trusted in America. This means replacing some engineers in China with ones in America, and perhaps cutting off the Chinese business from the rest of the world. Such a rearrangement is hard to swallow for a firm like Zoom, whose mission is to foster global communication. It would cost time and money.

The alternative is to continue to bestride both systems and accept the consequence that trust—arguably the most important attribute of a communication tool like Zoom—is at the mercy of the Chinese Communist Party. Many users will have no problem with that; Zoom book clubs may be happy to bore Chinese eavesdroppers to death. But on sensitive topics in business and politics, wariness should prevail. Even though Zoom says there is no “back door” enabling snooping on its users, in the back of some minds is the thought of using a Soviet telephone during the cold war.

The rebirth of distance

Zoom’s business may suffer as a result. Cisco’s Webex, Microsoft’s Teams and Google’s Meet can easily compete for its most sensitive clients. More significant, the kerfuffle reinforces how geopolitics is splitting the global internet into rival camps. Tech companies are increasingly facing the invidious choice of which side of the divide to be on. The word for that is not “wow”. It is “ugh”. ■

Correction (June 19th 2020): A previous version of this article stated that June 4th marked the 21st anniversary of the massacre around Tiananmen Square. Some of the wording of this article has also been amended for clarity.

Finance & economics

From yields to maturity

The Fed has been supporting markets. Now it must find ways to boost growth

Economists expect it to begin yield-curve control in September

Jun 20th 2020 |

IT SEEMS AS if there is nobody to whom the Federal Reserve will not lend. Since the covid-19 pandemic wrought havoc on financial markets in March, America's central bank has promised to buy up to $750bn in corporate bonds and $500bn in state- and local-government debt. It has stood behind the market for commercial paper, behind money-market funds and behind foreign central banks in need of dollars (see article). On June 15th lenders were invited to register for its "Main Street Lending Programme", which will purchase loans to small- and medium-sized businesses. The same day it announced that it would buy corporate bonds not only through exchange-traded funds, but directly, too. Such uninhibited use of its balance-sheet brings to mind the words of Walter Bagehot, the primogenitor of modern central banking, whose advice for times of stress was to lend “to merchants, to minor bankers, to ‘this man and that man,’ whenever the security is good”.

The security in this case is mostly a guarantee by America’s Treasury to absorb some of the Fed’s losses. And yet the biggest beneficiary of the monetary fire hose remains the government itself. Since early February the central bank has bought $1.7trn of federal debt, equivalent to 163% of the government’s entire net issuance in 2019. On June 10th it promised to keep buying at least $80bn in Treasuries per month. Many analysts expect that in September it will promise to buy as much as needed to keep shorter-term bond yields near zero—a policy known as “yield-curve control”.

In March the Fed’s bond-buying was intended to calm markets and arrest an alarming rise in Treasury yields. It still sees its purchases as preserving “smooth market functioning”. But as the memory of market stress recedes, its focus will shift to stimulating the real economy, about which the Fed is gloomy. Its median rate-setter expects the unemployment rate to be no lower than 6.5% at the end of 2021. On June 16th Jerome Powell, the Fed’s chairman, warned Congress about the potential scars that a long downturn might inflict.

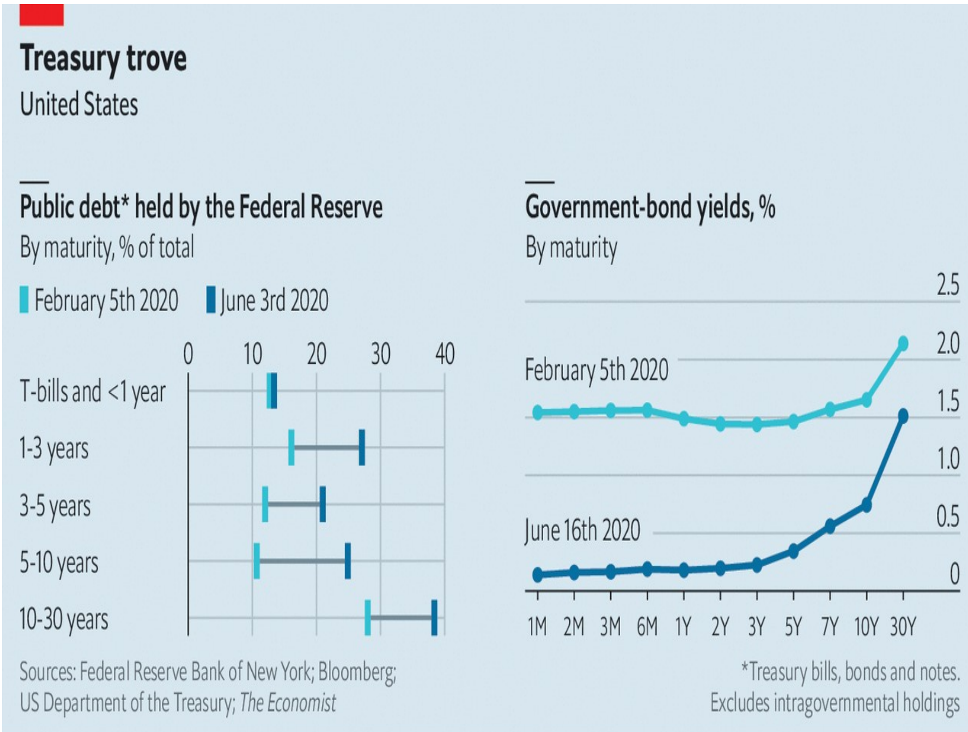
The Fed made a similar transition from supporting markets to stimulating growth after the global financial crisis of 2007-09. It has not attempted yield-curve control, though, since 1951. The possible return to it marks a shift in the debate over market intervention—whether it is more effective to set the quantity you buy, or the price you pay. Choosing one means leaving the other to the whim of your counterparties. In the 2010s the Fed stuck to buying fixed quantities, fearing the unlimited commitment to buy that comes with pegging bond yields. In any case, economists wielded studies that found that bond purchases had a predictable impact on yields.

Yet the attitude of central bankers is evolving. That is partly because of recent experiments with yield-curve control. In 2016 Japan began fixing its ten-year bond yield around zero; in March this year the Reserve Bank of Australia (RBA) started pegging three-year yields around 0.25%. The evolution also reflects doubts about how quantitative easing (QE) works.

Some economists, such as Gertjan Vlieghe, a rate-setter at the Bank of England, and Michael Woodford of Columbia University, argue that, when markets function normally, QE only brings down long-term yields on a sustained basis if it signals to traders that the short-term interest rate—the more humdrum instrument of monetary policy—will not rise for a long time.

Yield-curve control, then, might be a more transparent way of signalling the future path of the short-term rate. The RBA, for instance, pegged the three-year yield at 0.25% in order to underscore its expectation that the short-term rate will stay at that level for several years.

Moreover, yield-curve control can send the signal while reducing the need to purchase vast quantities of debt. As long as investors believe the central bank's promise to target a certain variable, be it a bond yield, an exchange rate or inflation, they tend to bring about the outcome on their own. The Fed's pledge to buy corporate bonds calmed the market in March, for instance, even though it did not start buying until May. So too with yield-curve control. In order to back its peg the RBA has bought only A$50bn ($34bn), less than 8% of Australia's public-debt stock. Although some analysts regard the Bank of Japan's yield-curve cap as an innovative form of stimulus, close observers see it as an excuse for the central bank to buy less. When it was introduced the Bank of Japan kept its existing target of buying ¥80trn ($748bn) of government debt a year—but then ignored it. Before the pandemic, it was buying bonds at less than a fifth of that pace.



The Economist

Swapping purchases for pegs might eventually seem attractive to the Fed. It already owns over a fifth of all net government debt, and nearly twice that share of longer-dated bonds (see chart). It might also prevent seeming clashes between monetary and fiscal policy. So far the Treasury has financed America's enormous fiscal stimulus almost entirely through short-term bills. It will probably refinance that borrowing at longer maturities. But doing so puts back into the market the longer-dated assets the Fed is buying up in order to keep yields low. In the 2010s refinancing led to allegations that the Treasury and Fed were "rowing in opposite directions". Were the Fed pegging rates, it would offset the effect of any Treasury debt-maturity operations passively, and avert controversy.

Working out how best to manage bond purchases to boost growth is only a part of the daunting task that confronts the Fed. It will have to consider, as the economy emerges from lockdown, how to withdraw the vast support it has put in place for the private sector, and face losses on some of its loans. But getting monetary policy right is its most important responsibility—not just to lend to "this man and that man", but to ensure that the economy is strong enough for each to prosper. ■

Swapping panic for calm

The successes of the Fed's dollar-swap lines

America's central bank shines in a global role it resents

Jun 20th 2020 | HONG KONG

THE FEDERAL RESERVE steadfastly refuses to view itself as the world's central bank, which is a pity, because it is becoming quite good at the job. One sign of its success is the stabilisation of the world's reserve currency. The dollar spiked by over 8% against a basket of six other widely traded currencies between March 9th and 20th, as covid-19 panicked investors. But now the greenback is roughly back to where it was at the beginning of the year.

Central banks usually concern themselves with their own country's money supply, which is chiefly composed of depositors' claims on the country's banks. But the supply of dollars extends far beyond national boundaries. Last year, banks outside America's jurisdiction had dollar liabilities worth over $10trn, reckon Iñaki Aldasoro and Torsten Ehlers of the Bank for International Settlements (BIS).

To fund themselves, these banks rely heavily on selling short-term dollar liabilities, including certificates of deposit and commercial paper, to investors. The traditional buyers of this paper are "prime" money-market funds (which are a little more adventurous than funds that stick to government bonds and the like). After the pandemic shattered global market confidence, investors began pulling their money out of these funds, and the funds, in turn, stopped buying the banks' paper. That forced the banks to scramble for other sources of funding. Borrowing from each other became dearer (at the height of the panic, banks had to pay a risk premium of about 1.4 percentage points). And it became costlier to obtain dollars through foreign-exchange "swaps", in which one party borrows dollars from another, while simultaneously lending them euros, say, or yen.

As the offshore market is not fenced off from America's own markets, these stresses washed onshore. That gave the Fed an excuse to act. On March 15th it eased the terms of its swap lines with central banks in Britain, Canada, the euro area, Japan and Switzerland. Four days later it extended additional lines to nine others, including the central banks of four so-called "emerging markets" (Brazil, Mexico, Singapore and South Korea).

The Fed has always been uncomfortable making quasi-diplomatic decisions about swap lines. It knows that by picking some countries, it risks sowing doubt about others. Turkey, for example, has long coveted a swap line. India also sought one, according to the *Indian Express*, a newspaper. The swap-envy is telling. It shows that a Fed swap line is not a source of stigma in the way an IMF loan can be. (Indeed, the fund has tried to brand its new, condition-light loans for stronger countries as "swap-like", in the hope of making them more popular.) Brazil, with its comfortable stock of reserves, has not even used its swap line. It values it more for the insurance it provides and the signal it sends, says Alberto Ramos of Goldman Sachs, a bank.

By the end of April ten central banks had drawn over $440bn between them. The biggest take-up was by the Bank of Japan. Its country's banks need dollar funding for their heavy overseas lending. And Japan's pension funds and life insurers also need to hedge their large holdings of dollar assets by, in effect, borrowing dollars, points out Brad Setser of the Council on Foreign Relations, a think-tank.

Favourable dollar funding meant financial institutions did not need to resort to a fire-sale of dollar assets, say Egemen Eren, Andreas Schrimpf and Vladyslav Sushko of the BIS in a recent paper. In the five countries first given swap lines, the cost of borrowing dollars fell sharply. Indeed, some banks in these countries were able to borrow more cheaply (via commercial paper or certificates of deposit) than their American peers, according to the authors. Moreover, banks in these countries sometimes lent their dollars to other banks elsewhere, helping to alleviate the dollar shortage globally. Perhaps, then, the Fed's agonising over whom to favour with a swap line did not matter all that much. As long as it provided enough dollars to central banks somewhere, their banks could funnel any surplus dollars elsewhere.

One of the Fed's innovations was to offer longer-term swaps lasting 84 days. The first of these matured on June 11th, reducing the amount of dollars outstanding by almost $92bn. If the foreign banks that had borrowed these dollars (through the Bank of England's and the European Central Bank's swap lines with the Fed) still needed them, they would have rolled them over. But they did not—suggesting that the swaps had eased much of the stress that motivated them. ■

Clarifying the battle lines

China’s poverty line is not as stingy as commentators think

Nor is China as poor as Li Keqiang implies

Jun 20th 2020 | HONG KONG

SINCE 2017 China’s government has described fighting poverty as one of three “tough” or “critical” battles (alongside quelling pollution and financial risk). Despite the covid-19 pandemic, it still seems confident of victory this year. In March Xi Jinping, the president, pointed out that the number of rural poor fell to 5.51m in 2019. That is only 0.4% of China’s vast population. Regional overall poverty, he said, had been basically eradicated.

The claim seemed wildly at odds with another statistic, cited last month by Li Keqiang, the prime minister. “There are still some 600m people [whose] monthly income is barely 1,000 yuan,” he said at the close of the annual meeting of China’s parliament. Since 1,000 yuan is worth only about $140, the figure seemed both surprising and depressing. Many commentators concluded that China’s victory against poverty was hollow, achieved not by lifting people up but by watering the definition of poverty down.

This scepticism, though, is dogged by two misunderstandings. The first is the conviction that China’s rural-poverty line must be ridiculously stingy, lower than the global standard of $1.90 a day. The second is the belief, inspired by Mr Li’s imprecise remarks, that 600m Chinese live on 1,000 yuan a month or less. Neither claim is true.

About a decade ago China drew its rural poverty line at 2,300 yuan a year, or 6.3 yuan a day. The World Bank’s most commonly used global poverty line is $1.90 a day. Since 6.3 yuan is worth only about $0.90 at today’s exchange rate, it seems natural to think that China’s poverty line is much lower than the World Bank’s.

Natural, but wrong. A fair comparison must first note that China and the World Bank drew their poverty lines with different years in mind. China’s line is based on the prices prevailing in 2010; the World Bank’s, on prices in 2011. China updates its line every year to reflect the inflation faced by the rural poor. In 2011 the threshold was 2,536 yuan, or 6.95 yuan a day.

That is still a meagre amount. But because prices tend to be lower in rural China than in America, 6.95 yuan stretches further than the equivalent amount of dollars would in America. So the yuan should be converted into dollars not at the market exchange rate, but at the purchasing-power-parity rate. That was 3.04 yuan per dollar in 2011, according to Martin Ravallion of Georgetown University, who helped set the World Bank’s line. Thus China’s rural-poverty line is equivalent to about $2.30 a day in 2011 purchasing-power-parity dollars, comfortably above the $1.90 global line. Indeed, the bank’s poverty count for China is lower than the government’s.

What about the second misunderstanding? After the furore caused by Mr Li’s comments, China’s National Bureau of Statistics tried to sort out the confusion this week. It pointed out that the 610m people living in the bottom 40% of China’s households had a monthly income per person of almost 1,000 yuan. In other words, if their combined income were divided equally between them, they would each receive roughly 1,000 yuan (ie, 3,000 yuan for a typical household of three). That is the basis for Mr Li's statement. But it is different from saying that all of these 610m live on 1,000 yuan or less. Imagine a country of ten people, where the bottom four earn \$1, \$2, \$3 and \$4 a day, respectively. Their income per person is \$2.50. But only two of them live on less than this amount. China's leaders often quote official statistics that flatter the economy. But on this occasion, Mr Li's comments unflattered to deceive. ■

Better tailored

The euro area's stimulus is less stingy than in past crises

Even so, more stimulus will be needed this year

Jun 20th 2020 |

THOSE STRUGGLING to break bad habits should take inspiration from the euro zone. During the global financial and sovereign-debt crises it did too little to shore up growth; at times monetary and fiscal policy were tightened precisely when they should have been loosened. By contrast, its response to the covid-19 pandemic has been less flat-footed. Consider the events of the first three weeks of June alone. Germany's government, usually tight-fisted, announced a stimulus package of at least €130bn ($146bn). The European Central Bank (ECB) said it would buy another €600bn in bonds. And as *The Economist* went to press, national leaders were due to discuss setting up an EU-wide "recovery fund" of €750bn, an idea first floated in April.

The question is whether policy can remedy a grave weakness: that countries facing the greatest economic damage are also those with the least fiscal space. Germany's outbreak was relatively less severe, and its lockdowns less stringent. Its new programme takes its total fiscal stimulus this year to 9% of GDP, according to economists at UBS, a bank (see chart). That is bigger than America's. But France, Italy and Spain, which have had worse outbreaks and stricter lockdowns, and risk losing valuable tourism revenues over the summer, also have higher government-debt ratios. Fiscal support has been stingier there.

The good news is that EU policymakers are trying to redress the imbalance. Thanks in part to Germany's newfound generosity, the recovery fund could direct cash to countries according to need rather than what they contribute. A proposal by the European Commission suggests that Italy could receive grants equivalent to about 5% of its GDP, and loans worth another 5%, says Jacob Nell of Morgan Stanley, a bank. Germany and the Netherlands might receive funds worth only 1% of GDP. The bad news is that although many economists expect an agreement to be struck, a few countries—such as the Netherlands and Sweden—are yet to sign up. As a result the fund could well become stingier. Moreover, the cash will only begin to be doled out in 2021, and will be spread over a number of years.

That means that the ECB must do the heavy lifting this year. All told, it is due to buy €1.6trn in public and private-sector debt in 2020, equivalent to 14% of last year's GDP. Like the commission the bank has shifted away from its usual "one-size-fits-all" approach. Instead of buying assets in line with its "capital key" (ie, a country's contribution to the bank's capital, which is in turn proportional to its economic size), it seeks to contain the spread between the bond yields of riskier countries and those on German bunds. Around 22% of the purchases through its pandemic programme and its older quantitative-easing scheme in April and May were of Italian paper, whereas Italy's share of the capital key is 17%, says Sven Jari Stehn of Goldman Sachs, another bank. That means the ECB could indirectly fund all of Italy's deficit this year.

Despite all this, the euro area is probably still short of stimulus in 2020. Though it seems likely to suffer a bigger economic hit than America, its overall fiscal support is smaller. The pace of ECB purchases is more sedate than that of America's Federal Reserve. Few economists think existing stimulus will rouse inflation, which was stubbornly below the ECB's target even before covid-19. Still more bond-buying is therefore probably on the cards. The recovery fund could set a precedent, hopes Mr Nell, allowing for a common fiscal tool to be used in other times of need. Good habits, once formed, tend to stick. ■

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