

The McGraw-Hill Companies

BusinessWeek

JANUARY 22, 2007


www.businessweek.com

REVENGE

The power of retribution, spite, and loathing in the world of business


BY JENA MCGREGOR (P.64)





The **CFO** expects increased stock value.

The **COO** expects improved supply chain efficiency.



The **CMO** expects accelerated market growth.

The **CEO** expects a better bottom line.



The **CIO** has the same expectations and now has the tools to drive business.

Welcome to **Business Service Management** from BMC Software. Business Service Management (BSM) means the goals of IT are the same as the goals of the business. And with proven software and processes from BMC Software, BSM can be implemented in stages, demonstrating the value of IT as you go. All business success stories have to start somewhere. With BSM, they begin in IT.

www.bmc.com/business

 **bmcsoftware**

ACTIVATE BUSINESS WITH THE POWER OF I.T.™

***Is there a parallel uni
is precise? We want to***



STATE STREET.



Before investing, consider the funds' investment objectives, risks, charges and expenses. To obtain a prospectus, which contains this and other important information, call 1.866.787.2257. Read it carefully.

ETFs, such as SPDRsSM, MidCap SPDRsSM and DiamondsSM trade like stocks, are subject to investment risk and will fluctuate in market value. SPDR shares, MidCap SPDRs, and Diamonds are issued by SPDR Trust, MidCap SPDR Trust, and Diamonds Trust respectively. 10051-1007

verse where everyone live there.

We don't like drivers who take up two parking spaces. Weather forecasters who always predict "sunny with a chance of rain." Or repairmen who say they're going to arrive between 8 and 12.

At State Street, we don't like things that aren't precise.

That's why we created SPDRsSM. It's a family of ETFs that includes virtually every market segment. Which means you can precisely match your investments to your investment strategy.

Interested in Technology? Energy? Retail? Now you can buy, hold and sell them just like a stock.

If you love precision as much as we do, visit www.spdretfs.com.

It may not be a parallel universe. But it is a whole other world.



Precise in a world that isn't.SM

The "SPDR" trademark is used under license from The McGraw-Hill Companies, Inc. ("McGraw-Hill"). No financial product offered by State Street Global Advisors, a division of State Street Bank and Trust Company, or its affiliates is sponsored, endorsed, sold or promoted by McGraw-Hill. Dow Jones Industrial AverageSM, The Dow[®] and Diamonds[®] are trademarks of Dow Jones & Company, Inc., licensed for use by State Street Global Markets, LLC. Diamonds are not sponsored, endorsed, sold, or promoted by Dow Jones and Dow Jones makes no representation regarding the advisability of investing in Diamonds. State Street Global Markets, LLC, member NASD, SIPC, is distributor for all SPDR products except for SPDR shares, MidCap SPDRs and Select Sector SPDRs which are distributed by ALPS Distributors, Inc., a registered broker-dealer.

Will my kids inherit the work ethic or the wealth ethic?

Relax. How you raise your kids is none of our business. We won't be checking their report card or their allowance for mowing the lawn. But we can help you pass on your values along with your assets—by understanding what your kids are like and how you want them to grow up.

Perhaps it's time to throw out your notions of what you can talk about with a Financial Advisor. At Smith Barney, we'll roll up our sleeves and help you make a plan for how your kids will begin to share in your wealth. Motivation may not be a gene. But it is something we can work on together.

To talk to a Financial Advisor near you or to receive a free copy of our brochure, call 1.800.Smith Barney or visit smithbarney.com/workingwealth

**Come to Smith Barney.
Where wealth works.™**





**WORKING
WEALTHSM**

AT SMITH BARNEY



© 2007 Citigroup Global Markets Inc. Member SIPC. Smith Barney is a division of Citigroup Global Markets Inc. and its affiliates and is used and registered throughout the world. Citigroup and the Umbrella Device are trademarks and service marks of Citigroup Inc. or its affiliates and are used and registered throughout the world. Working Wealth and Come to Smith Barney. Where Wealth Works are service marks of Citigroup Global Markets Inc.

citigroup
SMITHBARNEY



**What do you call a year in which you sell 63 million
Earth-friendly products? A healthy start.**

The Home Depot® is committed to home improvement, including the home we call Earth. We started this initiative in 1990 and brought our vendor partners aboard. Together, we offer customers a wide range of eco-savvy options. Last year, sales of ENERGY STAR® qualified products increased by 25%. And the energy saved by the compact fluorescent lightbulbs we've sold could light the homes in Washington, D.C., for three and a half years. All of which lets us know that we're on the right path. For our people. For our communities. For our planet.



The Business Week

34 News You Need to Know

Cheaper oil; the health governor; Gap up for grabs; patent wars; and more

News & Insights

39 A Bigger Voice for Small Investors

How mutual fund managers are increasingly asserting themselves

40 Apple's Very Smart Phone

Why Steve Jobs's latest gadget should scare the daylights out of phone makers

42 The Techie's Lexicon

What they were talking about at the Consumer Electronics Show

44 Smoke and Mirrors for Home Buyers

Realtors are pulling homes off the market and relisting them as "new"

46 B-School Dreams

Once it was Wall Street, then it was the Net. Now it's a job in private equity

51 All Donald, All the Time

The nonstop media event called Trump

Global Business

52 BP Feels the Heat

2006 was an *annus horribilis* for the oil giant, and the problems aren't over. Will CEO John Browne leave early?

54 Even Toyota Isn't Perfect

A raft of recalls has it scrambling to safeguard its reputation for quality

56 Taking Outsourcing to the Outskirts

Tech-services jobs are transforming villagers' lives in rural India

MORE GLOBAL COVERAGE:

For additional insights into European and Asian business, please go to www.businessweek.com/globalbiz

Economics

31 Business Outlook

Jim Cooper says the strong job market shows the economy is poised for a lift—and that's dashing hopes for rate cuts



Cover Story

64 Sweet Revenge In the numbers-driven world of business, it's easy to forget that the desire to get even is a primal human impulse. The importance of retribution, spite, loathing, and vindication

70 Grudges in the Cubicle A management guru answers questions about how to prevent destructive score-settling



NEWS & INSIGHTS

36 Board of Hard Knocks

Serving on a corporate board used to be a breeze. But activist shareholders, tougher rules, and mounting anger over supersized CEO pay have turned directorships into risky business. And as lawsuits fly, it's not just directors' positions on the line—it's their personal assets

COVER PHOTOGRAPH BY NICHOLAS EVELEIGH, DOLL BY MEGAN CAPONETTO

BusinessWeek (ISSN 0007-7135) Issue number 4018, published weekly, except for one week in January, July and August, by The McGraw-Hill Companies, Inc. Executive, Editorial, Circulation, and Advertising Offices: 1221 Avenue of the Americas, New York, N.Y. 10020. Periodicals postage paid at New York, N.Y. and at additional mailing offices. Canada Post Publication Mail Agreement Number 40012501. Return undeliverable Canadian addresses to: DPGMLtd., 2-7496 Bath Road, Mississauga, ON L4T 1L2. Email: bwkcustserv@cdsfulfillment.com
Postmaster: Send address changes to BusinessWeek, P.O. Box 8418, Red Oak, IA. 51591-1418

CONTENTS



Special Report

58 How BGI Outsmarts the Market

BusinessWeek takes you deep inside Barclays Global Investors, a “quant” shop with incredible brainpower. Its quest: to systematically do the impossible

Government

72 Lobbyists Who Want Nothing

Why Big Sugar’s reps are rejecting a government subsidy

The Corporation

73 Homeland Security 2.0

Five years after September 11, a new wave of smarter high-tech anti-terror tools is coming to market

InfoTech

75 Small Fry Sour on Search Ads

Now, the outfits that pioneered the medium are getting priced out

Finance

76 Private Equity Repellent

Companies are loading up on debt to make their balance sheets less enticing to voracious private equity firms

Environment

78 Who Will Run the Reactors?

The nuclear industry is starting to expand again, amid concerns about fossil fuels. The problem: A graying workforce

Marketing

80 Changing the Game on Nike

How budget sneakers are tripping up the company’s basketball business

Executive Life

82 The King of His Digital Castle

Net guru John Patrick has built the ultimate automated house. Dim the lights, turn on the music—even from half a world away

Personal Finance

86 Mutual Funds Scoreboard

BusinessWeek’s data mine finds tried-and-true funds that deliver rich returns with relatively low risk and minimal expense

92 Inside Wall Street

Gene Marcial’s stocks to watch

93 Figures of the Week

Columnists

26 Steve Wildstrom: Tech & You

Microsoft’s Windows Vista has irksome, but important, security features

28 Jon Fine: MediaCentric

Sling Media shows TV—nicely—how to weave in the Web and survive click culture

84 Mike Marrone: My Tunes

The Pernice Brothers’ instant pop classic

85 Robert Parker: On Wine

Plush, opulent pinot noirs from California’s Santa Rita Hills

98 Jack and Suzy Welch: The Welch Way

The columns that roiled readers in 2006

Ideas

95 Books

Klaidman: *Coronary: A True Story of Medicine Gone Awry*

96 Outside Shot: Stephen Slivinski

Why earmarking the “earmarks” won’t end pork-barrel waste in Washington

Features

13 UpFront

22 Readers Report

23 Corrections & Clarifications

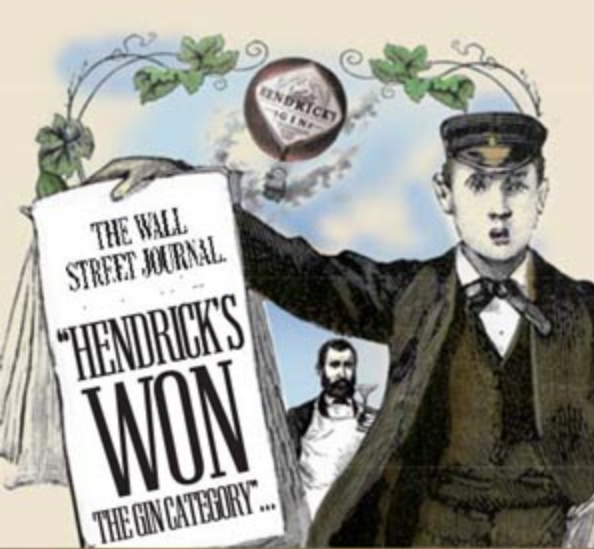
94 Index to Companies

WHO'S HELPING
THE NEW SUPERDOME
SCORE
HIGH-TECH POINTS WITH
SPORTS FANS? NORTEL.

Planning the rebirth of the Superdome was a team effort. With help from Nortel, the planners envisioned and created a wireless interactive multimedia experience that connects fans like never before. All while reducing operating costs. The new world-class stadium is once again a huge win for New Orleans and sports fans. nortel.com

NORTEL

Business made simple



THE WALL STREET JOURNAL

When it came to our tasting of "white goods," the superpremiums ruled the day. Here, our top three in each category, plus our tasters' comments:

LIQUOR BRAND/PRICE* OUR AWARD

TOP 3 GINS

Hendrick's Most Flavorful
\$30/750ml

Tanqueray No. Ten Smoothest
\$26/750ml

Juniper Green Organic Best Presentation
\$26.50/750ml



©2006 IMPORTED BY WILLIAM GRANT & SONS INC., NEW YORK, NY 10118. 44% ALC. BY VOL. (88 PROOF). DRINK THE UNUSUAL RESPONSIBLY.

HENDRICK'S®
A MOST UNUSUAL GIN

HENDRICKSGIN.COM

What's Hot This Week At BusinessWeek.com

Updated every business day, *BusinessWeek* magazine is available online free to subscribers: Go to www.businessweek.com to register. Find links to the online-only highlights below at www.businessweek.com/magazine/content/07_04/online.htm.



Anointing the iPhone

The much anticipated unveiling of Apple's new **music-playing iPhone** on Jan. 9 was greeted with fanfare by the Apple faithful and was welcomed by investors, who sent the company's shares soaring (page 40). But elsewhere in techdom they weren't cheering: BlackBerry parent Research In Motion and other makers of mobile devices became instant Apple rivals. In a BusinessWeek.com special report, **The Apple Economy**, we explore why the innovative iPhone is likely to rankle RIM and much of the rest of the wireless industry. Our slide show makes clear what's so unique (for now, anyway) about the phone and **Apple TV**, a new device for moving content from PCs to TVs. We also look at how Apple's success is influencing the way companies in a variety of industries now work to design their own innovative products. And lest you think that Apple is emphasizing consumer electronics at the expense of its computer business, we explain why corporations that long shunned Macs for machines that run Microsoft Windows are giving Apple's products a second look. Go to www.businessweek.com/go/07/apple for all this and more.

BusinessWeek weekend

Grab Your TV Clicker This Weekend for:
Consumer Electronics Show | Car Shopping



Check your local TV listings for program dates and times. For video clips go to www.businessweekweekend.com.

ERIC SLOMANSON/BLOOMBERG NEWS



Reliability and Style.

They only come together on one Network.

- Email
- Windows Mobile®
- Multimedia capabilities



Limited time offer **\$99⁹⁹**

\$299.99 2-yr. price—\$100 instant rebate and \$100 mail-in rebate=\$99.99.

Offer valid with new voice plan of \$39.99 monthly access or higher and a data feature of \$44.99 monthly access, or any new Voice and Data Choice Bundle™ plan starting at \$79.99 monthly access, with a new two-year activation.



Only Verizon Wireless has the Q that runs on America's most reliable wireless broadband network.

Get the **motorola Q™** from Verizon Wireless at verizonwireless.com/Q or 1.800.VZW.4 BIZ (899.4249)

Activation fee/line: \$35.

IMPORTANT CONSUMER INFORMATION: Subject to Customer Agmt, Calling Plan & credit approval. Up to \$175 early termination fee & other charges. Offers not available everywhere. While supplies last. Shipping charges may apply. Limited time offer. The wireless broadband network is available in 208 major metropolitan areas. Coverage limitations, maps & details at verizonwireless.com. Email: Additional charges apply. America's most reliable wireless network claim based on fewest aggregate blocked and dropped connections. See verizonwireless.com/bestnetwork for details.

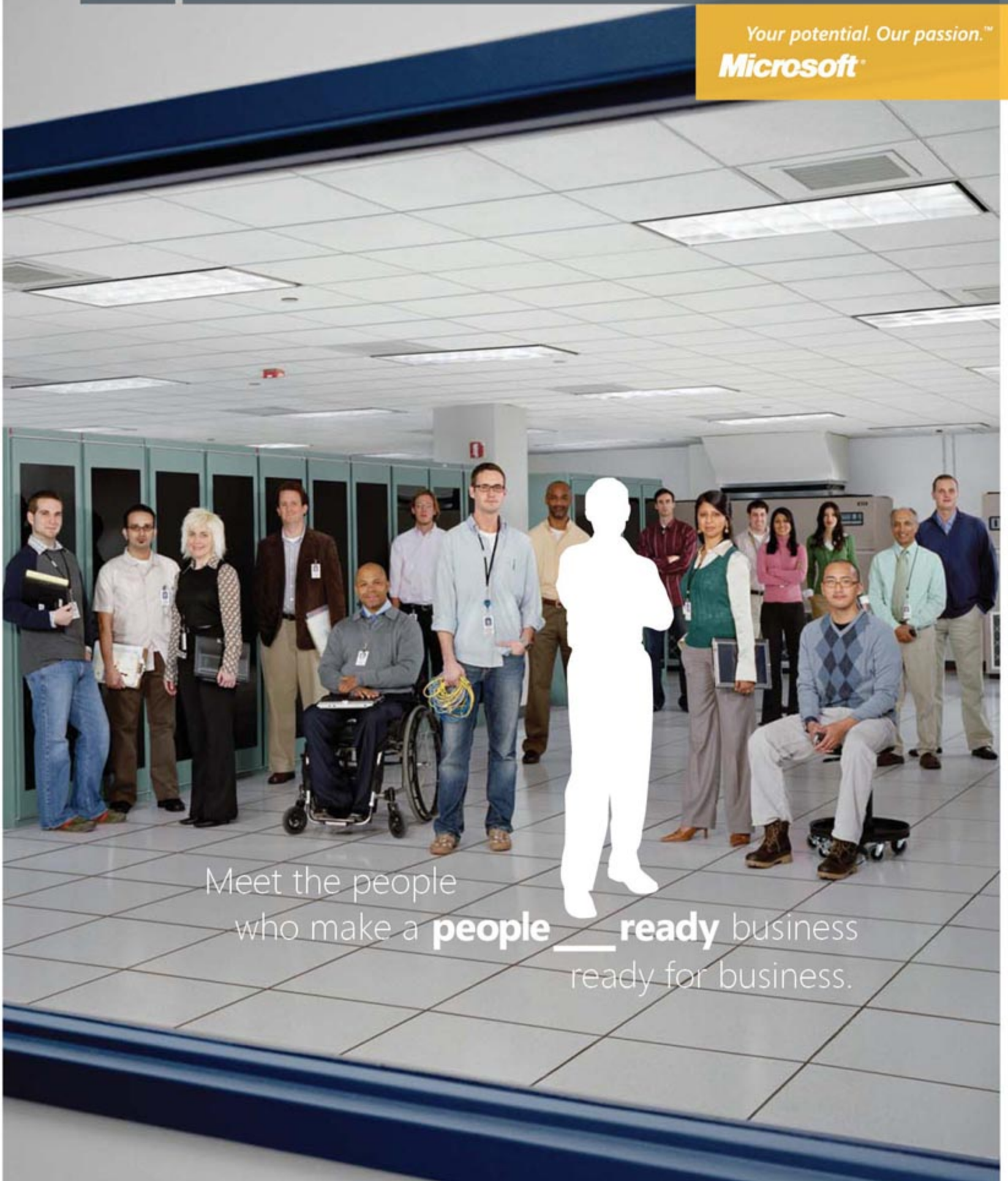


A people-ready business runs on Microsoft software.

How to free IT to be the killer advantage it was meant to be? Give your people software that automates routine IT tasks: networking, data recovery, and device, server, and security management. Software like Microsoft® Windows Server® 2003 R2, the Microsoft Forefront™ line of security products for business, and the System Center family of IT management solutions. You'll give IT people time to think big. And they'll use it to put you on the cutting edge. Microsoft. Software for the people-ready business.™ microsoft.com/peopleready

Your potential. Our passion.™

Microsoft®



Meet the people
who make a **people** **ready** business
ready for business.

UP Front

“There’s plenty of winter still left.”

—Jeremy Batstone, head of research at Charles Stanley, on speculation that unseasonably warm weather in the U.S. Northeast has helped send oil prices tumbling, as reported by Reuters

EDITED BY DEBORAH STEAD

STREET NEWS A BIG BOARD DEAL WITH SPLINTERS

WHEN THE NASD, which regulates **NASDAQ**, and **NYSE Regulation**, its **New York Stock Exchange** counterpart, announced a merger on Nov. 28 after years of fruitless

talks, the deal was expected to sail through. Instead, the plan to create a single oversight body for brokers and dealers—

meant to eliminate costly redundancies and to align rules—has hit a snag. As a Jan. 19 vote on the merger nears, a group of small NASD members is campaigning hard to stop the union.

Financial Industry Assn. co-founder John Busacca is rallying his small-brokerage members to vote against the consolidation, saying that the new regulatory entity

would marginalize small and midsize brokers by eliminating the one-member, one-vote rule that now regulates elections to the NASD board of governors.

The NASD is taking Busacca & Co. seriously. In a Jan. 8 e-mail it urged members not to sign over their proxies to Busacca, and it has been buying banner ads in Web publications

to promote the benefits of having a single oversight body. It has also enlisted industry leaders like

the **Financial Services Institute**, a trade group of independent broker-dealers, to rally support for the merger. Busacca, who holds several hundred proxies in addition to an unknown number of nay votes already cast by his allies, says the outcome is too close to call. The NASD, which is tracking the voting, won't say who's ahead.

—Lorraine Woellert



VERBATIM

Shareholder activist Carl Icahn, interviewed in the January issue of *Avenue*, a magazine covering New York's social Establishment:

“I have my anti-Darwinian metaphor: The CEO is the fraternity brother type who is great to have a drink with. He’s a survivor and maybe not all that smart, but he works his way up the ladder in the corporation. And if you’re a survivor you never have someone beneath you who’s smarter than you. So you eventually work your way to CEO. You have someone a little dumber than you underneath, and eventually we’ll have morons running everything...which we’re getting closer to.”



BOOM AND BUST

About That Short Housing Slump...

HAS HOUSING hit bottom? Not if history is any guide, says Hugh Moore, a partner at **Guerite Advisors**, a money manager in Greenville, S.C. Using data from the seven previous housing cycles since 1959, Moore concludes that the sector will fall further—and land hard. Take housing starts. In the past, they fell an average 51% from peak to trough. So the current downturn, with housing starts off about 30% from the January, 2006, peak has further to go. And it may meet recession on the way. That’s because in six of the seven cycles, when starts fell more than 25% from their most recent peaks, the economy tanked.

Another gloomy stat: In the same seven cycles, the amount people spent on new housing as a percent of gross domestic product fell an average 28% from market peak to trough. Worse, in six cycles, recession kicked in when the ratio fell more than 10% from its most recent peak. In this slump, Moore says, that ratio has fallen 10.5% from its fourth-quarter peak.

History also shows housing corrections take an average 27 months. Thus, the current doldrums may linger a year or more. “It’s just going to be this slow, grinding drain on the economy,” says Moore, who adds that month-to-month housing stats producing relief rallies are “just noise.” —Mara Der Hovanesian

ON BOARD



BILLY BEANE

NETSUITE BUILDS UP ITS BENCH

Will Billy Beane, the do-more-with-less general manager of the Oakland Athletics, lend NetSuite some of the magic he brings to his baseball team?

On Jan. 4, Beane became a director of the San Mateo (Calif.) company, which makes Internet-delivered business software. Naming an outside director signals the intention of nine-year-old NetSuite to go public this year. In 2006, it grew 60%, with \$70 million in revenues, 7,000 customers, and a positive cash flow. Still, it has yet to edge out crosstown rival [Salesforce.com](#), which, with 27,000 customers, is the "damn Yankees" of the Internet software industry.

Beane's connection to NetSuite is with CEO Zach Nelson, whom he met a decade ago when McAfee Associates, Nelson's former employer, bought naming rights to the A's stadium. Nelson is "a little nervous" about having on his board a shake-'em-up GM like Beane, who was profiled in Michael Lewis' *Moneyball*. "But it will be a great experience to have somebody like that pushing me," he says. —Steve Hamm

GREEN BIZ

WAL-MART: LET THE SUN SHINE IN?

WAL-MART is falling for the sun. The retail behemoth last month put out a request for proposals to install solar panels at stores and distribution centers in five states, according to people who have seen the RFP. The project could take into account as many as 300 buildings and produce 150 megawatts of power, making the Wal-Mart installation the largest in the world, according to a solar industry executive who is one of the bidders.

Wal-Mart has confirmed it made the call for bids, but it won't comment on the details. The company is exploring solar energy as

a component of CEO Lee Scott's goal, announced a year ago, of eventually converting Wal-Mart's operations to 100% renewable energy. Among other things, the RFP asks vendors to outline how Wal-Mart could own its solar energy systems, lease them, or simply buy power from Wal-Mart roof panels owned by the solar company.

The company plans to notify the winner at the

end of February. Once it graduates from the exploratory phase and sees the capital costs involved, it might wind up balking at the ambitious project. But given Wal-Mart's sheer size, says the solar industry executive, installing panels on just 40% of company buildings would still dwarf other corporate solar installation efforts, including the biggest in the U.S.: Google's 1.6 megawatt project. —Heather Green



PATENT PENDING NAME THAT NOISE

FROM AN APPLICATION to trademark a sound for use in slot machines, received by the U.S. Patent & Trademark Office in mid-December:

...a yell consisting of a series of approximately ten sounds, alternating between the chest and falsetto registers of the voice, as follows - 1) a semi-long sound in the chest register, 2) a short sound up an interval of one octave plus a fifth from the preceding sound, 3) a short sound down a Major 3rd from the preceding sound, 4) a short sound up a Major 3rd from the preceding sound, 5) a long sound down one octave plus a Major 3rd from the preceding sound, 6) a short sound up one octave from the preceding sound, 7) a short sound up a Major 3rd from the preceding sound, 8) a short sound down a Major 3rd from the preceding sound, 9) a short sound up a Major 3rd from the preceding sound, 10) a long sound down an octave plus a fifth from the preceding sound.

Filed by Fross Zelnick Lehrman & Zissu of New York, named by the Patent Office on Jan. 10 as the most prolific filer of trademark applications among all U.S. law firms. That was cause for a little chest-thumping at the firm. Still can't guess the sound sequence being described? See below.



(CLOCKWISE FROM TOP) CHRISTOPH HITZ; PHOTO-ILLUSTRATION BY JOE CALVIELLO; JED JACOBSONH/GETTY IMAGES

The Tarzan yell, already owned as a registered trademark by Fross Zelnick client Edgar Rice Burroughs Inc., for use in a Tarzan doll.



Home, sweet hybrid home.

If cars are being built to be more energy efficient, why shouldn't homes? At BASF, we've put our energies into building an affordable house in Paterson, New Jersey, to demonstrate how truly energy efficient a home can be. Our Near-Zero Energy Home utilizes BASF's high-performance products in insulating foam sealants, panels and concrete forms, and is 80% more energy efficient than the average American home. Who says a hybrid should only come on wheels? Learn more at basf.com/stories

Helping Make
Products Better™

 **BASF**
The Chemical Company

PUBLISHER'S ROW

THE WRITE STUFF ON A TOUGH BOSS?

BECAUSE SHE CAN, a novel written by a former ReganBooks editor, rode a prerelease wave of publicity back in December when renegade **Harper-Collins** publisher Judith Regan was fired. Now **Warner Books** is pushing up the publication date by a week, to Feb. 5, apparently to capitalize on the buzz surrounding Regan's downfall, legal battles, and putative comeback following her foiled plan to publish O.J. Simpson's *If I Did It*.

First-time novelist Bridie Clark worked for Regan for about a year in 2004. At the center of her book is one

Claire Truman, a young book publishing hopeful with a "notorious tyrant" of a boss, Vivian Grant. Industry insiders have pegged Regan as the inspiration for the ego-driven character with a taste for glamorous (and sometimes unsavory) authors. Warner says it pushed up the pub date to exploit "media interest" in



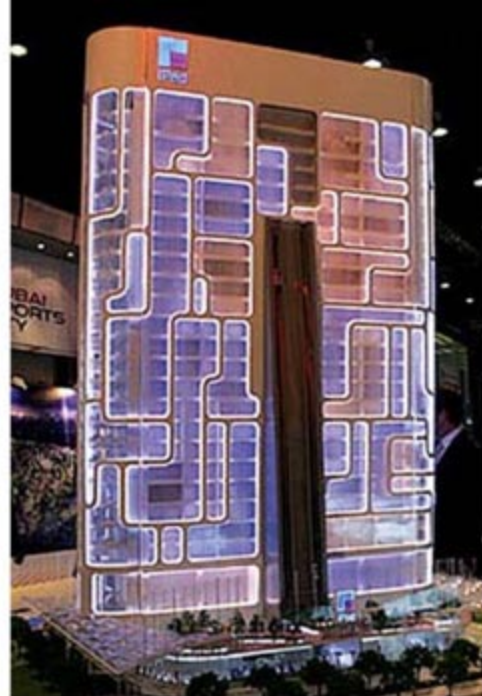
the book, not the Regan connection. "It's not about Judith per se," says Karen Kosztołnyk, the book's editor. "It's about anyone who's ever had an overly demanding boss." Reviewers (and Warner

publicists) compare the book to the 2003 best-seller and 2006 film *The Devil Wears Prada*. Does *Because* have the same franchise potential? Kosztołnyk says movie rights are still being shopped around. —Elizabeth Woyke

ARCHI-TECH

COME 2009, Dubai may be drawing iPod aficionados from across the globe. That is the expected completion

date for the iPad, a 23-story, \$800 million apartment building shaped like an iPod and tilted an iPod-like six degrees for anchoring in a "docking station" (the building's base). The building, developed by Omniyat Properties in Dubai and designed by Hong Kong architectural firm James Law Cyberecture International, will have a futuristic glowing facade and apartments with high-tech devices built in, says firm Chairman James Law (who won't yet reveal those features). It won't be "just a piece of architecture," Law says, "but an integrated piece of technology and architecture." —Nichola Saminather



TRENDSPOTTING HELLO, GOODBYE

» **MANAGEMENT** turnover was way up in 2006. Exec-level churn—from directors down to VPs—rose 68% in 2006, to 28,058 changes. CEOs came and went at a 30% higher rate. CFO churn rose 23%. The drug/biotech industry saw the most CEO and CFO turnover. In biotech, these posts are often filled first by people able to handle "the initial development of the company," says Richard Jacovitz, a senior vice-president at **Liberum Research**, which did the study using SEC filings and press releases of North American publicly traded companies. But as biotech firms enter the marketing phase, he says, many "need a different sort of talent." —Lindsay Gerdes



"THAT WAS THE BOARD OF DIRECTORS FIRING ME FOR SCREWING UP THE COMPANY—THEN THEY HAVE TO HUMILIATE ME WITH A \$100 MILLION SEVERANCE PACKAGE."

(TOP RIGHT) COURTESY OF IMRE; CARTOON BY PAT BAGLEY/SALT LAKE TRIBUNE/CAGLE CARTOONS.COM

WORK
in
Color



IT'S NOT EXPENSIVE TO LOOK EXPENSIVE. HP COLOR LASERJETS STARTING AT \$399.

It makes more sense than ever to get an HP Color LaserJet printer. These come network-ready and have renowned print quality when you use HP ColorSphere toner. And best of all, they're all from HP. *PC Magazine's* Readers' Choice for Service and Reliability for 14 straight years. Brilliantly Simple.



FAST

HP Color LaserJet 2600n.
Up to 8 pages a minute.
More affordable than ever.

\$399.

FASTER

HP Color LaserJet 3600n.
Up to 17 pages a minute.
A great fit for a growing business.

\$699.

FASTEST

HP Color LaserJet 3800n.
Up to 22 pages a minute.
There's no deadline it can't meet.

\$999.

To learn more or see special offers, visit hp.com/go/colorprinter.
Call 1-800-888-3119. Visit your reseller or retailer.

©2006 Hewlett-Packard Development Company, L.P. Estimated U.S. retail price. Actual price may vary.



DEALING WITH A CHALLENGING VALUATION ANALYSIS? GET THE POWER OF DUFF & PHELPS.

From purchase price allocation and real estate appraisal to business and tax valuation, Duff & Phelps provides trusted analysis and insight on critical issues. With more than 700 professionals working together across North America, Europe and Asia, we have the depth and breadth of industry and technical expertise to meet your needs. Get the strength of one of the world's leading independent financial advisory firms.

- > Financial Reporting Valuation
- > Tax Valuation & Consulting
- > Real Estate & Fixed Asset Services
- > Investment Banking
- > Transaction Advisory Services
- > Financial Restructurings
- > Dispute Consulting & Forensic Advisory Services

DUFF & PHELPS

duffandphelps.com / +1-866-282-8258

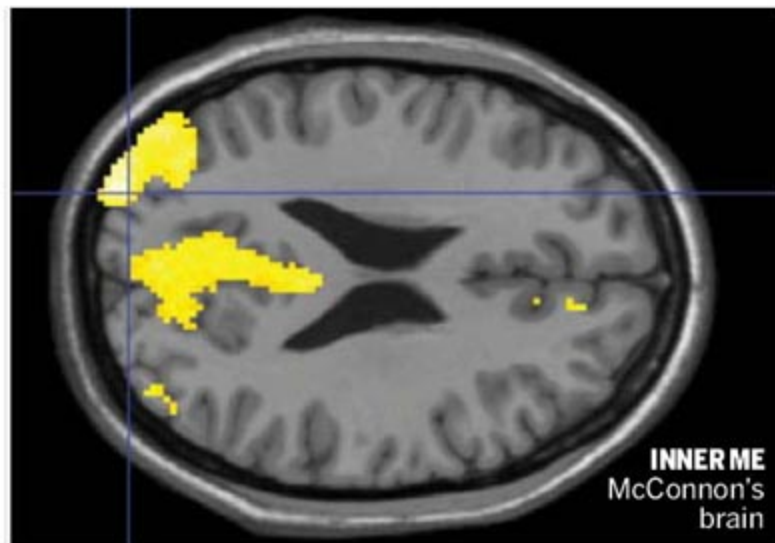
Investment banking services are provided by Duff & Phelps Securities, LLC, an NASD registered broker-dealer.

MAD AVE

IF I ONLY HAD A BRAIN SCAN

IT MIGHT SOON BE time to redefine MRI machines as “market research imaging” devices. At Harvard’s McLean Hospital not long ago, six male whiskey drinkers, ages 25 to 34, lined up to have their brains scanned for Arnold Worldwide. The Boston-based ad shop was using functional magnetic resonance imaging (fMRI) to gauge the emotional power of various images, including college kids drinking cocktails on spring break, twentysomethings with flasks around a campfire, and older guys at a swanky bar. The scans “help give us empirical evidence of the emotion of decision-making,” says Baysie Wightman, head of Arnold’s new, science-focused Human Nature Dept. The results will help shape the 2007 ad campaign for client Brown-Forman, which owns Jack Daniels.

The idea of peeking into



the brain for consumer insights isn’t new. More than a dozen universities have been using fMRI to study how people respond to products (prompting Ralph Nader’s Commercial Alert group to assert that “it’s wrong to use a medical technology for marketing, not healing”). But now a few agencies like Arnold—whose clients also include McDonald’s and Fidelity—and Digitas, another Boston-based shop, are offering fMRI research. “Neuromarketing” consultants, like Los Angeles-based FKF Applied Research, are springing up, too, to link

companies with hospitals seeking to lease time on their pricey MRI machines.

ADVERTISERS look to the scans to help tweak their messages. “If you’re going to spend \$50 million on an ad campaign, wouldn’t you want to know if the ad even gets out of the starting gate?” asks Joshua Freedman, M.D., who co-founded FKF. Because scans for 10 to 20 subjects can cost \$50,000 to \$100,000 (vs. \$4,000 for a focus group), FKF arranges fMRI time shares, allowing clients to show 10 subjects a 30-second ad for \$3,000, for instance.

Even that’s too much for skeptics. “Just knowing the area of the brain where something fires doesn’t tell you anything about why it fires,” says Eric Du Plessis, author of *The Advertised Mind*. But Wightman argues that consumers often can’t articulate what they like best. At McLean, she notes, the spring-break images sparked the most brain activity, even though the camping scenes were the spoken favorite. (Similarly, high-fat-food images fired up the brain of this reporter, despite her stated preference for photos of healthy snacks.) Since the McLean fMRIs were Arnold’s first, the agency itself paid for them. (Brown-Forman says it might fund a future round.) Wightman concedes that responding to an ad while in an MRI device differs from shopping in a store. That’s why she’s also considering doing research with a sensor-equipped shirt, originally developed for medical tests, that records rises in sweating or heartbeat as the wearer responds to a product.

—Aili McConnon

QUESTION OF THE WEEK

Toyota is poised to become the world’s No. 1 carmaker. Should the U.S. do more to support Detroit’s Big Three? If so, how?

—David Kiley

“If the goal is to create jobs, why should Washington prioritize Americans working for Ford in Kentucky over Toyota’s Americans in Kentucky? Are those who work for Toyota less American than those working for Ford or GM?”

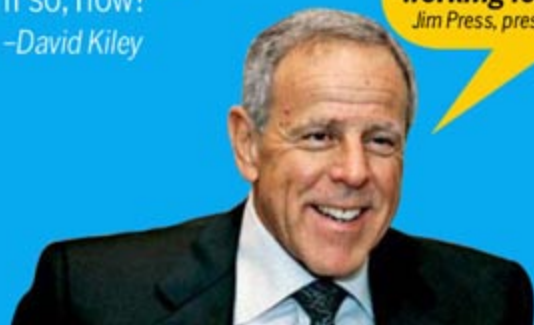
Jim Press, president, Toyota Motor NA

“I wouldn’t base my plans on expecting change. But if I had a wish, it would be for the government to pass health-care policy that would place far less of the burden on companies.”

Dieter Zetsche, chairman, DaimlerChrysler

“Health-care reform. But, politically, that’s like trying to boil the ocean. So I’d like Washington to invest much more to help with our plans to make more fuel-efficient vehicles.”

Mark Fields, president of the Americas, Ford Motor



(BOTTOM, LEFT TO RIGHT) DAMIAN DOVARGANES/AP PHOTO; SEAN GALLUP/GETTY IMAGES; CARLOS OSORIO/AP PHOTO

The most fuel-efficient auto



Environmentology
Honda thinking in action.

Meet Small Oil. Honda has always been committed to developing environmentally responsible technology. And with cars like the all-new Fit along with the legendary Civic, Honda will continue as the leader in fuel efficiency.* Through innovation and hard work, Small Oil can make a world of difference. That's our Environmentology.™

*Based on model year 2005 CAFE average fuel-economy ratings and weighted sales for passenger-car and light-truck fleets sold in the U.S. by major manufacturers.
†Civic Hybrid and Fit Sport with SMT shown. 2007 EPA mileage estimates: 49 city/51 highway; 33 city/38 highway, respectively. Use for comparison purposes only. Actual mileage may vary. ©2006 American Honda Motor Co., Inc. environmentology.honda.com

company in America.*



HONDA
The Power of Dreams

ReadersReport

“It is a statistical fact that 70% to 80% of money managers often fail to beat the [S&P 500] index’s market returns.”

—Srinivas Balla
Arlington, Va.



approach of the current U.S. model is tantamount to an ill-tempered parent smacking a baby. With communication ineptitude like this, Paulson did not deserve the hearing he got from the Chinese.

—Marcus Breen
Associate Professor, Communications
Northeastern University
Boston

HANK PAULSON HAS NO BUSINESS LECTURING THE CHINESE

“HANK PAULSON on China and the year ahead” (Face Time, Dec. 25/Jan. 1) provides further evidence of why the current Administration is consistently underperforming in its policymaking. For starters, [Treasury Secretary] Paulson is a nonpolicy specialist whose expertise is in making vast amounts of money, not in thinking through and creatively suggesting solutions to the financial challenges this Administration has wantonly produced.

More pressingly, Paulson is inept

as a communicator. His near-perverse suggestion that China should “speed up the pace of reforms because...they’re somewhere between a market-driven economy and [a managed economy]... and that’ll get them nowhere” is a logical fallacy. Last time I checked, the Chinese had a gross domestic product that is up 10%, industrial production that is up 14%, a trade balance of more than \$163 billion for the past year, a current-account upside of \$160 billion, and foreign reserves above \$987 billion.

The audacity of telling Chinese officials to drop their mixed, even quasi-managed economy for the free-market

ONCE MORE WITH FEELING: STEER CLEAR OF STOCKPICKERS

“WHERE TO INVEST 2007” (Cover Story, Dec. 25/Jan. 1) promised to help “plan a winning strategy for the new year, whatever your investment needs.” Fascinating, I must say. But what ever happened to the good old academic mantra of investing on the Standard & Poor’s 500-stock index and not having to worry about selecting specific stocks? It is a statistical fact that 70% to 80% of money managers often fail to beat the index’s market returns. Do you consider yourself within the other 20%?

—Srinivas Balla
Arlington, Va.

Importing



ARMs AND FORECLOSURE: OPTION ONE BEGS TO DIFFER

"THE 'FORECLOSURE FACTORIES' vise" (News & Insights, Dec. 25/Jan. 1) was wrong to mention a mortgage foreclosure recently experienced by borrowers who had a loan with our company. There's absolutely no association between the borrowers' situation and the story's premise that mortgage services are using predatory tactics to harm consumers.

The article grossly misrepresents, solely as late charges and attorney fees, an amount it states was owed on the loan. The fact is, the actual amount owed would have consisted almost entirely of past-due principal and interest and amounts advanced on the borrowers' behalf for real estate taxes and insurance. The borrowers also received and signed disclosures from their broker as well as additional plain-language disclosures from Option One Mortgage indicating that they understood how an adjustable-rate mortgage works, contrary to what the article contends.

No one wins when a borrower loses a home. As a top-rated servicer, Option One did all the right things to help the borrowers get back on track toward curing

their loan default and repaying their debt.

While the reasons for foreclosures, such as bankruptcy, job loss, and divorce, remain outside the control of the servicer, there are remedies. At Option One we will continue to focus on keeping people in their homes through early intervention, workout plans, and a compassionate, humane approach.

—Teji Singh
Chief Servicing Officer
Option One Mortgage Corp.
Irvine, Calif.

CORRECTIONS & CLARIFICATIONS

"Is Steve Jobs untouchable?" (News & Insights, Jan. 15) incorrectly said that Apple Inc. co-founder Steven P. Jobs is chairman of Apple's board. He is CEO and a board member but not chairman. At the time of the options backdating that Apple disclosed on Dec. 29 in its annual report, Apple did not have a chairman. But Apple's bylaws at the time stipulated that Jobs, in his capacity as CEO, preside over board meetings.

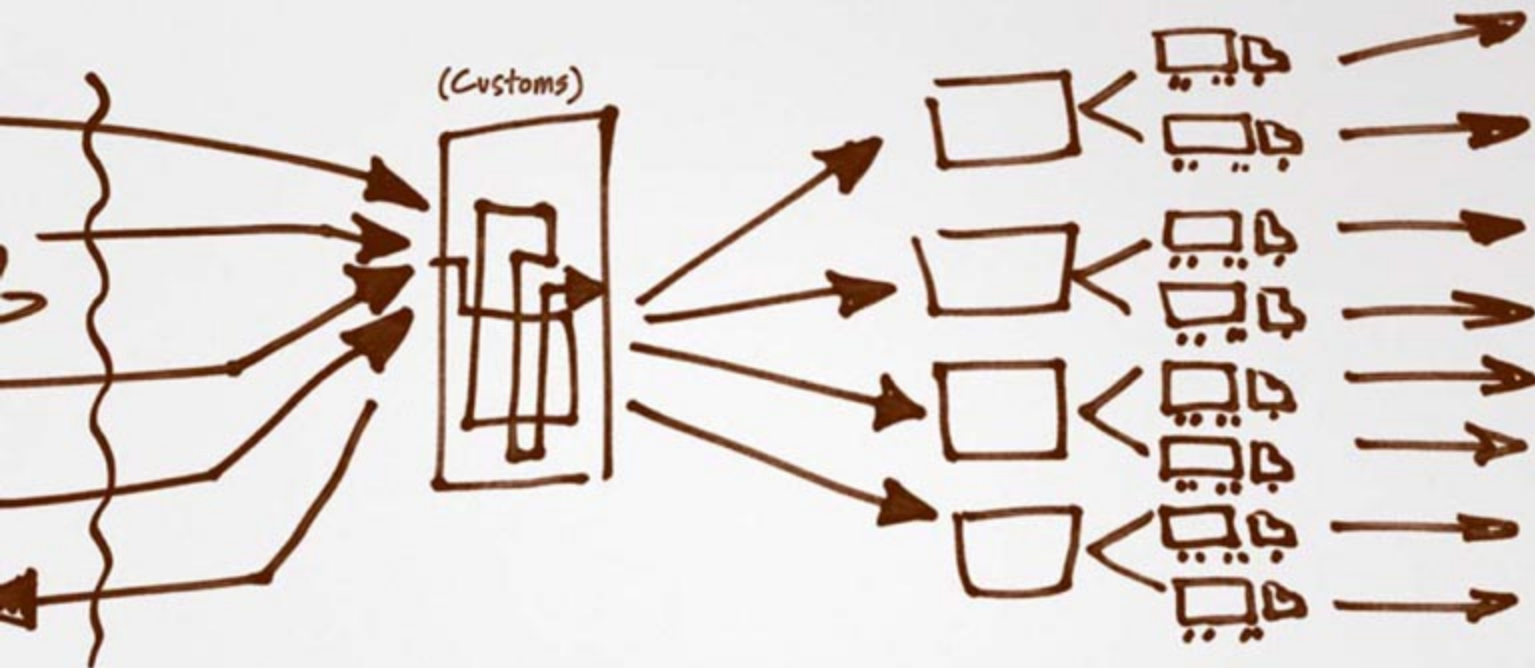
"Bankruptcy becomes Delphi" (News & Insights, Jan. 15) should have noted

that Highland Capital Management's offer to buy Delphi Corp. out of bankruptcy includes a provision that all current shareholders can maintain their stakes in the reorganized company.

"China: Falling hard for Web 2.0" (Info Tech, Jan. 15) misstated the name of the venture capital firm backing Internet company Qihoo. The correct name is Highland Capital Partners (unrelated to Highland Capital Management mentioned above).

ALLERGAN'S MARKETING BLITZ WON'T SWAY SMART WOMEN

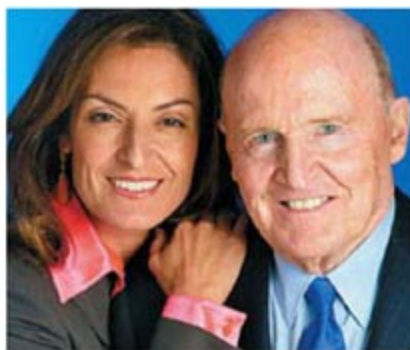
YOUR ARTICLE IS TITLED "Silicone goes subtle" (News & Insights, Dec. 25/Jan. 1), yet Allergan's marketing as outlined within is anything but. It includes Web sites with links to positive studies and an "ask the nurse" feature, a public relations "blitz" (your word, not mine) targeting editors of women's magazines, and a print campaign. The company is also poaching employees from Nestlé and Procter & Gamble as if selling sili-



ReadersReport

“Choosing a model of corporate governance is now every board’s challenge.”

—Alan Towers
New York



Up Front, Dec. 25/Jan.1). I suppose, by the implied standard, uncovering fraud against shareholders is simply sour grapes from those who weren’t quick enough to have already cheated.

It would be helpful to investors and others if *BusinessWeek* published an annual list of “Liars, Cheaters, and Thieves.” After all, anyone willing to cheat the federal government is certainly waiting for an opportunity to cheat shareholders, business partners, and the general public.

The list could serve as a warning. Prosecution has proved insufficient to deter fraudulent behavior, but perhaps being shunned by investors and others might work.

—Patrick Durusau
Covington, Ga.

cone breast implants were as innocuous as hawking candy and toothpaste.

Citing new studies that support the Food & Drug Administration’s lifting of the 14-year moratorium, Allergan is attempting to push its product on well-educated women with the tagline “You’ve never looked smarter.” But is it smart to believe only the results of the latest studies? Intelligent people know that all studies are suspect and that you can find one to support whatever theory you want to promote. And do women need bigger boobs to feel smart, to themselves and others?

Intelligent people know there is

no correlation between gray matter and externals. And finally, women’s experience with being experimented on by the medical Establishment makes it unlikely that they will be suckered again. Can you say “hormone replacement”?

—Karen Ann DeLuca
Alexandria, Va.

LET’S NAME THE LIARS, CHEATERS, AND THIEVES

IT’S INTERESTING that former House Majority Leader John Boehner (R-Ohio) characterizes proposed investigations into fraud in Iraq contracts as “revenge” by the Democrats (“Give-’em-hell Nancy?”

ARE CORPORATIONS DEMOCRACIES OR DICTATORSHIPS?

IF THE CORPORATION is a democracy of its owners, then anti-Wal-Mart union organizers have just as much right to be in the Wal-Mart Stores boardroom as they do in Congress, if they can get elected (“The boardroom bunker,” *The Welch Way*, Dec. 25/Jan. 1).

Importing w/UPS



While those in power never enjoy the process of dissent and diversity of opinion, its value to all institutions is well established. Did board members at General Motors welcome Ralph Nader's attack on the Corvair's safety? If they had, might GM have won a larger share of safety-conscious buyers?

If, however, you believe the corporation is a dictatorial institution, then aggressive dissent has no role or economic value in its boardroom. A third approach is to assume that all shareholders have similar basic values and that they are mirrored in the board's views on fundamental decisions, which are not open to debate.

Choosing a model of corporate governance is now every board's challenge. Before deciding, they should examine the purpose of shareholders' votes. If "corporate democracy" turns out to be an oxymoron, it should be eliminated permanently before it brings more fear and distraction to board members. If not, then directors should be prepared for more discomfort.

-Alan Towers
President
TowersGroup Inc.
New York

The McGraw-Hill Companies

BusinessWeek

JANUARY 22, 2007 (ISSN 0007-7135) ***** 4018

Published weekly, except for one week in January, July and August by The McGraw-Hill Companies, Inc. **FOUNDER:** James H. McGraw (1860-1948).

EXECUTIVE, EDITORIAL, CIRCULATION, AND ADVERTISING OFFICES: The McGraw-Hill Companies Building, 1221 Avenue of the Americas, New York, N.Y. 10020. Telephone: 212-512-2000. Telex: Domestic 127039; Intl. 2360127039. For single copy sales call 1-800-298-9867 or email: busweek@mhfi.com. Subscriber Services: 1-800-635-1200. TDD: 1-800-554-1579

POSTMASTER: Send address changes to BusinessWeek, P.O. Box 8418, Red Oak, IA 51591-1418. Periodicals postage paid at New York, N.Y., and at additional mailing offices. Canada Post Publication Mail Agreement Number 40012501.

Registered for GST as The McGraw-Hill Companies, Inc. GST #R123075673. Copyright 2005 by The McGraw-Hill Companies, Inc. All rights reserved.

Title registered in U.S. Patent Office. European Circulation Office, McGraw-Hill House, Shoppenhangers Road, Maidenhead, Berks SL6 2QL, England. Telephone: +44 (0) 1628 502900; Fax: +44 (0) 1628 630545.

OFFICERS OF THE MCGRAW-HILL COMPANIES, INC.: Harold W. McGraw III, Chairman, President, and Chief Executive Officer; Kenneth M. Vittor, Executive Vice President and General Counsel; Robert J. Bahash, Executive Vice President and Chief Financial Officer; John C. Weisenseel, Senior Vice President, Treasury Operations.

PHOTOCOPY PERMISSION: Where necessary, permission is granted by the copyright owner for those registered with the Copyright Clearance Center (CCC), 222 Rosewood Drive, Danvers, MA 01923, to photocopy any article herein for the flat fee of \$2.00 per copy of each article. Send payment to the CCC. Copying for other than personal or internal reference use without express permission of The McGraw-Hill Companies, Inc. is prohibited. Address requests for customized bulk reprints to BusinessWeek Reprints, 1221 Avenue of the Americas, New York, NY 10020 or call 212-512-3148. ISSN 0007-7135/00/\$3.95

PRINTED IN THE U.S.A.

How to reach BusinessWeek

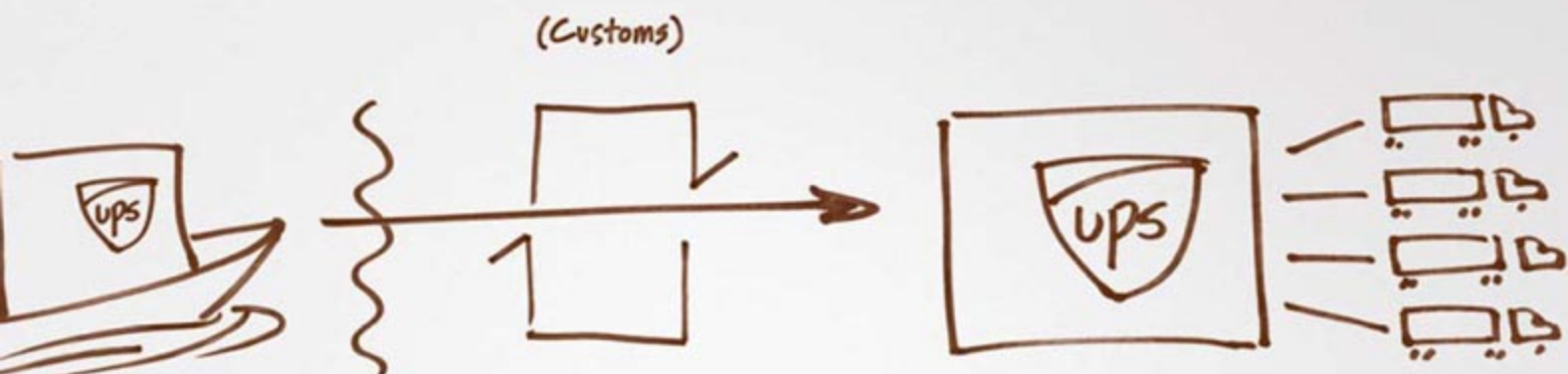
LETTERS FOR READERS REPORT We prefer to receive letters via e-mail, without attachments. Writers should disclose any connection or relationship with the subject of their comments. All letters must include an address and daytime and evening phone numbers. We reserve the right to edit letters for clarity and space and to use them in all electronic and print editions.

E-mail: bwreader@businessweek.com Fax: (212) 512-6458

Mail: BusinessWeek Readers Report, 1221 Avenue of the Americas, 43rd floor, New York, NY 10020

BusinessWeek .com www.businessweek.com

The full text of BusinessWeek, BusinessWeek Top News, and access to BusinessWeek archives starting in 1991 are available on the World Wide Web at: www.businessweek.com and on America Online at Keyword: BW



- Group all your packages as one.
- Breeze through customs.
- Bypass distribution centers.

And use your supply chain to your competitive advantage. With UPS Trade Direct™, importing is simple.

Find out more at ups.com/whiteboard

WHAT CAN BROWN DO FOR YOU?®





Burglar-Proof Windows?

The Microsoft marketing hoopla set off by the Jan. 30 launch of Windows Vista will focus on the software's spiffy new look and enhancements such as greatly improved search abilities (BW—Jan. 15). But the really important changes, mostly hidden, aim to improve Windows' leaky security. What you see of this may be annoying, but trust me, it's good for you.

One big reason Windows has been so vulnerable over the past 15 years is that Microsoft chose to make things easy when faced with a trade-off between security and convenience. But in recent years, as Windows users have grown increasingly outraged by nonstop hacker attacks, Microsoft's attitude has evolved. The company originally intended to base Vista on Windows XP but scrapped that idea a couple of years ago. Instead, it resolved to work off the much more secure foundation of Windows Server 2003. The Server version has generally won good marks for security.

All operating systems have security holes, and Vista will be no exception: One potential vulnerability has already been identified by security experts. The difference is that the holes in Vista should be much harder for the bad guys to exploit, compared with earlier versions of Windows.

A couple of protective features introduced in Windows XP have been expanded in Vista. Windows Defender, an anti-spyware program that was a free download for XP, is built into the new version. And the Windows Firewall is much enhanced. The XP version could block incoming attacks, but the Vista edition watches traffic both in and out of your system, which can help stop malicious programs from stealing data or spewing spam e-mails.

THE CHANGE YOU WILL NOTICE MOST is called user account control. Mac owners have long been used to Apple's OS X asking their permission before installing any software. This is a good thing. Microsoft, similarly, tried to clean up its act in 2004 with a major upgrade to XP called Service Pack 2, and again with Internet Explorer 7 last fall. But Windows has always been promiscuous about loading software from dubious sources without asking questions.

No more. Vista won't install anything, from any source, without explicit permission. (You can turn account control off in a control panel, but it's not wise.) To let an installation proceed, you will have to either click a button to give permission or supply a password, depending on how your



account was set up. Among other things, Vista allows you to set up restricted accounts for your kids to keep them from downloading software to your computer without your password.

But some work needs to be done, especially by third-party software suppliers, to keep account control from driving you nuts. For example, every time I start up, the Logitech mouse software wants to check the Web for updates—and triggers an alert. So does a test version of Norton Antivirus. Eliminating these false alarms will encourage users to pay attention to the warnings rather than just reflexively clicking O.K. Stopping to think for a moment before permitting an installation can help keep Windows more secure.

The new security features may be annoying, but they're good for you

Versions of Vista designed for corporate use include a feature called BitLocker that allows simple but strong encryption of hard-drive contents. It's likely to make its way eventually to home versions, too, but only when a required piece of hardware, called a Trusted Computing Module, becomes common in consumer desktops and laptops.

I'm usually the last person to salute anything that makes life more complicated for computer users. But in the case of Vista, a little inconvenience up front can save you a lot of grief that malicious software and other attacks can cause. The long-overdue security enhancements are bound to irritate some users, but they're all for the best. ■

E-mail: tech&you@businessweek.com

BusinessWeek.com For past columns and online-only reviews, go to technology&you@businessweek.com/go/techmaven/. To hear Steve Wildstrom's podcast on his latest column, go to www.businessweek.com/search/podcasting.htm.





“ Migrating from UNIX to Linux is no simple feat. ”

DELL™
POWEREDGE™ 2950
SERVERS FEATURE
THE RELIABILITY
OF DUAL-CORE
INTEL® XEON®
PROCESSORS.





MediaCentric

BY JON FINE

Creative, But Gentle, Disrupter?

One very genial, very excited gadget geek—that pasty indoor pallor may be explained by the seven TVs in his apartment—is practically bouncing up and down in front of his laptop. As he watches a live basketball game on the screen, he records key plays on the fly and e-mails Web links to the video snippets to a pal. The glee is understandable; the technology cannot help but impress.

Then again, he is adding weight to the cement shoes of those who'd prefer to keep TV more or less as it is.

The snip-and-clip guy, Jason Hirschhorn, spent years inside a traditional media company—his last position was chief digital officer of MTV Networks, where his job was to figure out how MTV would survive in a YouTube-ing world. Today, he's president of Sling Media Entertainment Group.

Sling Media sells the Slingbox, which wirelessly beams programs from your TV to your laptop or cell phone via the wonders of broadband. TiVo, and digital videorecorders like it, time-shift TV programming; the Sling Box and similar devices place-shift TV so you can watch local programming anywhere in the world. This, like many other recent developments, is good for overall TV consumption while being very, very bad for key parts of the TV equation. (For starters, local TV station owners and cable systems have business models built around hitting consumers in specific geographic locations.)

SLING UPPED THE ANTE during the annual January geekathon known as the Consumer Electronics Show by announcing two major developments: the pending release of the SlingCatcher, which makes Sling's technology two-way and lets Web video—from video clips to movie downloads—be viewed on your TV; and the Clip + Sling technology, the snippet-snatch-and-send function that had Hirschhorn so hopped up. Hirschhorn's job is to build out a Sling-branded video destination site and, most important, to convince the kind of people he used to work with that Sling is friendly, not fanged. That CBS CEO Les Moonves demonstrated Clip + Sling onstage during his CES keynote suggests the degree to which guys like Hirschhorn and gadgets like his are leading the way at this media moment.

Technology is busy blowing up your video (if I may recast a phrase first used by AC/DC) as it has done, or is doing, with virtually every other media form. This does



HIRSCHHORN

not make Hirschhorn's charge easy. Sling may seek to be the next Apple—the disrupter with a friendly face. (Or since Steve Jobs has unleashed Apple TV, which pushes online video to your television, a more apt metaphor for Sling might be the non-Apple—in the way that Democratic Presidential candidates jostle to be the non-Hillary.) But Sling is also trying to move from threat to partner without Apple's bona fides or Google's omnipresence. For this, Hirschhorn's past helps. "I understand the paranoia media companies have about their content," he says.

Sling is happy to placate media's jittery giants

His argument is that Sling can help them figure out how to thrive in the "click culture" of today. He suggests Sling's data on viewer habits will prove valuable if shared with media companies. (The most clipped parts of a sitcom, for example, offer a road map to which supporting characters on a show deserve a higher profile.) There's the potential for ad revenue-sharing on its upcoming video site, which will be built around the video streams that get Clipped + Slung—once, that is, ads and revenue are there. Its first big partner: Moonves' CBS, which will beta-test Clip + Sling.

It may or may not make sense for the networks to get in bed with Sling—which, by bringing Web video to the living room, threatens to further erode their monopoly on television. But, as with much else these days, the traditional players have no choice: The details of the victory are uncertain, but the gadget geeks are winning. ■

BusinessWeek .com For Jon Fine's blog on media and advertising go to www.businessweek.com/innovate/FineOnMedia



(TOP TO BOTTOM) PHOTOGRAPH BY ETHAN HILL; CHRIS CASABURI

DELL™ POWEREDGE™
2950 SERVERS FEATURE
THE RELIABILITY
OF DUAL-CORE
INTEL® XEON®
PROCESSORS.



“ Fortunately I get advice from the company ”
that does it every day.



Dell is the U.S. leader in Linux-based server shipments.*
Who better to help you migrate off UNIX?



Purely You

See the Dell difference at www.dell.com/proven/buswk
1.866.219.2670

*IDC Worldwide Quarterly Server Tracker, May 2006.

Dell cannot be responsible for errors in typography or photography. Dell, the Dell logo and PowerEdge are trademarks of Dell Inc. Intel, Intel logo, Intel Inside, Intel Inside logo, Xeon and Xeon Inside are trademarks or registered trademarks of Intel Corporation or its subsidiaries in the United States and other countries. Other trademarks and trade names may be used in this document to refer to either the entities claiming the marks and names or their products. Dell disclaims proprietary interest in the marks and names of others. ©2007 Dell Inc. All rights reserved.

Experienced Hire Career Fair

Bringing Top Experienced Professionals and Elite Employers Together

March 20, 2007 • McGraw-Hill Conference Center • 1221 6th Avenue, 2nd Floor • New York, NY



EMPLOYERS:

Seeking a more efficient way to recruit top experienced talent?

Want to reduce hiring costs and find top-quality, experienced candidates?

The Vault/BusinessWeek Experienced Hire Career Fair is your solution. Sign up today.

- Pre-select candidates who meet your experienced hiring requirements
- Save time and interact only with qualified candidates
- Find top employees quickly and efficiently, at below-industry cost

Learn more and register at www.vault.com/experiencedhire



EXPERIENCED PROFESSIONALS:

Are you a business professional with 5+ years of work experience?

Want to take your career to the next level?

Register for the Vault/BusinessWeek Experienced Hire Career Fair today.

- Interact with hiring decision-makers and recruiters in small groups
- Gain access to elite jobs at top companies – normally found only through recruiters or inside referrals
- Free of charge to professional attendees

Learn more and register at www.vault.com/experiencedhire

At this time, these top employers have already signed up for the Vault/BusinessWeek Experienced Hire Career Fair:



Experienced hire job seekers must pre-register for the event by **March 1, 2007**.

Employers must sign up for the event by **February 1, 2007**. Visit www.vault.com/experiencedhire today!

BY JAMES C. COOPER

Strong Job Markets Dash Hopes For Rate Cuts

Payrolls show the economy is poised to pick up, not weaken further

U.S. ECONOMY

The Labor Dept.'s monthly roundup of job market activity has always been the economic report Wall Street listens to more than any other. It's a market-mover because of its timeliness, breadth of coverage, and its influence over policymakers at the Federal Reserve. What investors heard from the surprisingly strong

December data on Jan. 5 was a death knell for hopes that the Federal Reserve would be cutting interest rates in 2007. The markets, which have been building in expectations of rate cuts for months, promptly tanked.

The report, which showed December payrolls rose by 167,000, along with upward revisions to gains in October and November, was a watershed, at least for perceptions about the economy's current strength and near-term prospects. The broad gains in the labor markets at yearend ran counter to some recent downbeat reports portraying the economy as on the verge of succumbing to the housing recession and softness in manufacturing. The labor strength was powerful evidence that the weakness in those two sectors remains isolated—and is likely to stay that way.

Outside of construction and manufacturing, job growth in the second half of 2006 was even faster than it was in the first half. Job markets were tight enough to keep the unemployment rate at 4.5% last month, only a tick above October's 5½-year low of 4.4%. The labor gains imply businesses are not retrenching but remain optimistic enough about future demand to continue adding to their payrolls. They also show, despite retailers' disappointments over holiday sales, a labor market strong enough to generate the income gains necessary to keep consumers spending at a healthy clip (chart).

Combined with gathering signs that the slowdowns in both housing and manufacturing will be easing in the first half of 2007, the latest job report hardly portrays an economy soon in need of lower interest rates. Just the opposite. Once those drags ease, overall growth is poised to rebound as the economy's underlying strength reasserts itself. In fact, the job report supports the Fed's tough talk of late: The bigger risk to the economy down the road is not weak growth but accelerating inflation.

EXPECTATIONS OF LOWER RATES have always been predicated on weaker consumer spending, which in turn can lead to slowdowns in corporate hiring and capital spending. December's strong labor markets throw cold water on that scenario. Solid gains in jobs and incomes through December, along with lower energy prices, explain why real consumer spending appears to have

grown last quarter by about 4%, at an annual rate—a strong showing by any benchmark.

In December, traditional retailers sounded down-in-the-mouth about their holiday sales, with receipts up only 3.1% from a year ago. However, that modest showing partly reflects a couple of new trends that don't fully show up in the regular holiday numbers. First of all, through Dec. 26, Internet sales at U.S. sites for nontravel items during the holiday season were up 26% from a year ago, to \$23.2 billion, according to an estimate by comScore Networks. The company says retail e-commerce outside of gas, autos, and food now accounts for about 7% of all retail outlays.

Second, gift-card sales are booming, a trend that boosts January receipts, often at the expense of retailers' December numbers. Prior to the holidays, the National Retail Federation Gift Card Survey projected a 34% jump in card buying from the previous year, to \$24.8 billion. Those sales won't show up in a big way until January, when the cards are redeemed. The International Council of Shopping Centers says this pattern is lifting the annual importance of retailers' January sales,

noting that gift-card redemptions could drive about 20% of this month's industrywide receipts.

AMID RESILIENT CONSUMER DEMAND, it's not surprising businesses are shedding some of last summer's concern over the outlook. CEO confidence improved moderately in the fourth quarter after having fallen to a five-year low in the third quarter, according to a Conference Board survey. Those results jibe not only with recent hiring gains but also with other reports last quarter showing strength in capital spending. Through November, production of business equipment was

MORE BUYING POWER FOR JOBHOLDERS



Retail Federation Gift Card Survey projected a 34% jump in card buying from the previous year, to \$24.8 billion. Those sales won't show up in a big way until January, when the cards are redeemed. The International Council of Shopping Centers says this pattern is lifting the annual importance of retailers' January sales,

making solid advances, and outlays for new business construction were still in an uptrend. Even if businesses are a little more uncertain about the outlook, they have not materially altered their spending and hiring behavior.

With businesses expanding payrolls, consumer spending is getting lots of support from income growth. Average hourly pay of production workers in December grew 4.2% from a year ago, up from the 3.2% growth rate this time last year. At the same time, inflation has fallen, boosting buying power. With more people at work, overall income growth is also impressive. Based on the employment report's data on hourly wages and hours worked, income of production workers last quarter was up 6.4% from a year ago. Adjusted for inflation, the pace was the strongest since the boom of the late 1990s.

WHILE THE ACCELERATION in wage growth is great for consumers, it is not so comforting to the Fed. With labor markets tight enough to keep upward pressure on wages, the Fed is not about to cut interest rates for fear that easier credit conditions would only increase demand, further tightening job markets, and add new cost pressures that could eventually push up inflation.

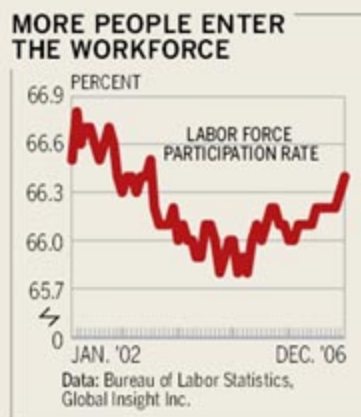
Somewhat surprisingly, the labor markets have shown no hint of loosening despite the economic slowdown. After growing at a heady 5.6% annual rate in the first quarter of 2006, the economy posted modest gains of 2% in the third quarter and 2.6% in the second. Yet the jobless rate still managed to fall from 4.8% in July to 4.5% in December.

However, the current degree of tightness in the labor market is no reason to believe the Fed will have to hike

interest rates—at least not yet. Overall labor costs are being held down by a reduction in benefit payouts, which largely reflects a sharp deceleration in health-care costs. Also, the increase in average hourly pay is partly because a lot of the recent payroll additions have been in higher-paying service jobs. For example, business and

professional services accounted for more than 30% of the gains in overall payrolls during the fourth quarter.

Improving employment prospects also are preventing job markets from tightening too rapidly by drawing more potential workers into the workforce. The labor force participation rate, which is the percentage



of the adult population either employed or looking for work, jumped sharply during 2006, to a 3½-year high of 66.4% (chart). The more people there are in the job hunt, the less downward pressure on the jobless rate.

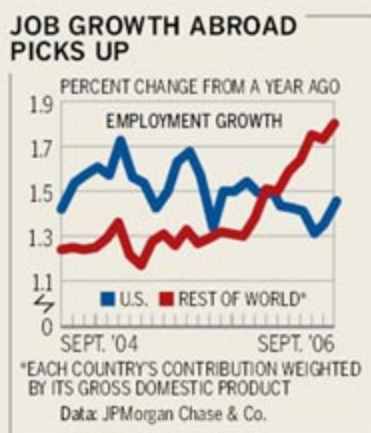
So the latest job data actually have two messages for investors. First, don't expect rate cuts, but don't be too morose: The numbers don't suggest any immediate need for the Fed to begin hiking rates. For now, at least, the economy appears to be in a sweet spot: decent growth with ebbing inflation and the Fed watching from the sidelines. ■

GLOBAL EMPLOYMENT

Where the Jobs Are: Everywhere

THE LABOR MARKET is heating up across the globe. Businesses in developed and emerging economies alike are adding workers at a rapid clip as the global economy keeps expanding. If the hiring trend persists, it could have important implications for the U.S. economy.

Employment growth outside America is at its fastest rate since 2000. According to JPMorgan Chase & Co., in September, 2006, the latest period available, overall job growth in 18 countries was up 1.8% from the previous year. The pace is also better than in the U.S., where employment in December was up 1.4% from a year ago.



Early returns on job figures during the fourth quarter remain strong around the globe. The most recent job reports from Canada, Argentina, Australia, and Britain were positive, and the outlooks for employment remain upbeat as well. In Brazil, for example, the Institute of Applied Economic Research, a government-run public foundation, is forecasting job growth of no less than 2.7% for 2007.

In addition to continued hiring, JPMorgan Chase economist David Hensley wrote in a Jan. 8 research note, "We look for a broader acceleration in wage growth in 2007 as unemployment rates fall further

and companies compete more aggressively to fill positions." That bodes well for U.S. multinationals and exporters. Tighter labor markets should lead to stronger consumer demand, which would boost business activity and investment spending.

But signs of accelerating wage gains will also lead to higher rates, says Hensley: Central banks in Britain, Canada, and the Scandinavian countries would raise rates in response to faster wage gains, but the "European Central Bank also will be sensitive to signs that wage growth has turned up."

If the Federal Reserve holds rates steady as hikes abroad occur, the dollar could face greater downward pressure. That would make American-made goods more attractive abroad and fatten profits earned outside the U.S. when they are turned into greenbacks. ■

—By James Mehring in New York

we
ENABLE
mobile content and
PROTECT
its delivery

so the world can
MOVE



Today we are living in the "Any Era," where the world demands access to the latest content *anytime, anywhere, on any device*. Whether it's ringtones, pictures, games, or videos, VeriSign intelligent infrastructure services enable and protect the exciting new ways carriers, portals, and media companies are reaching their customers. To learn more, visit www.enableandprotect.com.

The Business Week

News you need to know

EDITED BY HARRY MAURER



Cheaper Black Gold That midsummer nightmare—oil prices near \$80 a barrel—feels long ago and far away. Crude prices have tumbled nearly a third from their July peak. On Jan. 10 the price plunged \$1.62, to \$54.02, on the **New York Merc** after the **Energy Dept.** reported the biggest surge in three years in inventories of distillate fuel, the category that includes heating oil.

Is warm winter weather behind oil's slide? That's part of it, but only about 7% of oil is used for heating. Other factors include slower economic growth and cheating by **OPEC** members on their production-cutting deal (a Jakarta depot, photo). Plus, Belarus reported progress on Jan. 10 in a spat that halted shipments of Russian oil across its territory to Europe. In any case, for oil-consuming nations (and that's most of us), less pricey oil is as good as a tax cut.

ONLINE See "The oil market's weather obsession," www.businessweek.com/go/tbw

The Health Governor Maybe it was because he broke his leg skiing over Christmas, but three days after he was sworn in to a second term as California's governor, **Arnold Schwarzenegger** proposed offering health-care coverage to the state's 6.5 million uninsured residents. The plan, costing an estimated \$12 billion a year, would be funded by businesses, doctors, and hospitals. Conservative lawmakers are expected to challenge it as an open-ended tax. The move would make California one of four states to provide universal coverage and will shine a spotlight on the issue in the 2008 Presidential election season.

Phonemakers Tremble As is his wont, Steve Jobs set tongues wagging around the globe on Jan. 9 when he announced the forthcoming iPhone, a music, camera, Internet, video, and cell-phone combo. He also portentously dropped "Computer" from Apple's corporate name.

See "Turning cell phones on their ear," page 40, and **ONLINE** "The future of Apple," www.businessweek.com/go/tbw

A Slimmer Trade Gap Could the seemingly inexorable decline in America's competitive position be ending? The November trade deficit in goods and services, released on Jan. 10, was \$58.2 billion, the lowest since July, 2005. Even more encouraging are glimmerings of a turnaround in the nonoil trade gap, which isn't influenced by the recent drop in crude prices. The nonoil deficit, averaged over the previous 12 months, actually shrank in November compared with the 12 months ending in October. That's a cheery sign, since it has expanded in 55 out of the past 57 months.

Gap up for Grabs After years spent struggling to sell more jeans and tees, Gap is trying to sell itself. On Jan. 8, **CNBC** reported the giant chain has hired **Goldman Sachs** to seek a buyer, driving Gap shares up 7.25%, to \$20.26. Analysts say any potential bidder would be a private equity or other investment group rather than another specialty retailer, which would have trouble digesting Gap's thousands of **Banana Republic**, **Old Navy**, and Gap stores. Gap and Goldman declined to comment. On Jan. 10, the head of Gap's adult division and Old Navy's design chief announced their exits.

ONLINE See "Gap on the block," www.businessweek.com/go/tbw

Patent Wars A **Supreme Court** ruling has the patent world buzzing. In 1997 biotech **MedImmune** licensed technology from **Genentech** to make a drug used to prevent respiratory illness in children, but did so under protest, claiming Genentech's patent was invalid. On Jan. 9 the justices said MedImmune didn't have to terminate the license—and risk huge damages for infringement—to go to court and try to void the patent. The case now goes back to a trial court for resolution, while attorneys light up the Internet with speculation whether it will make it easier for other patent licensees to bring challenges.

Dogfight Over Delta Decisions, decisions. **Delta Air Lines** may have yet another way out of Chapter 11: hooking up with the other big boy in bankruptcy, **Northwest**. Delta had been insisting it wanted to emerge as an independent, spurning an \$8.4 billion takeover bid from **US Airways** last fall. But US Airways may have made that course impossible on Jan. 10 by boosting its offer to \$10 billion. While Delta management was just saying no publicly, however, it has been in talks with Northwest about a merger, reported *The Wall Street Journal* on Jan. 10. Time is of the essence: Northwest plans to file its reorganization plan in court on Jan. 16. The maneuvers come as **United** and **Continental** explore a combo of their own.

ONLINE See "Delta's 'leave-us-alone' plan just got trickier," www.businessweek.com/go/tbw

GE's Plastics Auction It's hard to make money in plastics these days, so **General Electric** wants out. It has put its \$7 billion plastics unit up for auction—with the caveat that private equity firms might not be able to team up for a bid. One reason, first reported in *The Wall Street Journal* on Jan. 9, is to abate growing antitrust concerns over private equity "clubs." But the company also wants as many bidders in the party as possible. GE is likely less concerned about the **Justice Dept.** than its own bottom line.

Executive Shuffle The king has a new throne, but his crown is less bejeweled. Nine months after abdicating as head of **Burger King**, saying he wanted to spend more time with his family, **Gregory Brenneman** on Jan. 8 was named CEO of sandwich chain **Quiznos**. Other notable managers moving on: **Stephen Jonas**, who revamped **Fidelity Investment's** mutual fund unit, will retire at the end of January; and **Lawrence Jackson**, head of global sourcing at **Wal-Mart**, quit on Jan. 8 after nine months in the job, the fourth top-rank exec to leave since December.

Stern's Latest Bonanza Shock jock and stripper aficionado **Howard Stern** should have no problem this year paying his tab. His employer, **Sirius Satellite Radio**, said on Jan. 9 that Stern will be given stock valued at \$83 million because the company beat subscriber targets for 2006. Before Stern was hired, Sirius expected to have 3.5 million subscribers by yearend 2006, but it ended up with 6 million. The bonus sweetens the \$500 million, five-year contract Stern signed in 2004. Meanwhile, Sirius and its chief rival, **XM Satellite Radio**, are bleeding red ink, while Sirius stock sank 40% over the past year. On Jan. 10, Sirius **CEO Mel Karmazin** said a merger with XM would make sense, and both stocks jumped.

Bombshell of the Week

Venezuelan President Hugo Chávez sure knows how to throw a scare into the financial markets. When the leftist leader said on Jan. 8 that he intends to nationalize a number of utilities, it raised the possibility that Mexican tycoon **Carlos Slim** would walk away from a deal to buy the nation's largest telecom provider, **CANTV**. Last April, **Verizon** announced a plan to sell its 28.5% stake in CANTV for \$676.6 million to a company jointly owned by **Teléfonos de México**, Mexico's biggest telco, and **América Móvil**, a Latin American wireless outfit. Slim, the world's third-richest man, controls both of those companies. The Chávez announcement crushed CANTV's value: By Jan. 10, its shares had fallen 29%, to \$14. On paper, Verizon's stake is now worth a mere \$441 million.



CHAVEZ—DEALBREAKER?

ONLINE See "Venezuela's Chávez rattles markets," www.businessweek.com/go/tbw

HOWARD YANES/AP PHOTO

Sprint's mobile broadband works in places Cingular's can't raise a single bar.

Sprint Mobile Broadband works in 2x more cities than Cingular's BroadbandConnect.



PX-500 by Pantech*

Get the power to download huge files and attachments instantly from anywhere on the nation's largest mobile broadband network. It's another way Sprint Business helps you make just about any place a workplace. And now, get a card for free.

FREE CARD

with new card activation on unlimited data access plan. Requires 2-yr agreement and \$49.99 mail-in rebate. No voice plan required.

1-8SPRINT-BIZ
sprint.com/mobilebroadband

Sprint  **POWER UP™**

Together with NEXTEL

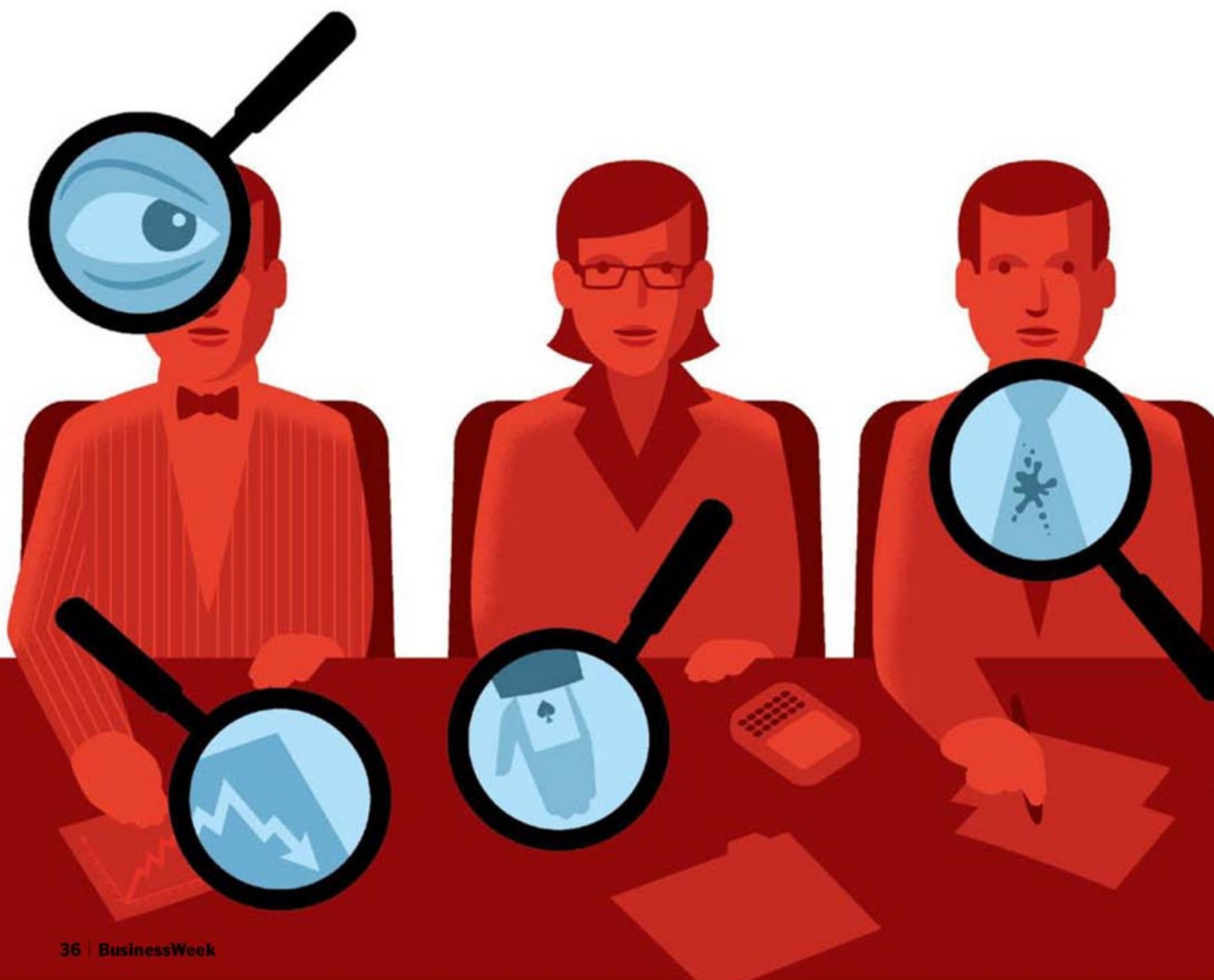
Sprint Mobile Broadband Network reaches over 180 million people. Coverage not available everywhere—see map for details. Coverage comparison based on most recent available information regarding Cingular broadband market coverage as of 11/27/06. Offer not available in all markets/locations. Subject to credit approval. Additional restrictions apply. Requires purchase by 2/17/07 and activation by 3/3/07 of a new line on Unlimited Data Plan (\$59.99) and two-year agreement. \$36 activation fee and \$200 early termination fee apply. Mail-in Rebate: Rebates cannot exceed purchase price. Taxes excluded. Line must be active 30 consecutive days. Allow 8–12 weeks for rebate. ©2007 Sprint Nextel. All rights reserved. Sprint, the "Going Forward" logo and other trademarks are trademarks of Sprint Nextel.

GOVERNANCE

BOARD OF HARD KNOCKS

Activist shareholders, tougher rules, and anger over CEO pay have put directors on the hot seat

BY NANETTE BYRNES AND JANE SASSEEN



JUST FIVE YEARS AGO, THE Directors' College run by the Stanford Law School was a pretty tiny affair. If the three-and-a-half-day training program drew even 100 people, that was big. But in the wake of the corporate scandals, board members realized they needed to bone up on everything from financial accounting to governance, and applications exploded. Stanford has since enlarged the program to some 250 slots. This year, it also added a twice-yearly session in conjunction with its Graduate School of Business that will take in an additional 100 attendees.

Yet even with this expansion, last June's session sold out months in advance. And this year's openings are filling up even faster. "The pressures on boards

are already great, and they are only going to grow," says Joseph A. Grundfest, co-director of the university's Rock Center for Corporate Governance.

A new era for directors dawned with the passage of the Sarbanes-Oxley Act of 2002. Then board members were hit with the frightening prospect of real financial liability in a smattering of lawsuits that followed the corporate crime wave. Now the heat on directors is growing more intense. Their reputations are increasingly at risk when the companies they watch over are tainted by scandal. Their judgment is being questioned by activist shareholders outraged by sky-high pay packages. And investors and regulators are subjecting their actions to higher scrutiny. Long gone are the days when a director could get away with a

quick rubber-stamp of a CEO's plans.

The new dynamic has played out in recent board dramas involving Home Depot, Hewlett-Packard, and Morgan Stanley, among others. If Home Depot's directors had any hope that the spotlight on them would fade in the wake of departure of ex-CEO Robert L. Nardelli on Jan. 3, they now know better. Unhappy investors are continuing to agitate for new blood in the company's boardroom. "The culpability is not on the CEO for asking [for high pay] but the directors" for approving it, says Richard Ferlauto, director of pensions and benefits policy for the American Federation of State, County & Municipal Employees, one of the more vocal investment funds putting pressure on Home Depot's board. "Compensation is a symptom. It flags for us a board



that is unwilling to challenge a CEO.”

And that just won't do. The old rules of civility that discouraged directors from asking managers tough or embarrassing questions are eroding. At the same time, board members are being forced to devote more time and energy to many of their most important duties: setting CEO compensation, overseeing the auditing of financial statements, and, when needed, investigating crises. That's the good news. The bad news is they are so busy delving into the minutiae of compliance that they don't have nearly as much time to advise corporate chieftains on strategy. Many board candidates no longer find the job

attractive. “If someone has accumulated a lot of wealth, they just don't think it's worth the risk,” says retired General Hugh Shelton, the former chairman of the Joint Chiefs of Staff who now heads the compensation committee at Red Hat Inc.

The latest luminary to sound off about the situation is Jim Clark, who resigned from the board of photography Web site Shutterfly Inc. on Jan. 8. “I basically kept that company alive. I hired the CEO and have been involved in every step,” said Clark in an interview two days later. Because he owns 30% of the company, however, new rules on director independence limit his role on important board commit-

tees. “Being on the board of directors of a public company has already got all this risk. And I have all these constraints and essentially no power.”

The hottest issue for boards this year is shaping up to be executive compensation. For the first time ever, companies are required to disclose a complete tally of everything they have promised to pay their executives, including such until now hidden or difficult-to-find items as severance, deferred pay, accumulated pension benefits, and perks worth more than \$10,000. They will also have to provide an explanation of how and why they've chosen to pay executives as they do. The numbers are

likely to be eye-popping. Michael S. Melbinger, a top compensation lawyer in Chicago, thinks that when all the proxies are filed, there could be 50 companies or more with CEO pay packages worth \$150 million-plus.

And this is, believe it or not, coming as just as big a surprise to many directors as it will be to investors. Up to now, most directors have never seen a tally for the total pay they've promised to executives. “Pay was all compartmentalized: Boards would approve a salary, a certain amount for a bonus, or a certain amount if he got fired, but no one ever added it all up,” says Fred Whittlesey, the head of pay consultants Compensation Venture Group.

With proxy season approaching, boards are finding themselves digging deep into compensation consultant reports and questioning the logic of these packages—and even sometimes, in awkward meetings, asking CEOs and other highly paid officers for give-backs. Compensation lawyer Melbinger tells the story of a meeting several months ago in which he sat down with a board and their CEO and outlined his perks. The CEO had a provision in his contract that not

PLAYBOOK: BEST-PRACTICE IDEAS

The New Rules For Directors

<p>PAY</p> <p>Companies will disclose full details of CEO payouts for the first time in their 2007 SEC filings. Activist investors are already drawing up hit lists of companies where CEO paychecks are out of step with performance.</p>	<p>KNOW THE MATH</p> <p>Before O.K.'ing any financial package, directors must make sure they can explain the numbers. They need to adopt the mindset of an activist investor and ask, What's the harshest criticism someone could make about this package?</p>
<p>STRATEGY</p> <p>Boards have been so focused on compliance that duties like strategy and leadership oversight too often get short shrift. Only 59% of directors in a recent study rated their board favorably on setting strategy</p>	<p>MAKE IT A PRIORITY</p> <p>To avoid spending too much time on compliance issues, strategy has to move up to the beginning of the meeting. Annual one-, two- or three-day off-site meetings on strategy alone are becoming standard for good boards.</p>
<p>FINANCIALS</p> <p>Although 95% of directors in the recent study said they were doing a good job of monitoring financials, the number of earnings restatements hit a new high in 2006, after breaking records in 2004 and 2005.</p>	<p>PUT IN THE TIME</p> <p>Even nonfinancial board members need to monitor the numbers and keep a close eye on cash flows. Audit committee members: prepare to spend 300 hours a year on committee responsibilities.</p>
<p>CRISIS MANAGEMENT</p> <p>Some 120 companies are under scrutiny for options backdating, and the 100 largest companies have replaced 56 CEOs in the past five years, nearly double the terminations in the prior five years</p>	<p>DIG IN</p> <p>The increased scrutiny on boards means that a perfunctory review will not suffice if a scandal strikes. Directors can no longer afford to defer to management in a crisis. They must roll up their sleeves and move into watchdog mode.</p>

FED UP Jim Clark's frustration at Shutterfly drove him off the board



MUTUAL FUNDS

A Bigger Voice for Small Investors

BY ROBEN FARZAD

The very rich, F. Scott Fitzgerald once observed, “are different from you and me.” That has applied even to shareholder activism, a niche of the investing world dominated by hedge fund managers who are paid enormous fees to holler and claw for every last nickel of return on behalf of their wealthy clients.

But with corporations under mounting pressure to acknowledge shareholder rights, ordinary mutual fund managers are increasingly asserting themselves on behalf of smaller investors.

The standout example is David J. Winters, chief executive of Mountain Lakes (N.J.)-based Wintergreen Advisers, a mutual fund firm with \$1.3 billion in assets under management. His 15-month-old Wintergreen Fund returned 20% in 2006, four points more than the Standard & Poor’s 500-stock index, thanks in good part to his activist approach. “We don’t treat our stocks like rental cars,” says Winters. “You’ve got to think and act like an owner, getting the company to think better.”

That’s what Winters has been doing with his second-largest position, Consolidated-Tomoka Land Co. The 105-year-old property developer owns a vast expanse of virgin land in Florida. Winters has been using his 16% stake to encourage management to stay the course on its measured development

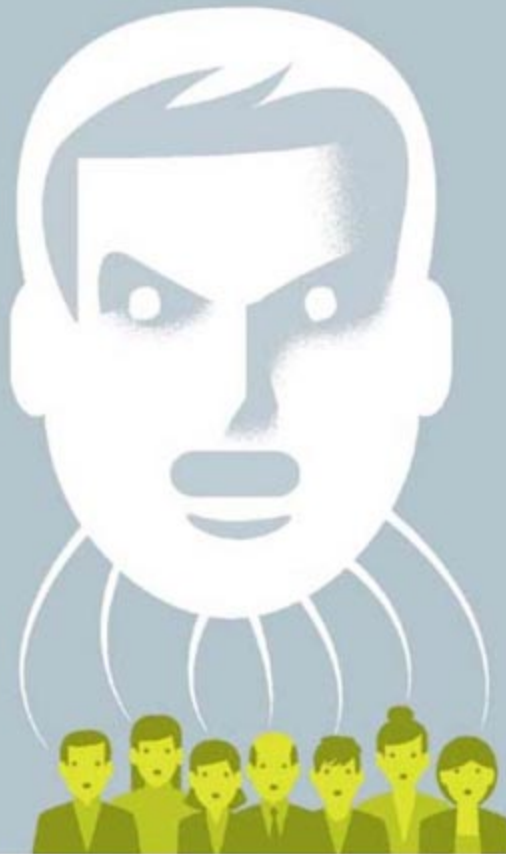
campaign and to buffer it from pressure to liquidate its acreage. “We try to engage companies in a long-term constructive way,” says Winters. “They’ve been very receptive.”

Meanwhile, Franklin Mutual Advisers, Winters’ old fund shop, has affixed itself to the ankle of forest products giant Weyerhaeuser Co. Franklin is using its

\$1.2 billion stake to petition the company to convert itself into a real estate investment trust in order to gain tax advantages.

Even Wall Street, which takes great pains not to offend investment banking clients, is flexing its muscle to benefit fund investors. Morgan Stanley Investment Management is using its 7.6% stake in The New York Times Co. to lobby Times management for more shareholder accountability. In December the \$450 billion asset manager—whose funds are widely available to retail investors—hired a respected activism expert to deal exclusively with corporate-governance issues.

So-called socially responsible investing is also exerting more activist influence. The asset management arms of Deutsche Bank, Goldman Sachs, Merrill Lynch, Morgan Stanley, and UBS are all signatories to the 2006 Carbon Disclosure Project, a global effort to push companies to recognize their impact on climate change. The roster of more than 200 supporting investment firms, representing \$31 trillion in assets, is emboldening a slew of socially responsible proposals at shareholder meetings. “We’re seeing a strong increase in the support for our proposals,” says Stu Dalheim, manager of advocacy and policy for Calvert Group, the \$14 billion socially responsible fund shop. He says the company’s environmental and social resolutions at corporations are now “routinely getting support in the 20%-to-30% range,” three times what it was five years ago.



only required the company to reimburse him for his medical coverage, deductibles, and co-pays but it also had to give him a “tax gross-up” for the payments. One of the stunned board members said: “Now let me get this straight—not only do you not have to pay the amounts for your medical coverage that every other employee of this company has to pay, we pay your taxes on it, too?” The CEO turned bright red, Melbinger says, recognizing how badly that was going to look on the disclosure forms. He quickly agreed to give up the perk.

Elsewhere, too, such goodies are disappearing—but not without a price. In a December filing with the Securities & Exchange Commission, the board of Lockheed Martin Corp. said it would eliminate certain executive perks—including fees for country clubs, a car and driver, and

tickets to sports events—in return for onetime salary adjustments. Lockheed’s directors had no comment. But getting executives to actually notch down their pay isn’t so easy. On the really big-ticket items directors have little leverage to alter the terms of employment contracts.

It’s not just compensation committee members who find the world changing. Audit committees used to meet only twice a year: once when it was time to take the audit in and once more to ratify it. Dick Swanson, chair of the audit committees of two NASDAQ-traded companies, says he now holds 8 to 12 meetings a year for each committee. In addition, he spends many more hours keeping up on what all the other board committees are doing, especially focusing on any risk—financial, operational, or otherwise—that the company

may run. “It’s not like the old days when you could join a board for the twice-a-year dinners,” says Swanson.

Some argue that as a result of the heightened pressure, boards are getting better. “One of the reasons bad stuff went on so much in the past,” says Warren L. Batts, former chairman and CEO of Tupperware Brands Corp. and now a director of Methode Electronics Inc., “was the board wasn’t organized to deal with them. People would look around at each other and say, ‘Who’s going to be the first to say something here? I don’t think I want to.’” Now, better-educated and maybe a little scared, more directors are speaking up. ■

BusinessWeek.com For a Q&A on corporate governance with tech legend Jim Clark go to www.businessweek.com/extras.



LISTEN
For Jobs,
a bravura
San Francisco
presentation

HELLO, WORLD

TURNING CELL PHONES ON THEIR EAR

Is the new iPhone a genre-buster in the mold of the Mac and iPod? Yes—and no

BY PETER BURROWS
AND ROGER O. CROCKETT

HIS USUAL SMOOTH voice turned raspy, Steve Jobs nonetheless radiated the satisfied glow of a man who had just pulled off a bravura performance before a packed house at San Francisco's Moscone Center. In his hand was his latest gem: a combination phone/music player/Web browsing device called the iPhone. Tapping on its sleek, candy-bar-size screen, Jobs conjured up Wall Street's verdict: "Let's see, Apple's stock is up...8%!" he said matter-of-factly. "Now let's look at RIM [cell-phone rival and BlackBerry maker Research in Motion]. Hmm, it's down 7%."

Look out—here comes another genre-

busting gadget from Jobs and the newly named Apple Inc. Despite the iPhone's high starting price of \$499, Jobs is promising to turn the cell-phone business on its ear. That's no idle threat, coming from the guy who paved over the personal computer's awkward interface of arcane commands with easy-to-use graphic icons in the 1980s. Apple also set the tone for the digital music market when it brought out the iPod in 2001, sweeping away a clutter of clunky, hard-to-use players.

DROP THE 'COMPUTER'

NOW, JOBS AIMS to leapfrog rivals with a device that offers a similar panoply of capabilities to other high-end "smart phones" like the BlackBerry and Palm's Treo—minus the frustrating complexity that has turned away mainstream consumers. "The problem is that they're not

so smart, and they're not so easy to use," Jobs told the adoring Macworld crowd.

Here's why the iPhone should scare the daylights out of phone makers: Despite Apple's announcement that it was dropping "Computer" from its name, there's more computer in the iPhone than just about any other smart phone out there. It runs a slimmed-down version of the Mac OS X software found in every Mac PC. And it's a lot easier for Apple to add phone features to a mobile computer than it is for a handset maker to move the other way. If the iPod helped people take all their music with them anywhere, the iPhone promises to cut the moorings from a whole new swath of digital activities, from e-mail to video entertainment. "This clearly underlines the fact that we are entering a new phase of computing," says Seamus McAteer, co-founder of the market research firm M:Metrics Inc. "Mobile phones are becoming full citizens in the computer world."

The iPhone could set a new standard for the universal digital device when it goes on sale in June. An ingenious interface lets the phone play many roles. Gone is the keyboard, the usual mess of tiny keys and cryptic buttons, replaced by a touch-sensitive 3.5-inch screen.

But if the iPhone is to be truly revolutionary, it must also crack open the power structure of the cellular industry. That will be a much tougher nut. Today, most consumers choose a carrier, then pick from various phones that are compatible with its network. Apple created the online music infrastructure in an environment where the established market had been disrupted by file sharing (remember Napster?). But the wireless phone industry is completely different, with strong incumbents. And unless Apple drops the price, iPhone may not appeal to enough buyers to seriously disrupt the industry. There's also the little issue of whether Apple can wrest the iPhone name away from Cisco Systems Inc.

Still, Apple's rethinking of the phone may spur the whole industry to deliver on its many visions of an easy-to-use, universal digital device. This has been an



Gone are tiny keys. Instead, a touch-sensitive screen

(L. TO R.) JOHN TODD/ISIPHOTOS.COM; COURTESY OF APPLE



Conventional wisdom would tell you small farms can't operate as efficiently as large ones. But in Poland, Cargill is going beyond the conventional to help small livestock farmers compete. Large farms in Europe have traditionally had the advantage of feed delivery services while small producers must travel to dealers to buy the few bags they require. So Cargill worked with feed dealers to bring the store to the farm, on trucks that efficiently deliver small feed orders on a regular schedule. The dealers get new customers and farmers get service they never thought possible. This is how Cargill works with customers.

collaborate > create > succeed™



HOW DO YOU EFFICIENTLY DELIVER FEED TO A FARMER WHO KNOWS ALL HIS ANIMALS BY NAME?



ongoing struggle for Motorola Inc., even while it was scoring a major hit with its slick-looking RAZR. CEO Edward J. Zander is now pushing simplicity. His new RIZR Z6 model, due out midyear, will let users download a song, send photos, or leap to the Web in a click or two, down from about six with current phones. "Wouldn't it be great to have an easy-to-use, same-as-your-PC mobile device in your pocket?" Zander asked an audience

at the Consumer Electronics Show in Las Vegas on Jan. 8.

Sure—but it sounds like the iPhone. If it really catches fire and Cingular Wireless, Apple's exclusive U.S. partner, benefits from the relationship, other carriers may have to rethink their strategy. Instead of pushing their mobile services such as movies and music, they might let handset makers and content partners control more applications that lead to

greater data usage. The iPhone's capabilities also could help spur Cingular's sales of other services, from photo sharing to basic three-way calling.

It's still six months before Jobs's latest brainstorm hits stores. But already it is delivering the phone industry a wake-up call. ■

—With Cliff Edwards and Steven H. Wildstrom in Las Vegas, and Arik Hessel-dahl in New York

LEXICON

TALK OF THE TECH TOWN

BY STEPHEN H. WILDSTROM,
CLIFF EDWARDS, AND JAY GREENE

When **Steve Jobs** took the wraps off Apple's new iPhone at the Macworld Expo in San Francisco, he instantly upstaged an even bigger technology event in Las Vegas. More than 140,000 dedicated gearheads mobbed the hotel showrooms at the Consumer

Electronics Show to ogle a bewildering array of gadgets. These have a variety of exotic capabilities and their own geeky names. So memorize this list before you try talking with haughty store clerks.

BusinessWeek weekend See the latest gadgets from the Consumer Electronics Show on our weekly TV show, *BusinessWeek Weekend*. Check local listings or go to businessweekweekend.com.

ILLUSTRATION BY ROBERT NEUBECKER

Full HD (aka 1080p)

Currently the best image quality you can get on high-definition television. But content is scarce.

Follow-me TV

Lets you start watching a recorded TV show in your family room, say, and then move to your bedroom without losing your place.

Blu-ray Disc, HD-DVD

Two rival standards for next-generation, high-definition DVDs—it's still too early to call the winner.

HDMI

A mysterious standard for connecting an HDTV source, such as a cable set-top box, to an HD display. The mystery: How a cable can cost \$80 to \$120.

Slingbox

A device from Sling Media that makes live or recorded TV from your home system available to PCs and handhelds over the Net.

HSDPA/EV-DO

Two superfast third-generation mobile networks, the former from Cingular Wireless, the latter from Sprint Nextel and Verizon Wireless.

Location-based services

Global positioning chips in your phone let companies figure out where you are and point you to the best local shop or restaurant.

WiMAX

A new mobile Internet standard, more advanced than Wi-Fi, that will soon be available from Sprint Nextel, Clearwire, and others.

IPTV

Stands for Internet protocol television—meaning TV delivered over the Web.

Home servers

Put all your photos, music, and video on one server that can dish them up on different devices in your home.



NEW GOOD BUSINESS



TRADE FAIRS ORGANISED BY IFEMA

JANUARY

INTERNATIONAL GIFT, JEWELLERY AND FASHION JEWELLERY WEEK
 INTERGIFT 
 IBERJOYA 
 BISUTEX 

FEBRUARY

SIMM Madrid International Fashion Fair 
 CIBELES FASHION SHOW
 CASA PASARELA Design Fair for Home Trends

MARCH

SAL Food Trade Show
 SIPIEL FOOTWEAR AND LEATHER GOODS INTERNATIONAL WEEK
 MODACALZADO 
 IBERPIEL MARROQUINERÍA 

APRIL

MADRID INTERNATIONAL FURNITURE EXHIBITION

MAY

MADRID INTERNATIONAL AUTO SHOW
 DIVERSE SELECT PRODUCTS

AUGUST

PROMOGIFT Promotional Gift Trade Fair

SEPTEMBER

SIMM Madrid International Fashion Fair 
 CIBELES FASHION SHOW
 INTERNATIONAL GIFT, JEWELLERY AND FASHION JEWELLERY WEEK
 INTERGIFT 
 IBERJOYA 
 BISUTEX 
 SIPIEL FOOTWEAR AND LEATHER GOODS INTERNATIONAL WEEK
 MODACALZADO 
 IBERPIEL MARROQUINERÍA 

OCTOBER

SICI International Integral Kitchen Exhibition



International event certified by UFI
 (The Global Association of the Exhibition Industry)

Madrid is the capital of innovation, a privileged enclave where the most competitive companies are concentrated. Here, you will find new opportunities and contacts for your business. Discover them at www.exportmadrid.com. Today, Madrid is an international meeting point and reference at the Fairs organised by IFEMA in the Fashion, Textiles, Footwear, Accessories and Furniture sectors, etc. A region with the best infrastructure and services, which also offers hospitality and many attractions, enabling you to enjoy all the cultural and leisure possibilities of a big city during your visit.



MADRID TRADE FAIR
 The most effective
 Business Centre

www.ifema.es

www.descubremadrid.com

www.exportmadrid.com

NEW
 GOOD
 MADRID



Cámara
 Madrid

www.camaramadrid.es



REAL ESTATE

NEW LISTING! (SORT OF)

Agents are pulling houses off the market and then presenting them as new offerings

BY PETER COY

REAL ESTATE AGENT ROSS Simone wasn't attracting any potential buyers for a house in Mechanicsville, Md., that had sat on the market for months, so last November he took action. He pulled the house out of the regional database of active listings and then immediately reinserted it, changing the property ID number used to track properties over time. The result: The house appeared to be hitting the market for the first time. "It's in the best interests of my client [the seller]," Simone said in a November interview. "I started doing it consistently this year. I do it as much as I can."

With open houses as quiet as death

lately in many parts of the country, sellers' agents are trying everything they can to make a sale, including sometimes tweaking the computerized data that potential buyers depend on. Fresh listings attract attention and can fetch higher prices because buyers are less likely to make lowball offers.

Real estate is largely self-regulated. In most of the U.S., agents are responsible for entering information about the homes they're selling into a database that is maintained by the local Multiple Listing Service. Each of the 900-plus MLSs sets its own rules. The trick of making old listings appear new is against the rules of Simone's MLS, although he said later that he didn't know it at the time.



What's perhaps more surprising is that in some regions, the local MLS does nothing to prohibit relisting a house in a way that makes it appear new on the market. In Atlanta, for example, First Multiple Listing Service Inc. charges sellers' agents just \$25 to withdraw a listing. When they then relist the home, it shows up on "hot sheets" of homes that are fresh on the market. A buyer's agent who investigates can see that the house was for sale before, but not for how long. First MLS President Cantey Davis acknowledges that the system could give buyers a wrong impression of how long a home has been for sale but says he has received a "minuscule" number of complaints about it.

KNOWING WHAT TO LOOK FOR

WHEN MANY HOMES in an area are relisted as new, it skews the "average days on market" statistic, making the market look healthier than it really is. For sellers, refreshing a listing can also disguise the fact that the previous listing was at a higher price. Buyers often regard a price cut as a sign of weakness.

Whether it's within the local rules or not, the practice of relisting houses to give them a new debut is a symptom of an imbalance in market knowledge. Buyers can sometimes spot manipulation of the databases, but you have to know what to look for, and many buyers' agents don't.

Is this wrong? Many MLS organizations think so. In Massachusetts, MLS Property Information Network Inc. recently improved disclosure of sales histories. Metropolitan Regional Information Systems Inc., which covers Mechanicsville, Md., says it checks its listings nightly for violations. In fact, it says it eventually caught and corrected Ross Simone's gambit, which was first pointed out by the Southern Maryland Housing Bubble News blog. (Simone's boss, Wayne Wivel, president of Re/Max 100 in Annapolis, Md., said in December he had no knowledge of any manipulation.)

But brokers often resist change. Northwest Multiple Listing Service in Kirkland, Wash., discloses the history of listings, but relists still show up on the hot sheets. CEO Jack Johnson says, "We've had difficulty convincing the board of directors" to eliminate what he calls "cancel/relist." As long as the buying public knows less about properties than the agents who list them, *caveat emptor*. ■

CHRISTOPHE VORLET

Resetting the Odometer

Here's how some real estate agents can manipulate computerized listings to obscure how long homes have been for sale:

WITHDRAW a house, then immediately relist it to reset "days on market" to zero

ZERO OUT the property ID number, which can track the history of listings

TWEAK the address so the system can't see that a house has been listed before

▶ Hitachi | true stories

COAL'S COMEBACK

The True Story of Clean Power in Council Bluffs



Coal used to be a four-letter word in environmental circles. But supercritical coal-fired technology from Hitachi is helping change that perception, starting with MidAmerican Energy Company's Council Bluffs Energy Center Unit 4.

Watch a new kind of power plant take shape in America's heartland, one capable of producing much of Iowa's electricity, with far fewer emissions than traditional coal-fired units.

Now playing ▶ hitachi.com/truestories



Hitachi | true stories

A documentary film series about the remarkable stories that unfold when real people and Hitachi technology come together to inspire the next great achievement.

HITACHI
Inspire the Next



JOB-HUNTING

WHAT B-SCHOOLERS LUST FOR NOW

These days, private equity is the No. 1 object of desire. But jobs are scarce

BY MICHELLE CONLIN

EVERY DECADE, ANOTHER faddish career opportunity dazzles the nation's business schools. In the 1980s, MBAs dreamed of Wall Street fortunes, swaggering their way into penthouses and private planes. During the dot-com bubble, it was about vesting swiftly and starting a foundation by age 30.

Today job lust among B-schoolers is fiercest for the gilded, clubby preserve of private equity. "Absolutely, it's become the hot job for MBAs," says Maury Hanigan, president of New York's *MBA Scouting Report*.

As always, MBAs chase the money. And nowhere are the pay packages more regal than in the land of private equity. First-year compensation of \$300,000 for top-tier talent at a Wall Street investment bank doesn't seem too shabby—until you consider that thoroughbred MBAs joining the largest private equity shops command base salaries and bonuses as high as \$450,000. Add to that, of course, the real payoff: the equity. "More equity is flowing downstream to these new hires," says Brian Korb, a partner at New York executive search firm Glocap Search, co-publisher of the *2007 Private Equity Compensation Report*. "Especially for the all-stars. It's just like in sports."

There's just one hitch: There aren't as many private equity jobs out there as you might think. While many of the biggest funds will hire about 20% more B-school

grads this year, says Korb, demand for such jobs outstrips supply by a factor of about five to one. And the positions typically go to those with prior experience. A taste of just how cloistered this world is: The mighty Carlyle Group sent co-founder David M. Rubenstein (BW—Jan. 15) to Harvard Business School in October to woo finance stars over dinner at a gourmet restaurant. But Carlyle's 50% jump in hiring? It amounted to a mere seven spots, says human resources manager Annie Paydar.

You wouldn't pick up on the exclusivity by visiting a B-school campus, though. From the Wharton School to the University of Chicago's Graduate School of Business, it sometimes seems as if private equity is all anyone is talking and thinking about. MBA programs have always had private equity clubs. But B-schools at New York University, Dartmouth, and Columbia all report record memberships in these networking fests. At Wharton, nearly half the student body is a member of the private equity club. Conferences starring such legends as Blackstone Group chief Stephen A. Schwarzman sell out months in advance. And the schools have been falling all over themselves to add classes teaching everything from innovative dealmaking to the art of wielding "influence" within a firm.

With jobs tight and

INVITING BIGWIGS
Wharton students organize a Private Equity Conference

standards high, students are scrambling to prostrate themselves at the private equity altar. Many of Troy Barratt's buddies at Columbia Business School are already

set with sweet deals at consulting firms and investment banks. But when they go down to New York City's meatpacking district to swig Grey Goose and go dancing, "I wave goodbye and tell them to have a good time," says Barratt, co-president of Columbia's Private Equity & Venture Capital Club. He stays behind to set up coffee dates and e-mail contacts.

At Dartmouth's Tuck School of Business, six students were so desperate to snag private equity work that they passed on surfing vacations over winter break to fly to Mumbai, India, where they performed free labor for private equity firms looking for research. While there, the students knocked on doors and chatted up receptionists in the hope of getting in front of some private equity and hedge fund partners. "You have to find innovative ways to differentiate yourself," says one of the students, Shelly Rastogi.

Some see this as a leading indicator of yet another bubble. We know where the earlier stampedes to Wall Street and Silicon Valley ended. In five years, when these junior barons want to start their own funds, will the wash of money still be in private equity? Then again, what better school for a lesson in risk? ■

—With Jena McGregor in New York

THE STAT

\$450
THOUSAND

First-year compensation for top-flight talent at a big private equity shop (before equity), vs. \$300,000 at an investment bank.

Data: Glocap Search

CHRIS CRISMAN/WONDERFUL MACHINE

Advertisement

Outlook



A special excerpt from the journal of high-performance business

accenture

High performance. Delivered.

Going the distance How the world's best companies achieve high performance

After three years of original research, industry analysis and rigorous testing, Accenture has developed a compelling set of practical insights for companies that aspire to uncommon business success.

What does high performance mean, and how can organizations increase their chances of achieving it?

These have been the driving questions behind an ongoing Accenture program of original research that is now entering its fourth year. The program—which to date has included analysis of 6,000-plus companies, from which we identified more than 500 high performers—has been important not only in terms of our ability to help clients achieve success but also in the context of the larger marketplace of ideas: A 2005 *Harvard Business Review* survey recognized Accenture's High Performance Business research as one of the 10 most notable initiatives in the field during the past quarter century.

Several recent and well-known attempts to define business success have used criteria that, on closer inspection, begin to look suspiciously like popularity contests. We were determined to set forth a course of research based on data and metrics, not just reputation. Accordingly, the definition of “high performance” that we arrived at and tested was the enduring or sustained out-performance of peers, across business and economic cycles, often across generations of leadership, measured by widely accepted financial metrics.

High standard

This distinctive definition sets a very high standard. Many companies appear to be high performers in the short run, but decline quickly when business conditions turn against them. To be a true high performer, on the other hand, a company must thrive across economic and market disruptions. And high performance must be determined not by the use of a single measure but of a specific set of measures. To this end, we analyzed performance over five key dimensions: growth, profitability, positioning for the future, longevity and consistency.



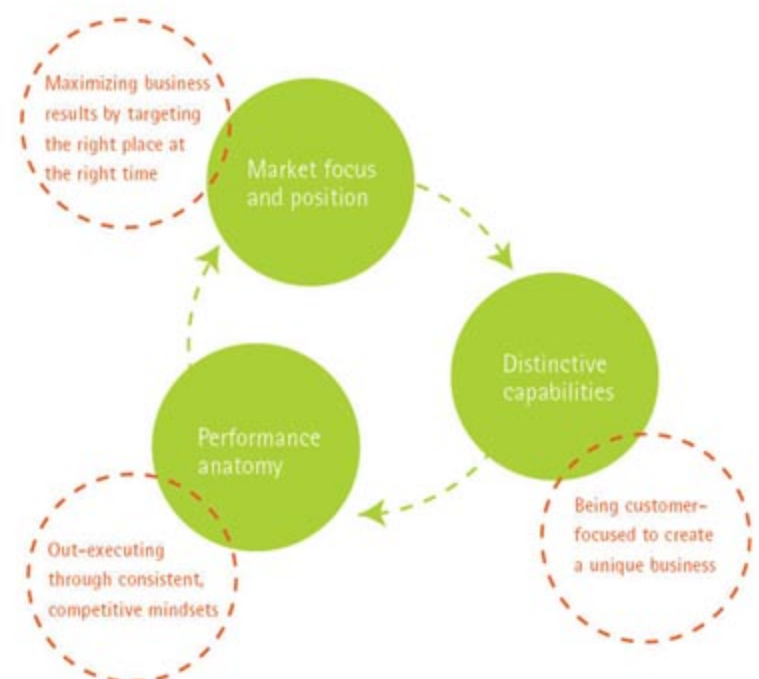
After analyzing the performance of leading companies, we were able to identify the common features of high performance—the attributes of excellence that all high performers display, regardless of industry. We called this common ground “competitive essence,” which, in turn, is comprised of three building blocks of high performance:

Market focus and position. High-performance businesses have remarkable clarity about where and how to compete. They always find where the market action is hottest. And when one market matures, high performers are ready with the next big thing.

Distinctive capabilities. High performers have a unique ability to build and connect capabilities in a way that drives significant value creation. They successfully translate big ideas regarding customer needs into a unique set of connected business processes and resources that cost-effectively satisfy those needs.

Performance anatomy. Organizational culture is a vital component of business success. It is also a concept that has been notoriously difficult to pin down. We have brought more specificity to this concept by developing

To achieve high performance, organizations need to get three things right.



Advertisement

an explanatory framework we call “performance anatomy.” This framework defines the essential mindsets that lead to the behaviors that determine how—and how well—an organization approaches tasks that are critical to business success.

The three building blocks have provided an essential means of organizing our insights about high performance. Subsequent industry and functional research has continuously enriched our understanding of the nature of these components.

Consider our research into how companies in various industries achieve the right market focus and position. For example, our study of health care providers found that to improve their performance, these organizations need to think differently about the markets they serve. One way this sector’s high performers have distinguished themselves has been by recognizing and exploiting growth opportunities in preventive health care and health maintenance. Analyzing high performance in this industry reinforced our judgment that being agile and having a view of multiple strategic horizons are key elements in achieving the most effective market focus and position.

Functional analyses of high performance

Along a track parallel to the industry analyses, Accenture’s global service lines took up the challenge of understanding the contribution that capability mastery in key functional areas makes to achieving high performance. (Our service lines consist of professionals organized internally along functional lines, including Strategy, Supply Chain Management, Human Performance, Customer Relationship Management and Finance & Performance Management, as well as cross-functional groups such as Information Technology.)

This article was excerpted from *Outlook*, the Accenture journal of high-performance business, and is part of a larger body of work—nearly 50 articles—published over the past three years. To read this and other *Outlook* articles on high performance in full, and to review the findings of our High Performance Business research, please visit accenture.com/research-articles

The central insight from these studies is that each high performer masters a highly select set of business processes and resources that we define as a “distinctive capability.” Unparalleled excellence in this set of functions constitutes a unique business formula for achieving competitive advantage. Lower performers, on the other hand, fail to achieve this mastery across a range of functions that is the price of admission to even above-average performance.

The next stage of the journey

In the next stage of our research, we will shine light on the paths organizations can and should take to arrive at high performance. We have already begun exploring how companies come to recognize the triggers of transformation—how they become committed to achieving high performance, how they set their course toward it and how they traverse one of the many possible paths to that destination.

To this end, we have embarked on a much deeper mining of our database of peer-set metrics. We also recently completed a cross-industry analysis of high-performance businesses versus their less successful competitors, uncovering several misconceptions about the nature of high performance and a number of reasons why every company can and should strive to become a high-performance business.

We began this journey three years ago with the stated belief that high-performance businesses are not simply born—they can be made. Our research has only deepened this conviction, as we have uncovered the evidence that companies can, through sheer force of will, propel themselves along the paths to high performance. We remain committed to identifying both the “what” and the “how” of high-performance business.

FAME AND FORTUNE

IT'S ALL DONALD, ALL THE TIME

For the self-described “hottest brand on the planet,” life is a nonstop media event

BY DIANE BRADY

DONALD TRUMP IS ABOUT to give me an exclusive look at his finances, but the phone is ringing off the hook. This time, it's a TV producer: “Is this the most handsome, the smartest, the most charismatic man in New York?” He's trying to book Trump on his show. But Trump is fresh from *The Today Show*, *The O'Reilly Factor*, *Access Hollywood*, *Larry King Live*. He's booked to do David Letterman. And there's a guy downstairs in the lobby of Trump Tower waiting to get a \$10,000 check that Trump offered him after he jumped on subway tracks two days earlier to save a man's life. The producer is begging. “I've got to get back to my real job,” says Trump with mock exasperation. He's clearly flattered.

Forget *The Apprentice*, which launched its sixth season on NBC on Jan. 7. The real entertainment right now is the Donald Trump show. The real estate mogul is taking on everybody from bombastic talk show host Rosie O'Donnell to author Tim O'Brien. He feels insulted, maligned. The common charge: that America's most famous billionaire isn't so good with money. O'Donnell snickered on TV that he had gone bankrupt. (He hasn't, although his public company did.) And Trump is suing O'Brien for citing, in his 2005 book, *Trump Nation*, three unnamed sources who pegged his net worth at as low as \$150 million. “I lost deals because of that,” complains Trump. O'Brien's lawyers say the suit is without merit.

The actual worth of his largely private



Trump seems wistful at the prospect of the Rosie feud fading

empire is, of course, hard to pin down. *Forbes* estimates it at \$2.9 billion. Trump has his chief financial officer, Allen Weisselberg, show me documents that put his net worth at roughly \$4.1 billion as of June, 2006, with assets totaling \$4.8 billion and liabilities of around \$700 million. That includes a valuation of \$370 million for Trump Tower which has a \$25 million mortgage—“and that's because there's no prepayment clause!”—as well as \$900 million for “club facilities and related real estate” such as 75 residential lots along the Palos Verdes Peninsula near Los Angeles. Then there's

the value of his name, which Trump calls “the hottest brand on the planet.” It's not Coca-Cola, but who else gets equity stakes in prime properties for putting up their name and little else?

Why this is the stuff of lawsuits is another question. By most sane assessments, Trump is rich. When he puts his name on bottled water, vodka, or a business suit, it sells. Trump buildings get a premium. People clamor to hear his speeches, for which he gets as much as \$1.5 million a pop. They buy his books. They even still watch his reality TV show, with 9.1 million viewers tuning into the Jan. 7 premiere.

The truth is that Trump likes combat, especially when it's played out in public. He's suing the town of Palm Beach, Fla., for \$25 million, with the money earmarked for “returning Iraqi vets” if he wins, because of the town's alleged harassment when it tried to get him to take down an 80-foot flag pole at his private club, Mar-A-Lago. “In life, you have fighters and nonfighters. You have winners and losers,” says Trump. “I am both a fighter and a winner.”

If fame could be converted to currency, few would doubt Trump's riches. And his media star has risen since his press conference last month to announce that he was letting Miss USA Tara Conner keep her title, despite her hard-partying ways. (Trump co-owns the pageant.) He even seems wistful at the prospect of his public riff with the prickly

O'Donnell fading into silence.

But there's work to do. Before subway hero Wesley Autrey comes to accept his check, Vice-President Rhona Graff asks Trump if he wants the media entourage surrounding Autrey to be allowed in, too. Is she kidding? “Bring them all in!” says Trump. Autrey's 6-year-old daughter comes over and sits on Trump's lap. “Would you like to help me run my business?” Trump asks. Cameras are clicking. The whole family gets in with Trump, and then he sits alone, striking a determined pose against the Manhattan skyline. Autrey and the gang of reporters leave. “That guy is amazing,” says Trump. The media moment is complete. “And what did it take? Five minutes?” Now, that's \$10,000 well spent. ■

PETROLEUM

BP FEELS THE HEAT

2006 was a horror, and problems remain. Will John Browne leave early?

BY STANLEY REED

EXECUTIVES AT BP'S HEAD-quarters on London's leafy St. James's Square are marking their calendars with grim resignation. In mid-January, a panel led by former U.S. Secretary of State James A. Baker III is due to release a long-awaited report on a series of mishaps at the energy giant. The study could further bruise BP's already battered reputation and might hasten the departure of CEO John Browne, until recently one of Britain's most celebrated corporate chieftains.

If the findings are as harsh as some BP insiders fear, it will probably refocus attention on Browne. In 11 years as CEO, he has transformed BP from a middling player into an intensely competitive money machine. Browne consummated five big deals in five years, including the \$62 billion takeover of Amoco in 1998 and a \$32 billion buyout of Arco in 2000. But in his quest to boost financial returns, Browne may have overlooked problems for which he has paid dearly. In 2005, a refinery accident in Texas City, Tex., killed 15 people, sparking a firestorm of lawsuits. Last June, U.S. regulators alleged that BP manipulated the propane gas market. Then in August, BP was forced to cut production in Alaska's Prudhoe Bay field after inspectors discovered corroded and leaking pipelines.

The Baker report is likely to criticize top management for being lulled into complacency. While safety statistics showed improvement, the report is expected to say not enough was done to

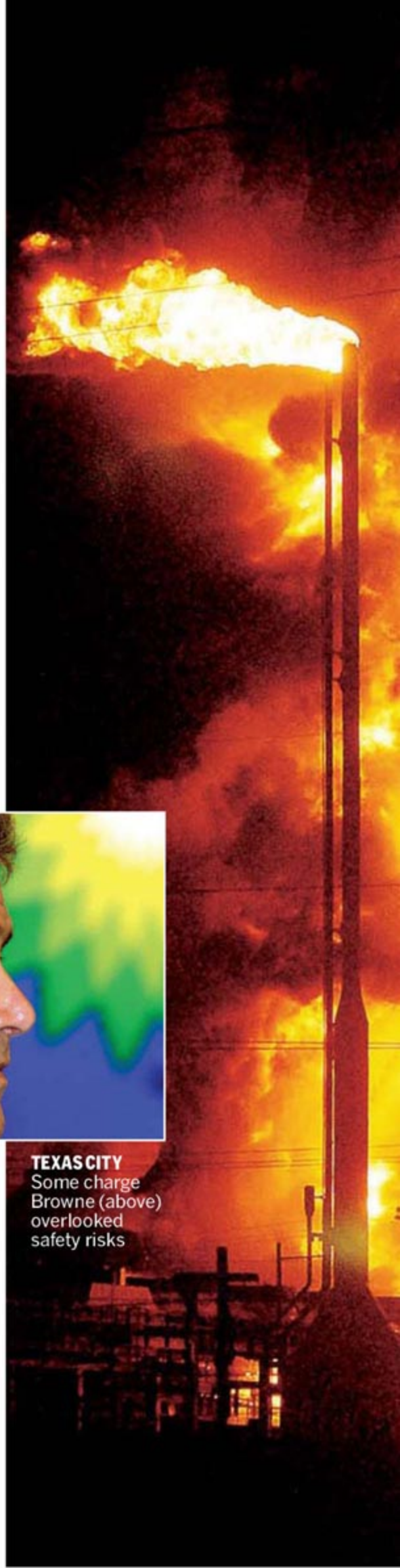
ensure correct procedures were followed. Browne might not disagree. "We learned a lot from what happened at Texas City," he says. "We are redoubling our efforts in safety processes."

The Baker panel, however, isn't Browne & Co.'s only upcoming worry. The U.S. Chemical Safety & Hazard Investigation Board (CSHIB), a federal agency that oversees refineries, has also been looking into the Texas City explosion and is expected to release its findings in March. As the inquiry has progressed, CSHIB Chairman Carolyn W. Merritt has emerged as one of the British giant's harshest critics. Among the shortcomings contributing to the Texas explosion, according to Merritt: failure to assess the impact of cost pressures on safety, and blindness to growing risks at the plant, which had already experienced three fatalities in 2004.

Merritt further faults BP for not learning the lessons of refinery accidents at Grangemouth, Scotland, in 2000. Following those incidents, BP was fined and criticized by the Scottish authorities for poor safety management, including inadequate maintenance. In its drive to increase production and slash costs, Merritt says, BP's leadership failed to communicate the importance of prudent work practices. "You can't assume that everyone understands



TEXAS CITY
Some charge Browne (above) overlooked safety risks





that safety comes first," says Merritt. She says she was so shocked by the lapses her investigators were turning up that she recommended that BP finance an independent investigation into safety and maintenance practices, which led to the creation of the Baker panel.

Executives privately say that problems were allowed to fester in a few of the less glamorous corners of the BP empire. Industry insiders say this may be partly due to Browne's view of the oil industry as a kind of three-dimensional chess game against rivals, particularly Shell and Exxon. "He has a restlessness; he is only interested in new ground," a close associate once said. Refining clearly didn't fall into the category of "new ground." It tends to be a low-margin business, and BP's focus has been keeping a lid on costs. BP executives say they recognized that the Texas refinery needed fixing, but the company did too little too late.

BP also commissioned its own study shortly after the Texas incident, which could hardly be called glowing. The 176-page report revealed a demoralized workforce that didn't follow the rules and where "safety knowledge and skills within management and the workforce were generally poor." The report identifies

numerous problem areas that could be tied to cost-cutting measures, including poor training and failure to replace a crucial safety device that was outmoded and "potentially hazardous."

tions. One source says Browne may have been guilty of "naivete" in trusting that managers in Texas and Alaska could achieve his demanding financial goals without compromising operations. Some put it more bluntly. BP "is a financial culture gone wild," says Bernard Picchi, an analyst at Wall Street Access in New York. "The company has been doing deals for the sake of doing deals with an almost maniacal focus on the bottom line, to the [detriment] of normal operating standards." BP shares traded on the London Stock Exchange are down about 17% in the past year—making it one of the worst performers among major European companies. BP's recent travails have stripped "the management premium out of the stock, which takes years to build up," says Jonathan Wright, an analyst at Citigroup in London. Brokerage Morgan Stanley forecasts that BP will earn \$21.1 billion in net income in 2006, a 7% decline from 2005.

TRICKY TASK

THE QUESTION NOW is whether Browne will stick around until his scheduled retirement at the end of 2008. For several months, the board has been mulling possible successors. The leading candidate is Tony Hayward, who heads up exploration and production, BP's most important businesses. But he could be hurt by recent disappointments such as BP's estimate on Jan. 9 that its fourth-quarter 2006 production would fall by 5%. Another possibility is Robert Dudley, CEO of TNK-BP, a joint venture in Russia that accounts for about 25% of BP's production. Dudley has pulled off

the tricky task of pleasing both top management and BP's Russian oligarch partners without running afoul of the Kremlin. As an American and an alumnus of Amoco, Dudley could also help bolster the company's U.S. credentials.

No matter who gets the nod, BP's continuing turmoil has sent a wake-up call to the company. The "mantra of more-for-less holds that we can get 100% of the task completed with 90% of the resources," Hayward said in a speech to employees in December. "But it needs to be deployed with great judgment and wisdom. Otherwise you run into trouble." ■

BP's Trail of Woe

Accidents and investigations have shaken investor confidence, helping push the giant's shares down by 17% in the past year:

MARCH, 2005

An explosion at a refinery in Texas kills 15 people, spurring investigations and lawsuits.

JUNE, 2006

U.S. regulators say BP manipulates propane prices. Other inquiries target its oil and gasoline trading.

AUGUST, 2006

Production is halved at BP's Prudhoe Bay oil fields in Alaska after pipeline corrosion and a spill.

JANUARY, 2007

Worries over potentially harsh findings by Baker's panel depress company morale.

Yet Browne's intense drive for results combined with BP's entrepreneurial culture may have also played a role in the company's woes. While Browne puts his managers through tough, detailed reviews each quarter, BP is less of a command-and-control company than rivals. It operates with a decentralized structure designed to reward individual initiative, and managers are expected to use their own judgment in running their opera-



CARS

EVEN TOYOTA ISN'T PERFECT

A raft of recalls lately has it scrambling to safeguard its reputation for quality

BY IAN ROWLEY

TOYOTA WAS BUILT ON details. After decades of study and refinement, the company has developed thousands of pages of guidelines that lay out exactly what needs to be done at every step of the automaking process. That attention to the nitty-gritty has helped create an industrial machine that's unparalleled in building problem-free cars and trucks.

But growing numbers of flaws have started to tarnish Toyota Motor Corp.'s reputation for quality. Since 2004 the automaker has had to recall 9.3 million vehicles in the U.S. and Japan—its two biggest markets—up from 2.5 million in the previous three years. The problems got so bad that, in July, Toyota CEO Katsuaki Watanabe felt obliged to bow deeply in apology.

Given Toyota's obsession with details, it's no surprise that it would ask someone who knows how to focus on the small stuff to fix the problem. In June, Toyota

ordered former Europe chief Shinichi Sasaki back to Japan to help get a grip on the issue. The 36-year Toyota veteran has spent three decades working to ensure glitch-free production. Although Toyota has long had a quality chief, Sasaki is the first person to do the job full-time. "My responsibility is to tell all Toyota employees the quality aspect of their jobs," says Sasaki.

Toyota chieftains say the company is making progress. In December, Executive Vice-President Masatami Takimoto said that when it comes to recalls, "the worst is now over." And Watanabe, while again apologizing for recent faults in vehicles, said Toyota is "right on track in ensuring good quality."

Sasaki's task is made more difficult by Toyota's rapid growth. In recent

FINAL INSPECTION

At the Tundra pickup assembly line in San Antonio

years, the company has opened at least two overseas plants annually, and this year

it's poised to overtake General Motors Corp. as the world's No. 1 carmaker. Today, Toyota makes nearly as many vehicles outside Japan as it does at home, meaning its cadre of Japanese engineers is no longer big enough to train all the new workers at foreign plants. To make up for the deficit, Toyota last year opened new "Global Production Centers" in Kentucky, England, and Thailand. These facilities, modeled after one established in Japan three years ago, teach trainees the Toyota way in tasks such as welding and painting.

GARAGE REPORTS

ANOTHER NEW INITIATIVE: better record-keeping. In years past, Toyota maintained repair data only on vehicles under warranty, which meant it missed glitches that popped up later on. Now, Toyota shops in Japan provide a full report on repairs to cars of any age. The quality chief is also asking suppliers to share information and use common parts. Denso, Aishin Seiki, and others have just started using one design for voltage stabilizers for electronics in Toyota's cars.

More important is designing quality into cars in the first place. To give designers extra time to get things right, Toyota has tapped the brakes on the introduction of new models. For instance, the new generation of Corollas, already on sale in Japan, has been held back for a year in the U.S. to ensure that American workers have the time to learn how to build the model without glitches.

There's clearly room for improvement. In July, the company recalled

157,000 Tundra pickups because the trucks lacked front-seat anchors for child safety seats—a feature required in any vehicle that has a switch to turn off air bags. (When deployed, air bags can kill children riding in the front seat.) Toyota, it seems, simply forgot about the anchors when designing the trucks. It's the kind of oversight Sasaki vows to spot long before any recall notices need to be sent out. "Every decision at every stage," he says, "must be done properly." ■

THE STAT

9.3
MILLION

Toyota's recalls in the U.S. and Japan since 2004, up from 2.5 million in the previous three years.

Data: Toyota, National Highway Traffic Safety Administration

YOU'RE STILL WORKING. IS YOUR RETIREMENT ACCOUNT?



**TRANSFER
YOUR 401(k)**
Into a rollover IRA
No fees
No minimums



**UNBIASED
ADVICE**
From our
Financial Advisors¹

Get started with 50
commission-free trades²



Click



Call



Visit

(800) 998-8490
etrade.com/retirement

1. Financial Advisors provide recommendations on mutual funds, bonds, preferred stocks, closed-end funds, structured products—including equity linked CDs, and asset allocation. Customers are required to complete additional forms and documentation in order to receive such services. Different commission structures may apply and in some cases may be less or more than the rates posted on the website.

2. Commission-free trade offer applies to new E*TRADE Securities Traditional, Roth, or Rollover IRAs. Not eligible are investment club, business trust, custodial, or other retirement accounts, E*TRADE Bank accounts, and any accounts not identified as valid. Excludes current E*TRADE Securities customers, E*TRADE FINANCIAL Corp. associates, and non-U.S. residents. The new account holder will receive a maximum of 50 free trade commissions for stock or options trades executed within 30 days of the opening of the new account. You will pay the standard commission rate on all trades at the time of the trades (plus all applicable options contract fees) and your account will be credited the standard commission rate per stock or options trade within eight weeks of qualifying (excluding options contract fees). Accounts must be opened by December 31, 2007 to qualify for this offer.

Securities products and services are offered by E*TRADE Securities LLC, Member NASD/SIPC.

System response and account access times may vary due to a variety of factors, including trading volumes, market conditions, system performance, and other factors.

© 2007 E*TRADE FINANCIAL Corp. All rights reserved.

GLOBALIZATION

OUTSOURCING HEADS TO THE OUTSKIRTS

GramIT brings tech-services jobs to rural areas—and transforms villagers' lives

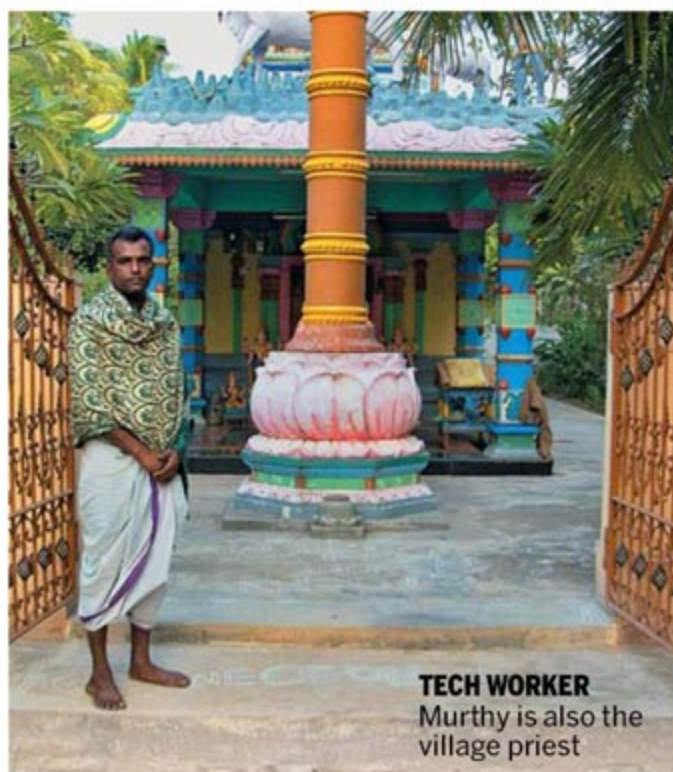
BY STEVE HAMM

THE VILLAGE OF ETHAKOTA in India's Andhra Pradesh state hardly looks like a place that has been transformed by the Information Revolution. To get there, you take a 10-hour train ride from Hyderabad, the nearest big city, then drive an hour on narrow roads past rice paddies, coconut groves, and ponds teeming with prawns and crabs. The village itself is a collection of simple brick houses and thatch-roof huts. Yet in a tidy office shaded by 30-foot-tall palms, 50 young people sit at PCs connected to the Internet via a long-distance radio link, doing business process outsourcing (BPO) tasks such as checking expense account receipts for Indian corporations and arranging job interviews for applicants in distant cities.

They're working for GramIT, a 16-month-old nonprofit that's seeking to transplant India's tech services boom to some of the country's 600,000 villages. Workers in Ethakota earn a fraction of what the outsourcing troops in Bangalore do, but they're not complaining. Srinivas Ruddireddy makes twice as much money arranging car services online for people in Hyderabad as he does from the two-acre rice plot he tends in the early morning. He now plans to send his 4-year-old son to private school. "My lifestyle has entirely changed," says the 30-year-old. "But I'm able to stay in the village."

So far, GramIT operates in three villages in Andhra Pradesh. But the group hopes soon to expand to many more. "If work can shift from the U.S. to a city in India, why can't work

The fledgling nonprofit is proving itself one community at a time



TECH WORKER
Murthy is also the village priest

from cities in India shift to villages in India?" says Ramalinga Raju, chairman of tech services provider Satyam Computer Services Ltd. and founder of the Byrraju Foundation. He set up the group in 2001 to fund projects, such as GramIT (*gram* is the Sanskrit word for "village"), aimed at transforming the rural economy.

Taking outsourcing to the countryside makes sense. About 70% of India's 1.1 billion citizens—most of them subsistence farmers who barely scrape by—live in villages. Moving service jobs to rural areas provides work for the unemployed and could slow migration to the crowded cities. Entry-level GramIT employees, all with at least three-year college degrees, earn

\$800 a year, compared with \$2,000 to \$5,000 annually for an employee at an urban outsourcing shop. And because there are few other good jobs in these communities, GramIT's centers see just 5% annual turnover—dramatically better than the 60% rate in places such as Bangalore.

SCALABILITY

SATYAM HAS SIGNED on as the outfit's biggest customer and says the operation does good work. Hoping to cut back-office costs in half, the company has farmed out human resources and accounting jobs to GramIT; now it's reviewing other processes it might hand

off. Although the villagers speak little more than basic English, it's sufficient for the jobs they're doing, says Surya Gadiraju, vice-president for technical development in Satyam's e-support operation. "It took just a couple of weeks to get them up to speed and quality," he says.

The concept isn't an easy sell. "It would be very hard to achieve international standards for service and to scale up the operations" of village-based outfits, says Azim Premji, chairman of India's Wipro Ltd., which has 15,000 BPO workers scattered across India. That's why GramIT is starting small and focusing initially on the Indian government and domestic

corporate clients. "There's a fair amount of skepticism about the abilities of the villagers to provide quality services," says J.K. Manivannan, the Byrraju partner in charge of GramIT. "But if we show it can be done, others will follow." He has already gotten nibbles of interest from some global corporations.

GramIT is clearly having a profound effect on Ethakota. One beneficiary is K.V.S. Murthy, who was forced to leave home to find work a few years ago. Now, he's back in the village and working at GramIT. The income from his outsourcing job has allowed the 32-year-old to take up a revered but low-paying role in the community that has been passed down from generation to generation in his family—that of the village's Hindu priest. Murthy's good fortune won't assure GramIT's success, but you've got to admit the karma is good. ■

Our passion for tax services can lift your spirits, too.

You need to evaluate and manage your company's tax exposure. Your job's not easy. Grant Thornton understands that.

We know that in tax matters, robust analysis and well-developed documentation give you the power to act today...and plan for tomorrow. We apply technical expertise and industry-specific knowledge to help you manage financial statement obligations and manage tax exposure at local, state, national and international levels.

Passion for serving our clients, technical expertise, and partner involvement have been the hallmark of Grant Thornton in the U.S. for more than 80 years. Plus, you get the benefit of Grant Thornton International member firms in 112 countries around the world.

Give Mark Stutman a call today at 202.861.4155 or contact us at www.GrantThornton.com.

Find out how it feels to work with people who love what they do!



*Mark Stutman
Managing Partner-Tax*

Grant Thornton 

A passion for the business of accounting®

- Federal Tax Services
- State and Local Tax Services
- International Tax Services
- Compensation and Benefit Services
- Family Wealth Planning

Outsmarting





the Market

Behind Barclays' quest to build a world-class team of academic quants that systematically does the impossible. **By Anthony Bianco**

IT CAME AS NO GREAT SURPRISE that Richard G. Sloan took a leave from his tenured position at the University of Michigan's business school last summer to join an investment firm. Wall Street has stepped up its hiring of academics in recent years, and the 42-year-old Sloan is one of accounting's bona fide stars. But Sloan's explanation of why he left academia for Barclays Global Investors (BGI) is startling. "I just felt that BGI was getting ahead of me," he says. "I came here because this is where the leading edge in my area of research is now."

As one of more than 100 PhDs in BGI's employ, Sloan reinforces a cadre of highly credentialed brainpower that no university finance or economics department in the land can match. San Francisco-based BGI is descended from a firm founded in the 1960s, but it has parlayed its prowess in the field of quantitative investing into an astounding recent growth spurt. BGI has added \$877 billion in funds since 2002, boosting its assets under management to \$1.62 trillion and enthroning it above State Street, Fidelity, and Vanguard as America's largest money manager.

Barclays Global Investors' original claim to fame was invent-

ing the index fund, so it is fitting that the bulk of the wealth this prototypical "quant" shop manages—nearly \$1.1 trillion—is invested in vehicles that replicate the Standard & Poor's 500-Stock index and other indexes. However, Sloan and the other brainiacs that BGI continues to hire away from elite institutions around the world are not preoccupied with devising clever new ways to match market returns. Rather, they seek to do something that the efficient-market theories on which the firm was founded held to be impossible: to systematically beat the market.

Hard Data vs. Heroics

IN ITS OWN QUIETLY METHODICAL fashion, BGI has indeed topped many indexes with remarkable consistency by overweighting its investment in certain of their component securities—a conservative quant technique known as "tilting" or "enhancing." In fact, every one of BGI's 19 principal stock market tilt strategies has outpaced its benchmark over periods ranging from 4 to 20 years. Add the gains produced by more

aggressive vehicles such as hedge funds, and over the last five years BGI has generated a colossal \$19.9 billion above the market return—or “alpha,” in investment parlance—for the 2,800 pension funds and other institutional investors that are its clients.

Long dismissed on Wall Street as a think tank that runs money on the side, the firm and its eggheads have also engineered a tenfold rise in profits since 2001. BGI, a subsidiary of British bank Barclays PLC, is likely to take in more than \$1.6 billion in pre-tax profits this year, contributing to its parent company’s much promoted allure as a takeover target. BGI, which began as the investment arm of Wells Fargo Bank, was acquired by Barclays in 1995 for \$443 million—a great bargain, as it has turned out.

“When we first started, we were a bunch of guys who stared at our shoes at cocktail parties,” says Richard C. Grinold, a former University of California at Berkeley finance professor who is BGI’s senior research guru. “But now the rest of the world has to react to us.”

BGI’s ascendance highlights the coming of age of quantitative investing, which seeks to purge money management of human fallibility through the rigorous application of the scientific method. “The goal is to replace heroic personalities contending in an atmosphere of greed and fear with compelling hypotheses subjected to hard data,” declared Grinold and longtime colleague Ronald N. Kahn in a recent manifesto.

Fine, but how exactly does Barclays go about outsmarting the markets on such a scale? To find out, *BusinessWeek* interviewed scores of BGI’s alpha-seeking males and females, sat in on a brainstorming session of its Asian equities research group, and huddled with a portfolio manager on its trading desk as she put the firm’s “portfolio optimizer” smoothly through its high-tech paces.

This deep look into the workings of the planet’s largest quant shop abounds with informative lessons for the average investor. Unfortunately, though, they add up to this simple, humbling imperative: Get thee to an index fund. Now.

You and I can no more hope to do what BGI does than we can to rival such famously heroic stockpicking personalities as Warren Buffett and Peter Lynch. Quant investing BGI-style requires fluency in applied mathematics as well as access to the prodigious computing power needed to continuously crunch the numbers for 10,000 stocks and 2,500 debt issues and execute thousands of trades a day. With 2,640 employees spread among 11 offices around the



RECENT HIRES

The University of Michigan’s Sloan and Wharton’s Richardson are both on leave

world, BGI is the largest quant manager by a wide margin.

Much ink has been spilled over the rapid growth of hedge funds and their increasingly aggressive alpha-seeking tactics. Meanwhile, a less publicized but equally telling shift is taking place at the opposite end of the risk-reward spectrum, as the soaring popularity of exchange-traded funds (ETFs) breathes new life into indexing, BGI’s original forte. In the U.S. alone, ETF assets under management topped \$450 billion in 2006, up from \$102 billion in 2002. BGI dominates the ETF business with a 60% market share, according to Morgan Stanley.

The explosive emergence of both risk-intensive hedge funds and risk-averse ETFs can be explained by a single concept that is transforming the big-money world of institutional investing: alpha-beta separation. The basic idea is to lock in a market return (the beta part) on one end with low-cost index funds of one sort or another. On the other, pay up to put money into “alternative strategies” run by managers with a proven ability to beat the market (the alpha part).

A recent study by McKinsey & Co. found that by the end of 2005, “higher alpha and cheap beta products” accounted for 50% of all institutional assets under management, double the figure in 2003. “The warning bells have already begun to toll for many traditional firms not willing to depart from their business-as-usual approach,” McKinsey noted. Investment management consultant Casey, Quirk & Associates concurs, predicting that nearly half of the world’s 50 largest money management firms “are not going to be around in their present form for much longer.”

As the inventor of indexing, BGI has been separating alpha and beta since its founding. “The world has come BGI’s way,” says John F. Casey, Casey Quirk’s chairman and a longtime BGI

BGI’s Bonanza

America’s biggest money manager has added \$877 billion since 2002

ASSETS UNDER MANAGEMENT (IN BILLIONS)				
	ACTIVELY MANAGED	INDEX*	OTHER	TOTAL
2000	\$124	\$628	\$51	\$803
2001	126	590	53	769
2002	129	578	39	746
2003	217	735	118	1070
2004	281	919	162	1362
2005	340	1006	138	1513
2006**	369	1057	197	1623

*Includes exchange-traded funds (ETFs)

**As of June 30

Data: Barclays Global Investors

One weak spot: The quants' rational method makes them vulnerable when irrational manias and panics sweep the markets

champion. "I don't think a lot of clients consciously decided that they wanted to shift to quants so much as they wanted to go with someone who knows exactly what risks they are taking and will do what they say they will do. And that's BGI."

In traditional circles, quant has been derided as "black box" investing for its reliance on computer models comprehensible only to the double-domes who created them. The black box survives today in the more mystifying form of investing techniques derived from fuzzy logic, neural networks, Markov chains, and other nonlinear probability models.

As epitomized by BGI, though, modern quant investing is grounded in the same economic fundamentals that preoccupy mainstream analysts, though quants amass much more data and massage it more systematically than anyone else does. Another key difference is that quants ignore the story behind the numbers. The whole sprawling human drama of business is of no interest to Barclays researchers, who never venture out to call on a company or tour a store or a factory. If a thing cannot be measured and factored into an investment hypothesis for testing against historical data, BGI has no use for it.

Quants also are far more mindful of risk, as measured mainly by price volatility. Traditional portfolio managers tend to heighten risk by concentrating their investments in a relative handful of companies that they believe will beat the market averages over the long run. Instead of angling to get in early on the next Wal-Mart or Microsoft, BGI spreads its bets across a broad market swath, frequently trading in and out to exploit small pricing anomalies. The firm's \$19.9 billion in alpha represents just 1.64% above the market return, on average.

Quant is no investing panacea, however. Historically, its practitioners have fared better in periods when value trumps growth and have tended to flounder at the fringes of the markets, where data tend to be spotty. Quant's by-the-book formalism and dependence on historical data also leave its devotees particularly vulnerable to the manias and panics that disrupt markets at irregular intervals. The classic example is Long-Term Capital Management, a fixed-income superstar that boasted two Nobel Prize winners on its board. Highly levered LTCM imploded in 1998 under losses of \$4.6 billion after the Russian government defaulted on a bond issue, disrupting credit markets worldwide.

It was another catastrophe—the pricking of the tech bubble in 2000—that marked the beginning of quant's rise. A trickle of new funds from safety-minded institutional investors grew into a torrent as BGI, LSV Asset Management, Enhanced Investment Technologies, AQR Capital Management, and other top quant firms posted stellar returns in the buoyant, value-tilted markets of recent years. Each of the three firms that sit atop the latest hedge-fund rankings is a quant master of long standing: Goldman Sachs, Bridgewater Associates, and D.E. Shaw. (BGI ranks fifth, with \$17 billion in hedge fund money.)

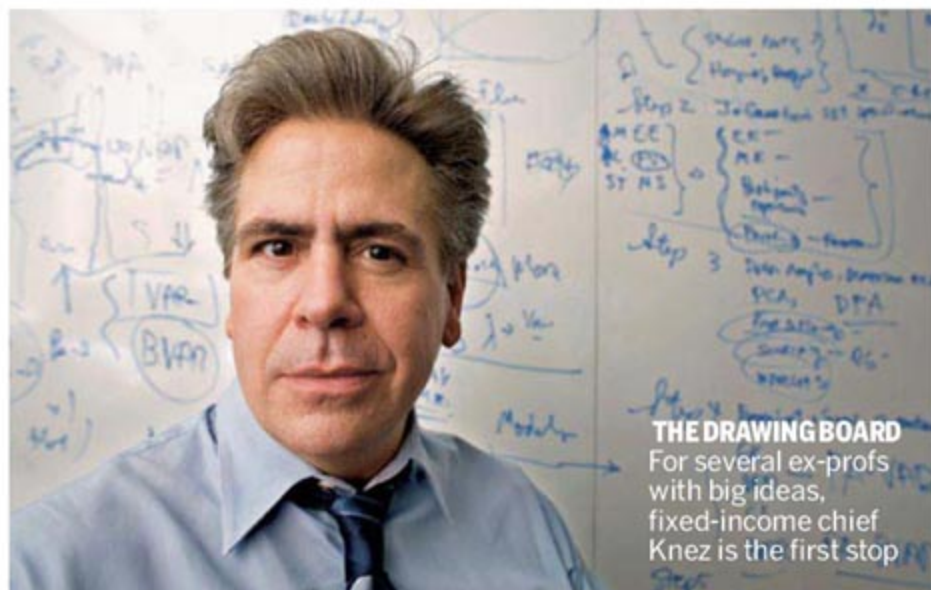
By contrast, the typical active money manager has struggled. Over the last five years the S&P 500-stock index has outperformed 71% of large-cap funds, the S&P MidCap 400 has topped 83.6% of mid-cap funds, and the S&P SmallCap 600 has bested 80.5% of small-cap funds, according to Standard & Poor's, a unit of The McGraw-Hill Companies, which also owns *BusinessWeek*.

Student Union Chic

BGI GOES TO GREAT LENGTHS to limit its exposure to human error by using computer technology to automate every investment process it can, including trading. And yet the ambiance at BGI's headquarters, in an office tower a block south of Market Street in downtown San Francisco, is much more coffee-stained grad school seminar room than antiseptic computer lab. For if the only investment ideas that count at BGI are those that can be expressed in software code, they usually begin as a flash of insight in the mind of someone like Xiaowei Li, one of BGI's 140 research officers.

Nov. 17, 2006, saw a milestone in Li's nascent career as an alpha hunter: her first presentation to BGI's Asia equities research group. The China-born Li brought impeccable credentials to the task, including degrees from Princeton University (a master's in economics and public policy) and Stanford University (a PhD in economics).

Li is the leader of a project analyzing non-Japanese Asian banks. The object is to identify statistical factors—or "signals," in quant speak—to help BGI determine which of the many banks traded



THE DRAWING BOARD
For several ex-profs with big ideas, fixed-income chief Knez is the first stop

RICHARD MORGENSTEIN

in Hong Kong, South Korea, Indonesia, India, and other countries are undervalued in the stock market and which are overvalued. A signal highlights a market inefficiency; good ones are rare and often prove a juicy source of alpha.

Li, who had just returned from a swing through southeast Asia that included stops in Hong Kong and Macao, began her presentation by passing around a list of 25 potential signals. Li's ideas were sketchily annotated, but that was to be expected at this early stage. The meeting was just an inaugural brainstorming session, not a PhD thesis defense.

Gathered around a table in a small conference room on the 28th floor of BGI headquarters were a half-dozen of Li's peers, plus her manager and the co-heads of the overall Asian research effort, Ernie Chow and Jonathan Howe, both of whom joined BGI in 1999 and were the fortysomething graybeards of the group. Everyone in the room had either a PhD or a master's degree in financial engineering. The disciplines represented included physics, applied mathematics, and operations research, as well as finance and economics.

Li stood throughout most of the two-hour meeting, the better to scrawl phrases and formulas on the floor-to-ceiling whiteboard behind her. The discussion was highly technical and surprisingly lively. Who knew pre-provision operating expenses could be such a hoot? Chow and Howe took the lead in questioning Li, raising their voices only to talk over subordinates who on occasion were a bit overeager to comment.

Li held her own throughout, demonstrating impressive command of Asian banking arcana even as she acknowledged the limits of her knowledge, and smilingly accepted suggestions for further research. Afterward, Howe described the session as "pretty productive," even though the group hadn't even made it halfway through Li's list.

Li's bank study is one of a dozen projects in Asian equities alone. At any given time, 50 to 60 more alpha quests are in the works across BGI's other research areas: U.S. and European equities, fixed income, and global macro, which handles cross-border investing, currencies, and commodities. In 2006, Barclays spent \$120 million—10% of its total budget—on research. In the scale of its commitment to commercial innova-

BGI uses its connections at top universities to get a look at promising academic research before it starts to circulate

tion through research and development, BGI is the Bell Labs of high finance.

"What's really distinctive about BGI is the research effort. They throw a lot of resources at getting the best people and the best systems they can," says David F. Deutsch, chief investment officer at the San Diego County Employees Retirement Assn., a BGI client that ranks as one of the U.S.'s top-performing public pension funds. "What they do has to work, and it also has to speak to guys like me, who think about this stuff but who are not in the trading pits every day."

Like other quants, BGI regards its investment signals as trade secrets and guards them accordingly. Here, the traditional academic imperative of publish or perish has been turned on its head: If you publish (or otherwise spill the beans), you will perish.

BGI comes up with scores of new signals every year, most

of which are refinements of existing strategies rather than brand new, market-thumping ideas. The global macro group came up with a notable example of the latter by devising a set of signals that can pinpoint the timing of an economy's pivot from recession to expansion. By buying a country's stocks and shorting its bonds before its recovery was generally recognized, BGI's Global Ascent fund was able to generate total alpha of 4% in 2005 and 2006. To date, BGI has used this strategy in 15 countries and plans to apply it to perhaps 10 more.

BGI's researchers seek inspiration indiscriminately. "We will beg, borrow, or steal ideas from wherever we can," says Kenneth F. Kroner, a 12-year veteran who heads BGI's global macro area. "Richard [Grinold] likes to say that we have no pride whatsoever."

BGI has a line or two into every top research university and makes determined use of its connections to get the most promising academic research before it starts to circulate. Every year, BGI brings in a couple dozen leading scholars to present their latest work in the sort of disputatious seminars that are a staple of campus life. Professors are generally flattered by the attention and open to remunerative arrangements, including paid consulting gigs. Of course, the best way to appropriate an academic's leading-edge insights is to pay his salary.

Richard Sloan's hiring was the culmination of an 11-year relationship with BGI. He was an unknown assistant professor at the Wharton School when he made his breakthrough discovery of the so-called accruals anomaly in the early 1990s. The investment implications of Sloan's findings were so momentous that they were generally presumed to be erroneous. The young professor was unable to persuade an academic journal to publish his findings until 1996, about a year after BGI invited him to San Francisco for a private seminar. "BGI was the first place to really pick up on my work," Sloan says.

What he found was that the stock market is slow to differentiate between good old cash flow and noncash accruals, such as changes in reserves for inventory levels and bad debts. By buying stocks of companies with the highest-quality earnings and shorting those most dependent on accruals, an investor could lock in 12% alpha. Analytical refinements noted in a second paper that was presented first at BGI in 2000 (and finally published in 2005) boosted the excess return to a gaudy 20%.

Sloan's assertion that BGI now sets the pace in earnings-quality research annoys many academics in the field. They include Russell J. Lundholm, who chairs the accounting department at the University of Michigan at Ann Arbor's Ross School of Business, from which Sloan is on leave. "I can't believe the cutting edge is at BGI or any other firm," says Lundholm, who still jogs with Sloan when he's in town.

Of course, Lundholm doesn't know exactly what BGI knows,





because not even Sloan was allowed a glimpse inside the firm's quality "bucket" until he became an employee. Inside he found 15 specific signals, including "a bunch of things that were new to me," Sloan says. Even as individual signals have come and gone, earnings quality has been BGI's single richest source of alpha over the last decade.

One of Sloan's closest academic colleagues, fellow Aussie Scott Richardson, joined BGI about the same time. Richardson took a leave from Wharton, where he is an assistant professor of accounting, to be BGI's director of U.S. credit research. In his first weeks there, he compiled a long list of highly specific research ideas for his boss, fixed income chief Peter J. Knez. "These are just things I see because I'm coming in from the outside and am closer to current academic research," he says.

Whatever a new idea's provenance, as a rule, BGI will not deem it portfolio-worthy unless it first passes four tests. In BGI speak, they are collectively known as SPCA, for Sensible, Predictive, Consistent, and Additive.

To start, a researcher must construct a hypothesis that makes basic economic sense. For Xiaowei Li, this means converting her list into a one-page "sensibility document" capable of persuading the firm to authorize the expense of empirical testing. Evidence must be assembled showing that the signal not only outperformed in the past but that it can predict future above-market returns. The opportunity to realize these returns must be consistently available, even in volatile markets. Finally, the idea cannot be an old notion repackaged to seem new but must add insight that is truly fresh.

Surprisingly, it is the initial criterion—sensibility—that is hardest to meet, with 40% to 50% of proposals failing to make the grade. "The key is the S factor," says Kahn, who has a PhD in physics from Harvard. "It's so easy to be fooled by the data into mistaking patterns in the data for a sensible hypothesis."

Sponsors of proposals authorized for testing usually spend a few months sifting data and assembling a so-called SPCA report of 20 to 25 pages. It is reviewed both by a group of senior research colleagues and a third-party referee. About a third of all refereed proposals are rejected.

BRAINSTORMING Li leads a project to see which non-Japanese Asian banks are overvalued or undervalued

quantdom, the question of whether alpha exists as a finite market commodity is a topic of debate. Unquestionably, though, the shift of vast sums into quant hands is making alpha more elusive. "The fact that there are more and more quants chasing the same sort of factors will shrink the alphas from those factors gradually," acknowledges Robert C. Jones, who runs Goldman's equity quant effort.

BGI's top executives seem acutely aware that galloping growth could undermine the rigor and integrity of the firm's investment methods. Having more than tripled assets under active management, to \$370 billion, over the past three years, BGI has closed many of its market-beating strategies to new investment, at least temporarily.

This doesn't mean, though, that Barclays is backing away from its pursuit of advantage through research. BGI's capital spending rose 30% in 2006 and "will only slacken if we run out of new ideas," says CEO Blake Grossman, who started at the firm in 1985 as a portfolio manager. "A half-dozen years ago, a couple of guys could make a difference. Now it takes dozens of people and terabytes of data to be competitive."

Recently, Duke University's David A. Hsieh, a leading hedge fund scholar, theorized that only \$30 billion in alpha is realizable annually from the \$30 trillion market value of all stock and bond markets worldwide. It was intended as a very rough estimate, but if BGI is extracting \$4 billion to \$5 billion a year, what chance do the rest of us have to top the averages?

Think of Barclays Global Investors as the Wall Street equivalent of one of those giant factory trawlers that have revolutionized commercial fishing. This super-quant methodically cruises global markets, sucking alpha from the depths while everyone else drifts about in rowboats, corks bobbing pathetically atop waters that are nearly fished out. ■

Once approved, a new signal is added to one or more of the computer models BGI uses to forecast returns (or expected alphas) for each of the 12,500 stocks and bonds it tracks. BGI portfolio managers turn such strategies into investment portfolios for clients by running its return forecasts through an "optimization engine" that takes into account numerous risk factors as well as trading costs and spits out a trade list in the form of an Excel spreadsheet. The whole process takes 10 minutes or less.

How much bigger can BGI get? The short answer: a whole lot—and therein lies the danger.

As the world's largest indexer, BGI appears unassailable on the beta side of the great divide that is transforming institutional investing. Remarkably, the firm's iShares brand has taken a growing share of the ETF business even as it has grown by leaps and bounds.

But if the index business is congenial to scale, the history of active management is littered with the corpses of firms that let their market-beating prowess attract more money than they could handle. Within

Sweet **REVENGE**

The power of retribution,
spite, and loathing in
the world of business

BY JENA MCGREGOR





WHEN IT COMES TO LARRY ELLISON, TERRY Garnett does not mince words. "I do hold grudges," Garnett says. "Am I motivated by that? Absolutely." A former Oracle Corp. senior vice-president, Garnett spent the early 1990s traveling around the world with Ellison, Oracle's CEO. They hobnobbed with the likes of media moguls David Geffen and Barry Diller as the company tried to become a player in the interactive-TV business. Garnett and the software billionaire were so tight that Ellison even invited him and his wife to go along on a vacation to Kyoto in 1994. That year marked the 1,200th anniversary of the founding of Japan's former imperial capital, a meaningful occasion for Ellison, a passionate Japanophile.

Together, he, Garnett, and four others made the pilgrimage along the cherry-blossom-lined Philosopher's Walk to the famed Ginkakuji Temple.

But what came next led to the bad blood that Garnett still tastes more than 12 years later. Within weeks of their return from Japan, Ellison summoned Garnett to his office. He scrapped the interactive-TV startup the two were planning and, Garnett claims, fired him without giving a clear reason. "It was pretty clinical," he recalls. "I tried to keep composed."

Feeling numb, Garnett returned to his office, not more than 30 feet away, and packed up. Afterward, he spent weeks trying to understand why he had been fired. Garnett later sued Ellison, accusing him of unfairly firing him, but then he dropped the claims. (Oracle officials declined to comment, but their reply to

Garnett's suit cites his "declining productivity.") Brimming with anger, Garnett made a vow to himself: "There will be a day of reckoning." Today he is acting CEO of Ingres Corp., a software upstart that's gunning to grab market share from Oracle.

Ask CEOs what drives them, and they'll talk about success, personal fulfillment—a few will even admit to be driven by the desire for money and power. But Garnett's professed appetite for payback is a motivation rarely leaked from executives' on-message lips. "It's one of the great undiscussables," says Kenneth N. Siegel, a Los Angeles psychologist and coach to senior executives. "Just as you don't talk about lust in the executive suite, you don't talk about revenge as a significant motivator for success. But it clearly is."

In our euphemism-laden, numbers-driven, "it's just business" corporate environment, it's easy to forget that the desire to get even is one of those primal human impulses that lurks behind executive behavior. Revenge is at least as old as the Bible ("Vengeance is mine," saith the Lord) and provided a plot line for many a Shakespearean tragedy, but it's also written into the script of many of the most memorable corporate dramas. And in today's hypercompetitive business world, as the spiraling rate of executive turnover leaves behind a trail of ousted managers and as leaders marred by recent corporate scandals try to restore their reputations, it's a subtext of many of the most dramatic recent business stories, too.

Exhibit A: The Hewlett-Packard Co. leak investigation. Yes, maverick board member and wealthy venture capitalist Tom Perkins did the world a service in alerting government officials

REVENGE is "one of the great

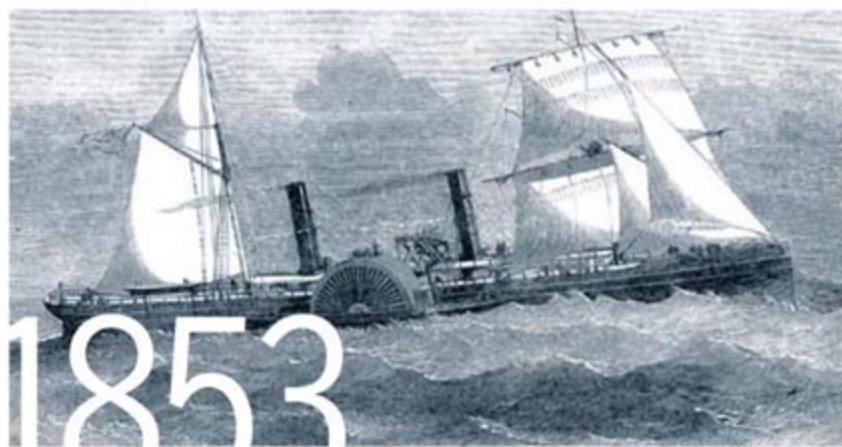
to the unsavory tactics being used by investigators hired by HP. But there's another way to look at this whole sordid saga.

Perkins, who would resign from the board, and Patricia C. Dunn, then its chairman, were embroiled in a bitter feud over board procedures. After the results of the leak probe, which fingered Perkins' good friend, George A. "Jay" Keyworth II, were presented at a board meeting in May, Perkins accused Dunn of betraying him, violating an agreement they'd made to handle the leaker's identity "offline." (According to Dunn, there was no such arrangement.) He claimed that the reputation of "a good man"—his buddy Keyworth—was being "ruined," Dunn has said. After she stepped down as chairman in September, Perkins seemed to relish the moment. "My No. 1 thing was to get Pattie [Dunn] out as chairman, and I got that," he told *Newsweek*. "So I'm happy." Perkins, one might say, had gotten his revenge. (A rep for Perkins says he "acted solely in the best interests of HP, its shareholders and employees.")

'POETIC JUSTICE'

THE HP TALE ISN'T last year's only payback-tinged business drama. Kenneth G. Langone, the fiery billionaire co-founder of Home Depot Inc. and onetime head of the compensation committee of the New York Stock Exchange's board, was named in a

Corporate Revenge: A BRIEF HISTORY



Cornelius Vanderbilt (left) ushered in the age of American moguls, and his legendary ruthlessness set the bar for many titans to come. In 1853 the Commodore took his first vacation, an extended voyage to Europe aboard his yacht. When he returned to the U.S. months later, he found two of his associates had used the power of attorney he had left them and sold his interest in his steamship concern, Accessory Transit Co., to themselves. "Gentlemen," he wrote, in a classic battle cry, "you have undertaken to cheat me. I won't sue you, for the law is too slow. I'll ruin you." He converted his yacht to a passenger ship to compete with them, added other vessels, and started a new line, aptly named Opposition. Before long, he bought his way back in and regained control of the company.



Having a boss who calls himself "**Ming the Merciless**" after the *Flash Gordon* character (above), should have been a warning. But **Bernie Marcus** (far left) was still a little surprised when he was fired from running Handy Dan Home Improvement Centers. The boss was Sanford C. Sigoloff, then CEO of parent company Daylin Inc. Within weeks, Marcus and another sacked Handy Dan exec, **Arthur Blank** (right), were developing their own form of revenge: A warehouse-style home improvement chain. By 1988, Home Depot had 96 stores and \$2 billion in sales.

undiscussables" in business, says one psychologist

lawsuit by former New York Attorney General Eliot Spitzer over his role in ex-Big Board Chairman Richard Grasso's giant \$187.5 million pay package. In early 2006, during Spitzer's campaign for the Democratic gubernatorial nomination, Langone and members of his family gave \$64,000 to Spitzer's long-odds opponent, Tom Suozzi. He also urged friends and associates to donate money. (In an e-mail, Langone said: "I thought it was time to stand up to [Spitzer] and demand accountability. It wasn't revenge, it was principle." His spokesperson says the funding was based "on the merits" of Suozzi's candidacy.)

And following the government's indictments in May of class action law firm Milberg Weiss Bershad & Schulman for alleged illegal kickbacks to plaintiffs, some in Silicon Valley are savoring the twist of fate. While William Lerach, who aggressively sued technology companies in the 1990s and left the firm in 2004, has not been named in the indictment, some executives still relish his former firm's misfortune. "We're all enjoying it because he's a parasite," says T.J. Rodgers, CEO of Cypress Semiconductor Corp. in San Jose. "It's just poetic justice."

Rodgers' glee has a name, of course: *schadenfreude*, or joy at others' woes. It's a close cousin to the desire for revenge. The satisfaction we receive from the punishment of others is not only something we can all identify with, but something to which we're all neurologically inclined.

Ernst Fehr, a behavioral economist at the University of Zurich, studies how our brains react when "social norms" are violated. In Fehr's research, two players are asked to exchange money according to various scenarios. When one player hoards the cash for himself, the other has an opportunity to punish him financially. The player who got burned is hooked up to a brain scan while he's considering whether to retaliate. Fehr found that the part of our brains associated with feeling satisfaction was more strongly activated while players contemplated getting even. "There is a hedonic force behind the punishment," says Fehr. Put simply: Revenge is biologically, scientifically sweet.

There's something delicious about getting back at someone who has hurt us. Or doing well as that person looks on. Savoring the balm of revenge does not require active stabs at retribution; it can also be a byproduct of success. "We hold the illusion that if the other person is as venomous as we think, [even] their knowledge of our success is psychologically damaging to them," says Jeffrey A. Sonnenfeld, senior associate dean at the Yale School of Management.

Spurned CEOs can experience this form of pleasure by turning around a struggling competitor. Consider Millard "Mickey" Drexler, the "merchant prince," as he has been called for his pitch-perfect retailing skills, who was pushed



Michael L. Muse (far left) and his father, **M. Lamar Muse** (right), begin operating Muse Air, shunning the hot-pants and high-jinks routine of his former employer, Southwest Airlines, for a more sophisticated, upscale, and smoke-free (a first in those days) flying experience. Michael had been Southwest's CFO, while Lamar had been president. Both

had been forced out in 1978 following a power play gone wrong. The payback, however, never really got off the ground: By 1985 the airline, which was widely dubbed "Revenge Air" in the industry, was deeply in debt, and Southwest bought out its foe, later renaming it TranStar Airlines.



Lee Iacocca (above), who was ousted as president of Ford Motor Co. by Henry Ford II in 1978, publishes his autobiography, *Iacocca*. The 1984 book came at a delectable moment for Iacocca, who had gone on to take the helm of Chrysler just as it sank

into near-bankruptcy in 1979. Five years, a government bailout, and a hard-fought turnaround effort later, Chrysler had paid back its government loans and had a winner of an innovation in its minivan. Iacocca lambastes Henry Ford II throughout the book. "Because of my pension, he still pays me a lot of money to go to work every morning to see if I can knock his block off."

out of Gap Inc. in 2002 after 19 years at the helm. Unlike most other CEOs, who walk out the door with millions in severance, Drexler left behind a hefty package and its non-compete restrictions.

That decision allowed him to bag a job leading preppy retailer J. Crew Inc., which he helped private equity firm Texas Pacific Group take public in June. Since joining J. Crew, Drexler, 62, has hired at least two dozen executives away from his former employer. He has also launched a new brand called Madewell that, with prices below J. Crew's, could compete with Gap. Madewell's two stores, which opened in August, carry hip, high-quality jeans, sweaters, and accessories. Sound familiar? (One J. Crew representative says Madewell is not intended as a Gap competitor.)

Drexler has insisted he is not motivated by revenge, but he has also said that anger over his departure "helps fuel my accomplishment now." Even if payback isn't an active pursuit, he's probably savoring the redemption. J. Crew's initial public offering was one of the most successful in 2006. In its most recent quarter, operating income increased 51% from the year before. Meanwhile, his successor at Gap, Paul Pressler, is experiencing steady drops in sales and may be exploring a sale of the company. "[Drexler's] parting at Gap now in retrospect is probably deeply regretted," Evan S. Dobbelle, a former Gap board member and now president of the New England Board of Higher Education, said in an e-mail. Drexler declined to comment to *BusinessWeek*.

THREATENED THRONE

REVENGE IS A RESPONSE to a perceived injustice or what psychologists call narcissistic injury, known to you and me as a wounded ego. This reaction is often acute in entrepreneurs or members of family businesses, whose sense of self-worth is bound to their businesses. "For a founder whose identity is wrapped up in his company, there's no end to the revenge that one could want to exact on those who threaten to take it away," says Kenneth Eisold, a New York psychoanalyst who counsels business executives.

In the case of an executive whose throne isn't just threatened, but taken away, nothing may be more fulfilling than being able to reclaim it. Steve Jobs, who was forced out of Apple Computer Inc. in 1985 only to return in 1997, isn't the only one who has achieved this unlikely feat. Take Malcolm Walker, a British entrepreneur who founded Iceland, a grocery chain specializing in frozen foods that's now among Britain's largest private companies. Back in December, 2000, when Iceland was

RESEARCH shows our brains'

still a public company and Walker was looking forward to his pending retirement, he controversially sold \$19.8 million of his equity stake just weeks before his successor, Bill Grimsey, who took over on Jan. 2, 2001, issued a profit warning amid slumping sales. Shares went into a free fall.

It quickly became clear Walker had to resign immediately. Britain's Department of Trade & Industry (DTI), a government agency, launched a probe into the stock sale. "When I left, I was no longer the guy who had built a successful business," he says now. "I was remembered as the dodgy guy who was being investigated for insider dealing." Later, Walker recalled: "I had a tremendous cloud hanging over me." Despite the dark days,



After a long battle, **Jeffrey Katzenberg** (left), whose ex-boss **Michael Eisner** (inset, above) called him "the little midget," won about \$250 million in compensation he argued he was owed after being fired from Disney in 1994. That year he started DreamWorks SKG, a rival to Disney, and went on to make *Shrek*, which grossed \$267 million at the box office and won a nomination for the Golden Palm at Cannes. Beyond the box-office bonanza, *Shrek* also poked fun at Disney's saccharine fairy tales. While Katzenberg has denied the accusation, some Hollywood observers viewed the movie's villain—the evil, perfectionist, and short **Lord Farquaad** (above)—as a parody of Eisner.

lambaste

praise

reward centers light up when contemplating revenge

Walker didn't waste time before firing back. Within months, he opened a rival shop, which he joked would be called "Frozen Out." (What was that again about retirement?) The store was actually named Cooltrader, and before long, Walker expanded to 20 outlets. Trapped on the sidelines of Iceland, he plotted his return. "I had something to prove," says Walker, who was later cleared of any wrongdoing.

In late 2004, Walker joined up with retail investment firm Baugur Group to buy back the grocery chain and, on Feb. 11, 2005, his birthday, returned to run his company. While he has busied himself with retrofitting stores and simplifying inventories, he has also been settling a few old

scores. He renamed the years he was away the "Dark Ages" on Iceland's Web site, where he has cobbled together a list of Grimsey's turnaround forecasts in the press, mocking the oft-promised recovery. ("It's my Web site, isn't it?") He has sent a dossier of his own to the DTI, questioning Iceland's finances during his absence. (Grimsey told *BusinessWeek*: "I take no notice of Malcolm Walker. I've moved on with my life.") Today, according to Walker, Iceland's sales are growing again at double-digit rates. "Everything I'm telling you now enables me to feel totally vindicated."

High-profile departures or firings are hardly the only circumstances that can spur people to want to get even. From vendettas against co-workers who shoot down ideas to grudge matches between middle managers vying for a senior job, payback plays a role in the more mundane scenarios in corporate life, too.

Indeed, in business, revenge often takes on passive forms. "You rarely see someone with a knife in their back" in a business context, says Richard Olivier, an Englishman who runs workshops that use Shakespeare's plays to help leaders unravel motivations such as revenge, ambition, and power. Rather, "you see lots of people who are dying the death of a thousand small cuts," says Olivier, the son of actor Laurence Olivier.

Yet another business scenario that incites its share of retribution is the passed-over executive. "It's not as visible," says Yale's Sonnenfeld, "but there's a seething sense of resentment in people who've spent a lifetime thinking they've earned something only to have it snatched away at the 11th hour." Consider Joseph Galli Jr., who in 1999 was president of the power tools and accessories group at Black & Decker Corp. At 41, he was pushing his boss, CEO Nolan D. Archibald, who had been in the job for 15 years, to step down and give him his moment in the sun. When Archibald resisted, a frustrated Galli quit.

Those who know Galli say he is still driven by not getting the top job. His fondness for the tool business never waned, either: In his brief, one-year term as COO of Amazon.com Inc., he introduced tool sales to the online retailer before other categories, such as toys and office products, that most analysts said made more sense. And in 2001 he joined Newell Rubbermaid, drawn by the offer to be CEO and the chance to expand Newell's tool line into a force that could eventually challenge Black & Decker's market share. That never happened: In late 2005, after four years of unmet earnings targets, Galli resigned.

His newest post, as chief of Techtronic Industries Co.'s



Back in 1997, soon after **Steve Jobs** (left) returned to the company he started, **Michael Dell** (right) was asked at a technology conference what he would do about **Apple Computer**. "What would I do?" Dell joked to the gathered attendees. "I'd shut it down and give the money back to shareholders." Then in January of this year, just as

Dell was beginning what would turn out to be a tumultuous year, Apple's market capitalization reached \$72.13 billion, surpassing Dell's. Jobs sent an e-mail to his employees. "Team, it turned out that Michael Dell wasn't perfect at predicting the future," he wrote. "Based on today's stock market close, Apple is worth more than Dell."

SHARE YOUR THOUGHTS.

Sun believes sharing is the way to create better ideas. That's why we've teamed up with *BusinessWeek* to offer you an opportunity to share your comments. Join the conversation about this week's Cover Story at businessweek.com/coverstory.



global floor-care division, appears to be a stepping-stone to running the entire Hong-Kong-based company, which includes tool brands such as Ryobi. Galli, a fiercely competitive former college wrestler, is widely expected to be named CEO of Techtronic when his noncompete clause in the tool category ends in late 2007. "He is utterly driven by the thought of passing Black & Decker, so much so that he took a divisional job after being CEO of a whole company in order to line up the stars," says one former Techtronic executive. Galli, still bound by his noncompete, says he can't comment on the tool business.

Noncompete or nonsolicit arrangements, designed to prevent people from hiring former colleagues, can stand in the way of executives turning their revenge fantasies into reality. They may be barred from battling their former companies if they want severance pay. Still, recruiters say they often see spurned execs try to get around such agreements by using a headhunter, who would first conduct an exhaustive search, as a shield. Mark Jaffe, a Minneapolis search consultant, says clients can be pretty explicit with him, both when responding to rivals' poachings or when, as departed executives who become newly employed, they try to exact damage upon the company they've left behind. "This is not typically something that's very veiled [to the recruiter]," he says.

Indeed, says Brian M. Sullivan, CEO of New York search firm Christian & Timbers, some companies have offered premiums for recruiting people from a competitor that has stolen one of their own. "They'll put a bounty on them," he says. And when the poaching is personal, watch out. Jaffe says he recently got a request from the division president of a major company. She had just had one of her top people stolen away by a friend who worked at a rival. In filling the

Getting Even—Online

On the couch: A Video View with Kerry Sulkowicz, a psychoanalyst and author of *BusinessWeek's* "Analyze This" column.

The story behind the story: For a podcast interview with Management Editor Jena McGregor by Executive Editor John A. Byrne, go to businessweek.com/search/podcasting.htm.

Recovering from disaster: In a Q&A, Yale management professor Jeffrey A. Sonnenfeld discusses his new book, *Firing Back: How Great Leaders Rebound after Career Disasters*.

BusinessWeek .com

www.businessweek.com/extras

now vacant job, Jaffe says, she urged him to focus heavily on the competitor. "Let's see how much damage we can do in filling that position," she told Jaffe, who nonetheless didn't find anyone at the firm.

Which brings us back to Garnett. Since getting sacked by Ellison, he has channeled his anger into investing in and building up companies that compete head-to-head with Oracle or Ellison projects. The most recent of these is Ingres, a low-cost, open-source software startup that Garnett hopes will poke a hole in Oracle's high-price database business. Garnett has targeted Ellison's team for several engineers and managers. He has also hired a small army of former Oracle folks to help him torpedo the old mother ship: Of Ingres' 250-member staff, 50 are ex-Oracle, including several top executives and key technologists. Many directors have the Oracle pedigree, too. "The simplest way to create a culture is to pick an enemy," says Garnett. "We have an enemy: It's Oracle." ■

—With Steve Hamm in New York and David Kiley in Detroit

Grudges in the CUBICLE

The best-known vendettas may take place in the corner office, but the cubicle is no stranger to sabotage. Revenge in the workplace has been the research interest

of Georgetown University management professor Robert J. Bies since 1996, when he co-authored one of the first academic papers on the topic. Management Editor Jena McGregor spoke with Bies about why revenge is such a taboo subject in business and what managers can do to prevent destructive score-settling by employees.

What has surprised you in your research?

As I began, I would ask people: "Do you guys engage in revenge?" They'd say: "Oh no, we never engage in revenge." Then I would ask if they ever tried to get even with people, and they'd answer: "Oh, all the time." There's something about the word "revenge" that is very loaded. That's the hypocrisy of revenge in the corporate world. We say it doesn't exist, but it does.

How is revenge in the workplace different

from revenge in other parts of our lives?

In the workplace, there are some real power differentials that may not exist in other institutions. So much of your identity and who you are is invested in your job. There are so many different ways people can do harm to you.

Why do we have such a hard time talking about it?

For institutions, the desired imperative is control, standardization, routinization. My point is that [revenge] should be predictive because I can tell you what the triggers are that can make it happen. That's what our research is. We've outlined a series of events—layoffs without warning, public beratings, budget cuts without explanations—that can cause people to take revenge. It shouldn't be a surprise.

So, can managers control vendettas in the workplace?

We need to be aware of the things that

provoke it, but we also need to teach managers and leaders to treat people fairly. If you can train managers how to do that—give employees advance notice, provide explanations—it will mitigate the feelings of revenge.

But isn't much workplace vengeance pathological? Isn't it being done by employees who think they've been wronged when really they haven't been?

Can there be people who are psychologically maladjusted who see a provocation that doesn't exist? Yes. But it's more common that they're not [maladjusted]: They got provoked, and nothing was done about it. Then they have people around them who say: "You got screwed." This just keeps the emotion going.



SHARP®

©2006 Sharp Corporation



Any MFP can print colorful growth charts.
How many can actually help you achieve them?

INTRODUCING THE SHARP MX-SERIES. Thanks to the revolutionary Sharp Open Systems Architecture, these multifunction products seamlessly integrate with your network to keep up with your growing business. They also deliver outstanding color and enhanced productivity. No wonder Sharp MFPs won the BLI award for "IT Friendliness" and the BERTL 5-Star Exceptional rating for product usability. To start your own renaissance of color, visit sharpusa.com/documents

COLOR • PRODUCTIVITY • SCALABILITY • SECURITY



As an ENERGY STAR® Partner, Sharp has determined that this product meets the ENERGY STAR® guidelines for energy efficiency.



MX-2000
MX-2700
MX-3500



Lobbyists Who Want Nothing

Why Big Sugar is refusing help from the Hill. A collision course with candymakers

BY EAMON JAVERS

FOR MANY INDUSTRIES, IT'S red alert time in Washington. The Democrats now in control of Capitol Hill are making threatening noises about what they call overly cozy relationships between business and government. Companies in defense, oil, and pharmaceuticals are girding for legislative battle.

Then there's the sugar industry, historically second to none in winning protection from Washington. What is Big Sugar doing in this season of corporate anxiety in the nation's Capital? It's trying to reject a new federal subsidy. That's right: The sugar lobby has said "no thanks" to a proposal that would send hundreds of millions of dollars its way. And astoundingly, there's still pressure on Congress to give sugar producers the money they don't want. "It's a crazy system," says Sallie James, a trade analyst with the Cato Institute, a libertarian think tank in Washington. "It's what happens when politics interferes with the market."

DISCONTENTED CANDYMAKERS

THE ODD TALE of the corporate subsidy in search of a taker begins with the elaborate structure of other protections the \$10 billion-a-year sugar industry already enjoys. Since shortly after the Civil War, lawmakers from sugar-producing states have pushed the government to prop up the price of domestic sugar. The Agriculture Dept. limits the amount of domestically produced sugar that may be sold in the U.S. The government also discourages the importation of foreign sugar with quotas and tariffs. In addition, Washington operates a federal loan program that effectively sets a minimum price for sugar.

These arrangements benefit major producers such as U.S. Sugar Corp. and

Florida Crystals Co., as well as the marketer Domino Foods Inc. But American candy makers, soft drink manufacturers, and other large consumers of sugar have grown unhappy with the current system—and they're the ones pushing the subsidy Big Sugar doesn't want. The candy manufacturers and their allies complain that the restrictions and tariffs make U.S. sugar prices about twice as high as the world market price.

Seeking to lower the price of sugar that goes into chocolate bars, soft drinks, breakfast cereal, and other treats, manufacturers represented by the Sweetener Users Assn. are pushing Congress to make direct subsidy payments to grow-

ers. They're lobbying members of the Agriculture Committees in both the House and the Senate, and they say they're open to other ideas.

"We're looking for a program that doesn't have the government controlling the supply, but at the same time would help the government maintain farm incomes," says Susan Smith, spokeswoman for the National Confectioners Assn., a trade group of major candy companies. For the big consumers, that's a compromise: For years they argued that sugar supports should be abolished entirely, but they were consistently defeated by the sugar lobby. Under this proposal, they would get lower prices and the growers would keep their existing government support.

But a sugar subsidy program would cost money and worsen sugar producers' reputation for dependence on corporate welfare. The sugar producers argue that a subsidy would shift the burden from consumers to taxpayers, at a cost of \$1.3 billion. That won't be politically popular. Worse, the subsidy could come back to haunt sugar growers at the World Trade Organization if foreign producers object to it as an unfair advantage. "We like the status quo," says Phillip Hayes, spokesman for the American Sugar Alliance, which represents growers. Or as Representative Jeff Flake (R-Ariz.), who generally opposes subsidies, puts it: "They've got a good thing going right now, so why chance it? They can have their sweet cake and eat it, too."

The sugar industry may have the money and the political muscle to keep things as they are. During the 2006 election cycle, they contributed \$2.7 million to congressional candidates; 60% of that went to the newly empowered Democrats, according to the Center for Responsive Politics, a nonprofit research group in Washington. The sugar-buying companies contributed just over \$800,000 to congressional candidates during the same cycle, but roughly 75% of their contributions went to now out-of-power Republicans.

Sugar producers also have a key ally in Representative Collin C. Peterson (D-Minn.), who assumed control of the House Agriculture Committee this month. His Red River Valley district is packed with sugar beet farmers, making it the single largest sugar-producing district in the country. Peterson says he'll fight the proposed sugar subsidy and might even try to raise sugar prices, which, he says, "candy manufacturers really won't like." ■





NEW YEAR'S, NEW YORK Keeping watch in Times Square

Homeland Security 2.0

Five years after September 11, a new wave of smarter high-tech tools is coming to market

BY AARON PRESSMAN

FEW IF ANY OF THE 68,000 rabid Philadelphia Eagles fans arriving for last Sunday's National Football League playoff game against the New York Giants knew that they had been scanned by one of the latest high-tech anti-terrorism tools. Pennsylvania security officials deployed radiation probes at the gates of Lincoln Financial Field to stop terrorists from sneaking in a homemade nuclear device that could kill thousands. Personnel on the grounds carried even more-sensitive equipment.

The new gear, made by Thermo Fisher Scientific Inc., was tailored to distinguish dangerous radioactive material from the harmless traces left by common medical procedures that have prompted screeners to question more than a few innocent fans at events such as the Super Bowl. The Waltham (Mass.) company's more discerning scanner and similar new products from competitors are part of a wave of advanced equipment coming to market five years after the September 11 terrorist

attacks. Call it homeland security 2.0.

After the 2001 attacks, federal, state, and local governments snapped up equipment that had been created for industrial applications such as detecting leaks at nuclear power plants. But the gear had been quickly adapted for its new use and didn't always perform as required. Portable detectors carried by some New York City policemen signaled an alarm near any radioactive source, even the granite around entrances to subway stations. Scanners for ports tagged containers carrying kitty litter as potential hazards. U.S. Customs & Border Protection, a division of the Homeland Security Dept., told Congress in May that it recorded 318,000 alarms from port sensors scanning 80 million containers over the past three years without finding any serious threats.

Thermo Fisher is aiming to eliminate the false alarms. "The govern-

ment rushed to buy systems that weren't optimized to detect the right thing," says Thermo's 49-year-old CEO, Marijn E. Dekkers. "We're working on better versions for a wave of reconstruction" that includes projects like installing next-generation scanners in major ports.

Dekkers, who closed an \$11 billion merger with Fisher Scientific in November, is looking for growth markets as he integrates the two companies' largely complementary product lines. Thermo is best known for lab gear such as mass spectrometers used in biotech research and detection equipment used by manufacturers and government security agencies. Fisher concentrates on test tubes, lab chemicals, and other basic items. Wall Street has given the merger a big vote of confidence: The stock has soared 47% over the past year, to almost 45 as of Jan. 9.

SAFE HARBORS

DEKKERS IS EXPERIENCED in the challenges of consolidating businesses. Raised in the Netherlands, the chemical engineer came to the U.S. in 1985 to work at General Electric Co.'s research unit in Schenectady, N.Y. After moving into management at Honeywell International, he arrived at Thermo in 2000 as chief operating officer and helped merge 24 publicly traded entities, each with its own stable of brand names, into one leaner corporation.

Security products are a big part of Dekkers' expansion plans. Last July the feds tapped Thermo and two competitors, Raytheon and Canberra Industries, for a \$1.2 billion pilot project to install next-generation scanners, starting with New York and New Jersey's ports. Thermo says the contract will be worth \$200 million over five years. A Democrat-controlled Congress may mean yet more orders. Republicans spent billions to protect airports but much less on ports. "Democrats have been yelling about this for years," says Brian W. Rutenbur, a Morgan Keegan & Co. analyst in Nashville who covers companies active in homeland security. ■



RADEYE Handheld radiation detector from Thermo Fisher



Maribel Martinez Lieberman

Chocolatier, Owner of MarieBelle New York

Ask Maribel Why She Loves Her BlackBerry

"I love the flavors of the world. The inspiration for my chocolate is ingredients. I travel to Mexico, Spain—everywhere—for cardamom, cinnamon, passion fruit, saffron. The first thing I do when I visit a country, I go to the outdoor markets. With BlackBerry®, I'm not tied to a single place. Everything is right here in my hand. It really doesn't feel like I'm working so hard with my BlackBerry because it's so easy. To me, that's elegant."

Join the conversation at www.blackberry.com/ask.



 **BlackBerry.**

The Small Fry Sour on Search Ads

Priced out by brand giants, the outfits that pioneered the medium are looking elsewhere

BY ROBERT D. HOF

FOR YEARS, RUNNING THOSE little four-line text advertisements on Web search engines brought in a profitable stream of new customers to BabyAge.com. But last year, search suddenly turned sour for the eight-year-old online baby products store, which posted about \$20 million in sales. Even as BabyAge's \$1.2 million worth of search ads got more clicks in 2006, they netted fewer actual buyers, effectively doubling their cost. "We're out of business at this rate," fumes Chief Executive Jack Kiefer. He plans to cut back on search ads this year.

Kiefer isn't the only one casting a more skeptical eye on what has been the fastest-growing and most lucrative Internet ad market. So are midsize online retailers such as jeweler Ice.com, luggage seller eBags, and consumer-electronics store eCost.com. Search ads, which run alongside query results on Google Inc., Yahoo!

Inc., and other search sites when someone types in "diamond necklace" or "DVD player," used to be the marketing weapon of choice for these outfits. They reached more targeted audiences and could be measured for effectiveness. Now the price per click on those ads is rising—by an average of 31% from a year ago in the third quarter, according to DoubleClick Inc. Some merchants are looking seriously at alternatives—even, of all things, print and radio spots.

Think of it as fallout from a new online land rush. Brand giants from Best

Buy Co. to Zale Corp. are diverting more and more of their marketing budgets to search ads. They're driving up prices and stealing customers from some of the smaller businesses that have bought the bulk of those ads. Web users have learned to shop around more, and now, instead of clicking on ads from the little guys and buying from them on the spot, they're often buying from the big brands they know well. If many of the small and midsize companies that pioneered this ad medium get disillusioned, search ads could lose their luster.

For the time being, Google's not worried. The rush of ad dollars from big brands into search is more than making up for any cutbacks by smaller outfits. National marketers from General Motors Corp. to Wal-Mart Stores Inc. are for the first time dedicating branding budgets to search, says Matt Greitzer, search director at Web marketing firm Avenue A/Razorfish. And Google and Yahoo say that even small companies with

the right products and message can still trump big brands online. "We're not seeing any erosion of ROI [return on investment] across the board by our customers," says Richard Holden, Google's director of product management for advertising.

Still, many small and midsize marketers are buying far fewer "keywords" and phrases. Merchants are also trying out ads on MySpace and YouTube, or advertising on blogs and niche shopping sites. Says consultant Andy Beal of Marketing Pilgrim: "The free lunch is over." ■

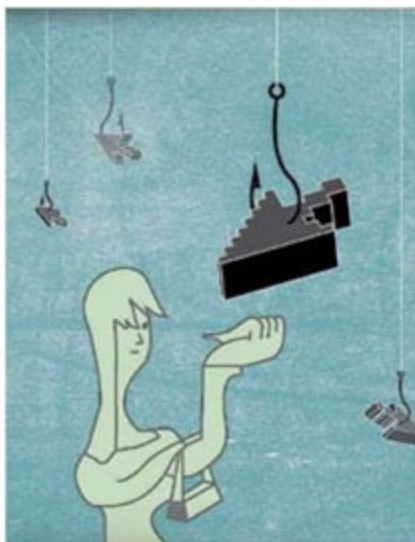


ILLUSTRATION BY JOHN HERSEY

Ask Someone Why They Love Their BlackBerry

In 1999, BlackBerry® hit the street.

Word of mouth ignited. People

loved the wireless freedom. Today

there are millions of BlackBerry

owners and their passion

continues to be the best form of

advertising. Every day. All around.

People are using BlackBerry to live

larger and more successful lives.

Tell us why you love yours at
www.blackberry.com/ask.

 BlackBerry.

©2006 Research In Motion Limited. All Rights Reserved. The BlackBerry family of related marks, images and symbols are the exclusive properties and trademarks of Research In Motion Limited.

Private Equity Repellent

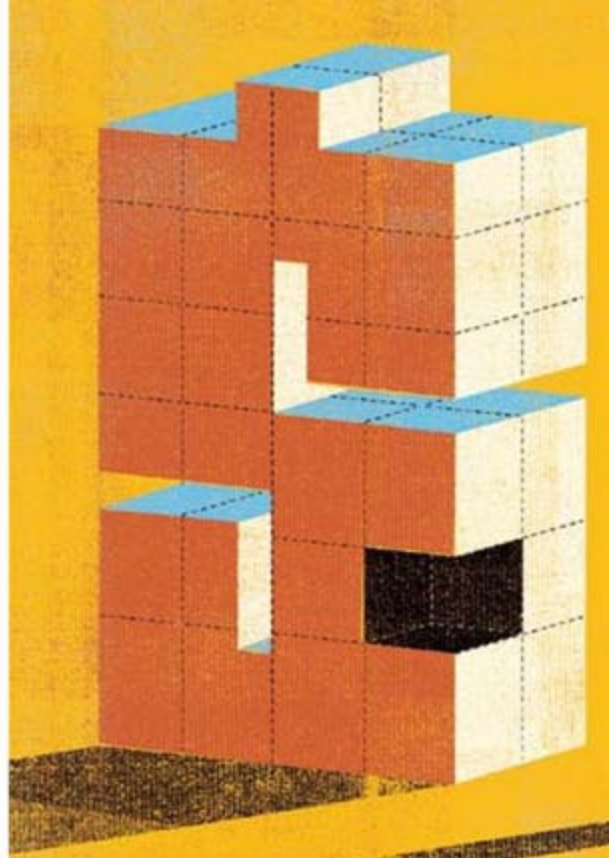
Why some companies are intentionally taking the bloom off their balance sheets

BY DAVID HENRY

THREE WEEKS BEFORE Home Depot Inc. CEO Robert L. Nardelli resigned, Standard & Poor's downgraded the company's credit rating, citing the retailer's "more aggressive" financial policy. In the past year Home Depot had taken on \$5 billion in new debt and tapped two-thirds of its cash reserves to buy back shares and increase dividends. The moves were

a sop to angry shareholders who had been pestering Home Depot to boost the stock price.

Nardelli, of course, won't be around to see how his maneuvers play out; he quit over pay issues. Yet Home Depot illustrates new thinking about corporate balance sheets. The underlying logic seems counterintuitive: By weakening the financial picture to return cash to shareholders, corporate managers can preempt shareholder challenges. At the same time, they make the balance sheet



less enticing to voracious private equity firms. Leveraging up, the thinking goes, can kill two birds with one stone.

Many companies are buying in. Share buybacks and dividends, all the rage recently, are starting to outstrip profits. In 2006, for the first time since 1990, cash held by nonfinancial companies in the Standard & Poor's 500-stock index

**This test had a lot of turns.
And one big twist.**

**This test had a lot of turns.
And one big twist.**

(Ford Fusion beat Camry and Accord.)

S

BOLD MOVES





solid over the years. According to a recent study by UBS equity strategist David Bianco, companies in the S&P 500 could increase their debt to still-prudent levels in 2007, return excess cash to shareholders, and raise the index's value 3% to 5%.

Such thinking is showing up at a wide range of companies. At the Hershey Co., spending on share repurchases exceeded free cash flow by \$1 billion over the past four years, estimates B. Craig Hutson, an analyst at Gimme Credit. S&P changed its outlook for Hershey's A+ rating to negative in October. Hershey de-

declined, according to S&P senior index analyst Howard Silverblatt. He pegs the drop at about 4%, based on preliminary data. Cash decreased "for a significant number of companies," he says, perhaps more than two-thirds.

The lurch toward debt isn't as dangerous as it sounds. Many experts say executives have made their balance sheets too

ten turn "investment-grade" bonds into junk. Similarly, Computer Sciences Corp. last year embarked on a \$2 billion buyback campaign, partly with borrowed money, a move that prompted a downgrade from S&P to A-. And Expedia Inc. saw its rating threatened last month when S&P sized up its repurchase plan and changed its outlook to "negative." Both companies declined to comment.

Among "investment-grade" borrowers, cash as a percentage of total debt has decreased from 17.5% in January, 2005, to 12.5%, according to Gregory J. Peters, chief credit strategist at Morgan Stanley. Yet that's still more than the historical

average of 10%, says Peters, and merely leaves balance sheets "less pristine."

Bondholders hate the change; they're losing safety without getting higher returns. Then again, a willful shift toward leverage could be the lesser of two evils, the other being a leveraged buyout. LBOs pile on debt and of-

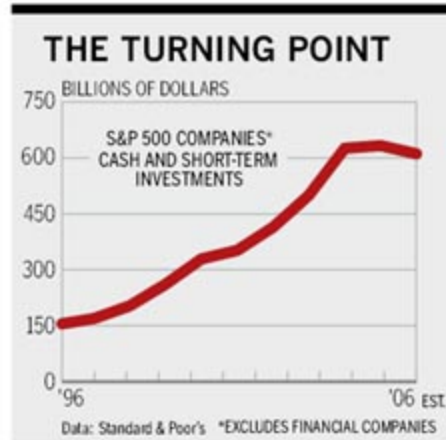


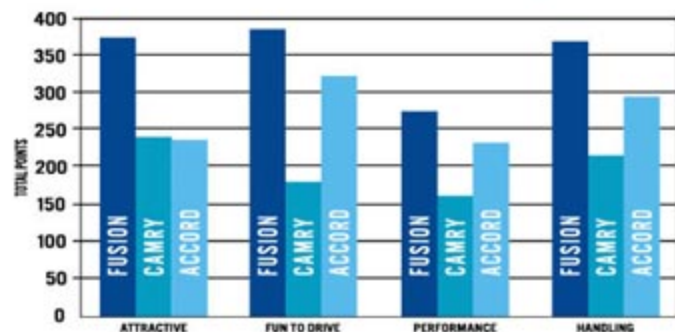
ILLUSTRATION BY KEITH NEBLEY; CHART BY ERIC HOFFMAN/N/BW

Recently, in Washington, D.C., a town known for its strong opinions, *Car and Driver* magazine held a head-to-head comparison. Six hundred car enthusiasts were asked to compare three cars in performance, handling and styling.

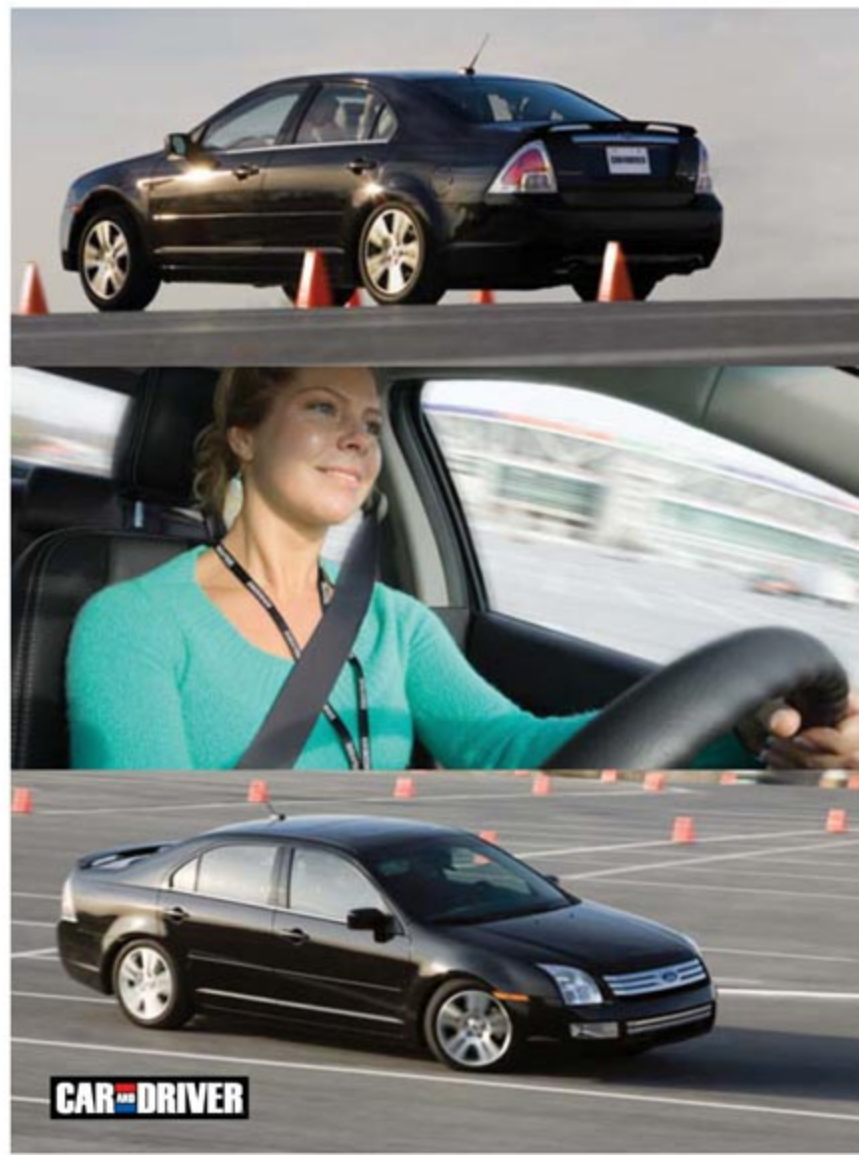
So, who won? Camry? Accord?

Actually, the all-wheel-drive Ford Fusion came in first – a fact that surprised a lot of people, but not *Car and Driver*.

Check it out yourself. Visit a Ford Dealer or go to fusionchallenge.com.



Results from 600 drivers who were asked if the cars were attractive, fun to drive, performed well and handled with precision. "Yes" responses scored one point. "No" responses scored zero. The results speak for themselves.



CAR AND DRIVER



Who Will Run the Plants?

As the nuclear industry starts to expand again, it faces a graying workforce

BY ADAM ASTON

IF YOU WALK THE HALLS OF WESTINGHOUSE or GE Nuclear, the top U.S. builders of atomic power plants, you'll notice a buzz in the air—the first stirring of excitement since the 1970s. With many experts endorsing nuclear power as a clean replacement for coal-burning plants linked with climate change, nuclear players are gearing up to build more than 20 reactors, the first new facilities on U.S. soil in decades.

But roaming the same hallways, something else seems odd: There are practically no young people. After years lying dormant, the industry faces a dire labor shortage, and it will get worse during the next 5 to 10 years as thousands of aging workers drift off to golf courses and retirement homes. So plant builders and utilities are frantically searching for fresh talent. If the industry is to have any future, “young workers are the key,” says Howard J. Bruschi, a retired chief technology officer at Westinghouse Electric Co. who helped design the company's newest reactor, a model that has been selected for 10 projects in the U.S.

The dilemma dates from the late 1970s, when skyrocketing costs began to chill investor enthusiasm for new plants. In 1979 a partial meltdown at Pennsylvania's Three Mile Island doomed the industry's optimistic vision of 1,000 atomic plants. Hiring stalled, and nuclear engineering programs at universities stopped churning out graduates. In short, a whole generation of nuclear workers went missing.

Today, the average age in the nuclear power sector is 48—one of the oldest of any U.S. industry. By 2010 about 27% of these workers will be eligible to retire—some 15,600 men and women. A further 7,600 or so are expected to exit the industry through turnover. That entire head count will need to be replaced to keep today's fleet of 104 reactors humming.

Factor in projected growth, and the situation is even more serious. A substantially larger workforce will be needed by 2010, when the first of two dozen proposed reactors enters the long design and construction process. Overseas, 27 plants are under way, 62 are on order or planned, and an additional 130 have been proposed.

Even if only a fraction of those plants are built, the industry faces a “severe shortage of qualified workers,” according to the American Nuclear Society. “We're probably getting 80% to 90% of what we need,” says Andy White, president and CEO of GE Nuclear Energy Inc., whose reactors have already been selected for seven new U.S. projects.

NO EMISSIONS

IT'S EASY TO SEE why some industry executives have started to fret. It can take years for new hires to master the industry's complex procedures and absorb its safety-obsessed culture. “Five years ago, we didn't dream we'd be building on this scale again,” says Amir Shahkarami, senior vice-president for engineering

and technical services at Exelon Corp., the nation's largest nuclear utility. Exelon operates 17 reactors today and is considering one new facility. “The aging workforce will result in a substantial loss of experience,” Shahkarami says.

Just how quickly colleges can crank out such highly specialized engineers remains a question. Some 34 nuclear engineering departments have closed since 1980, leaving just 29 today. By the late 1990s, the number of undergraduate students enrolled in such programs had fallen to fewer than 500 a year. Yet in the past several years, enrollment has again begun to rise. In 2007, total nuclear engineering majors in the U.S. will approach 2,000, predicts John Gutteridge, director of university programs at the Energy Dept.

Several factors account for renewed interest on campuses. Starting salaries in nuclear power jumped 6.6% last year, to about \$54,600. In addition, today's students are far more worried about global warming than the risks of a nuclear meltdown or the problems of waste disposal. Coming of age long after the disasters at Three Mile Island and Chernobyl, new hires in the power sector tend to regard atomic energy as a plausible solution to America's energy woes—as did the engineers who built the first generation of nukes. The fact that plants emit no greenhouse gases is a huge plus. “I want to be sure my kids can plug in their iPods someday, too,” says Michelle Yun, a recent grad who joined Exelon as a licensing engineer last year.



LOCKRIDGE One of Westinghouse's first new hires after a long freeze

that plants emit no greenhouse gases is a huge plus. “I want to be sure my kids can plug in their iPods someday, too,” says Michelle Yun, a recent grad who joined Exelon as a licensing engineer last year.

DeLeah Lockridge, a senior engineer in Westinghouse's services unit, is thrilled by the prospect of new plant construction. When she entered the company in 1999—one of the first new hires following a long freeze—Lockridge worried that nuclear energy might be a dying industry. “I didn't expect to have the opportunity my instructors had,” she says. “Now, I want to build a plant.” ■



How does your usual IRA investment compare with one from T. Rowe Price?

Look more closely this year, with T. Rowe Price's Mutual Fund Compare Tool.

It's easy to compare this year's performance numbers. But to find the best long-term mutual funds for your IRA, look a little closer. The choices are far from equal. T. Rowe Price's Mutual Fund Compare Tool lets you compare a fund you're considering for your IRA this year with a similar T. Rowe Price fund. The Mutual Fund Compare Tool goes beyond short-term performance, to let you compare long-term results, fees, and even fund manager experience. When you delve deeper into the investment options for your IRA this year, it's easy to see why more and more investors are switching to T. Rowe Price. Visit ira.troweprice.com today. Or call our Investment Guidance Specialists for help choosing a fund for your IRA. **Act before April 16 for your 2006 contribution.**

The more you  ask
the more we're different.

ira.troweprice.com | 1.800.541.4705

T. Rowe Price 
INVEST WITH CONFIDENCE

Request a prospectus or a briefer profile by calling 1-800-541-4705; each includes investment objectives, risks, fees, expenses, and other information that you should read and consider carefully before investing.

All mutual funds are subject to market risk, including possible loss of principal.

T. Rowe Price Investment Services, Inc., Distributor.

IRA074820

Changing the Game on Nike

How budget sneakers are tripping up its basketball business

BY STANLEY HOLMES

LIKE THE NATIONAL Basketball Assn.'s top-tier Dallas Mavericks, Nike Inc. continues to display a potent offense. Its recent second-quarter profit surged 8%, to \$326 million, and sales jumped 10%, to \$3.8 billion. The stock, up about 15% over the past 12 months, continues to fly high. "The brand is strong," Nike CEO Mark Parker told analysts in December. "The company is growing."

But the sporting goods giant is facing a full-court press at the heart of its U.S. business: basketball footwear. Industrywide unit sales of basketball shoes dropped 16% last year, says market research firm SportScanINFO. And Nike, which counts on basketball gear for an estimated 30% to 40% of its U.S. revenues, acknowledged last month that footwear inventories were 15% higher than a year ago.

Running shoes and the apparel business remain strong, but John Shanley, who tracks the industry for Susquehanna Financial Group, says Nike will have to sell a lot of shoes in the coming weeks or suffer a possible hit to earnings. Nike CFO Donald Blair told analysts he believed the inventory overhang would not "have a material negative impact."

Nike has been the king of the basketball sneaker

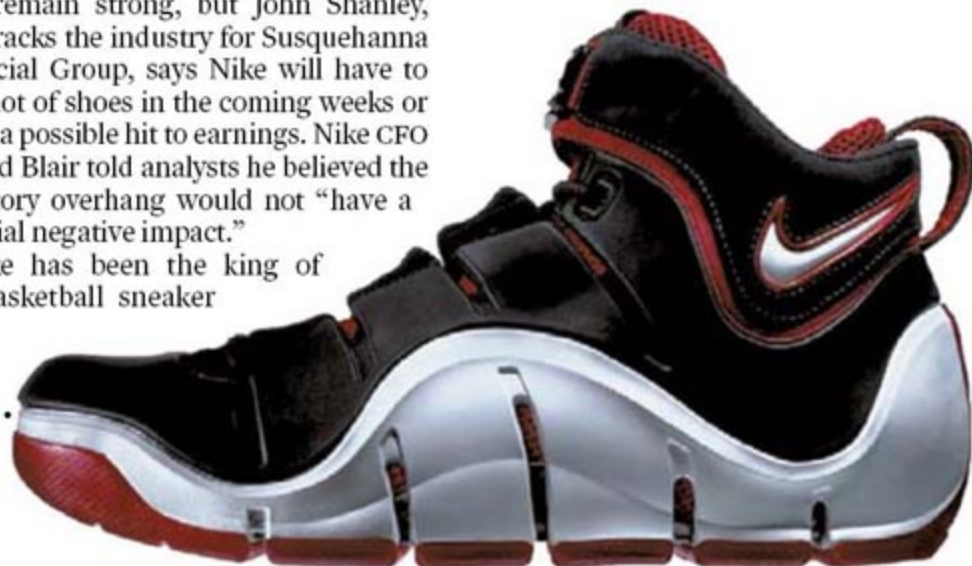
since the 1980s, when Michael Jordan-branded shoes first became a fashion statement on and off the court. But the current Jordan line is losing some cachet among suburban and inner-city kids. While a new release of the Air Jordan Retro did well over Christmas, some of the latter-day Jordan models are being sold at unusually deep discounts.

Nike has been betting on NBA up-and-comer LeBron James to help it make the transition from the Jordan era. In 2003 the company announced it would pay the Cleveland Cavaliers forward \$90 million over a decade to promote its shoes. But while the new Zoom LeBron IV shoe has sold well, James is not a Jordan-caliber endorser, in part because the NBA is not

the draw it was when Jordan was a star.

It's no secret that for the past few years, kids have been trading in their high-tops for skateboarding shoes made by the likes of Vans, DC, and Skechers. But the big news in the sneaker world is the advent of the cheap basketball shoe. Case in point: the Starbury One, which sells for \$14.98. Made and sold by the discount clothing chain Steve & Barry's, the sneaker is endorsed by New York Knicks guard Stephon Marbury, who says 3 million pairs have sold since its August debut.

The Starbury and its ilk have the potential to undermine Nike's basketball sneaker business. According to researcher NPD Group Inc., the low-cost shoe market—sneakers under \$50—has grown nearly 9% over the past two years and now makes up more than half of the \$16.5 billion of branded athletic footwear sold each year in the U.S. Nike sells its own cheap sneakers, but doesn't have much traction against



such low-cost entrants as the \$35 Amp runner, a creation from Payless ShoeSource. "If I were a branded athletic company right now, I'd be reconsidering my whole approach," says Jeffrey Bliss, president of Javelin Group, a sports marketing firm.

Nike has overcome big challenges before. It continues to dominate the basketball sneaker market and still sells 95% of \$100-plus shoes. It has a hit with the Converse Inc. Dwayne Wade, a sneaker endorsed by the Miami Heat guard that retails for \$100. Thanks to strong demand for the shoe, Nike says revenue at its Converse unit rose nearly 50% during the most recent quarter. The question for Nike is whether the current hunger for cheap sneakers is building long-term momentum or is little more than a fad. ■

PHOTOS: SCBLUE/GETTY IMAGES (BASKETBALL)

AT LAST, AUTO INSURANCE
THAT REFLECTS YOUR NEEDS.

TAKE A FRESH LOOK...



Find out why Esurance is one of
the fastest growing auto insurance
companies in America!

Compare & save instantly online:

www.esurance.com/save

 **esurance**[®]
Quote. Buy. Print.[®]

King of His Digital

Net guru John Patrick has built the ultimate automated house. Dim the lights, turn on

MICROSOFT CHAIRMAN BILL GATES may have electronic art on the walls of his \$50 million home outside Seattle and personalized music piped into each room. But a house with an even bigger technological wow factor is the 6,000-square-foot digital domain in Connecticut owned by one John Patrick, a 38-year IBM veteran who spearheaded Big Blue's Net strategy in the late 1990s. At Patrick's suburban castle, almost everything that can be automated is, and it's all tied together in a network that acts like a central nervous system for the house. We're talking security, music, TVs, computers, home theater, lighting, heat and air conditioning,

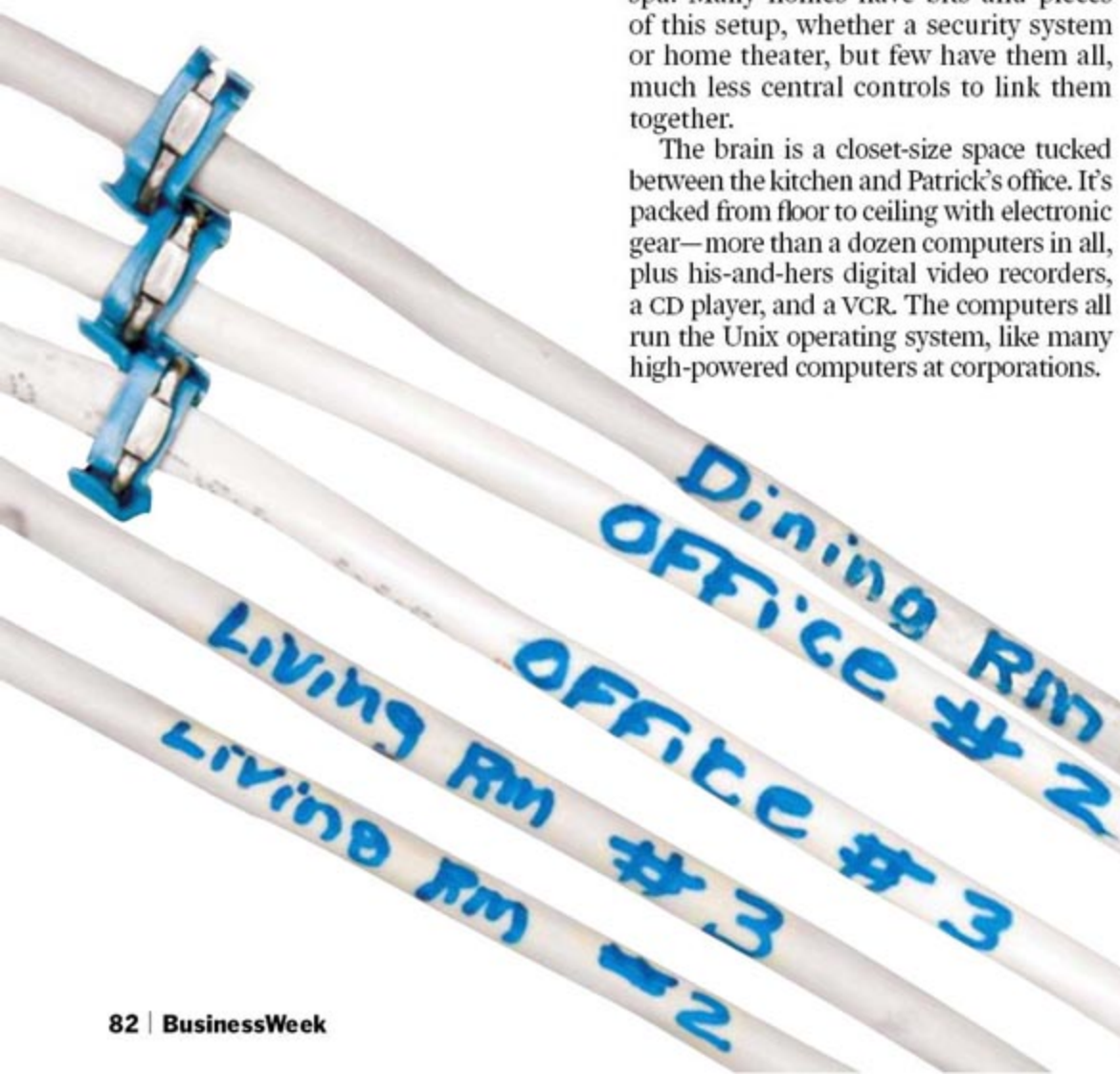
garage doors, window shades, propane, backup electrical generator, and outdoor spa. Many homes have bits and pieces of this setup, whether a security system or home theater, but few have them all, much less central controls to link them together.

The brain is a closet-size space tucked between the kitchen and Patrick's office. It's packed from floor to ceiling with electronic gear—more than a dozen computers in all, plus his-and-hers digital video recorders, a CD player, and a VCR. The computers all run the Unix operating system, like many high-powered computers at corporations.

This room is also where Patrick's home network connects with the outside world. A cable-TV line is split to handle video, wired and wireless Internet access, and phone service. The control room isn't big enough to hold the one-half terabyte storage device where he keeps his digital content. That refrigerator-size machine is in the basement. His music collection totals 20,000 tracks, with no fewer than 7,000 by Mozart, his favorite composer.

Patrick, 61, who grew up in rural southern New Jersey, is a consummate tinkerer. An electrical engineer by training, he's totally into gadgetry. "Some people love golf or sports or cars. I love technology," he says. He caught the domestic gadgetry bug when he set up a home office in his previous house in the late 1990s. When he and wife Joanne decided to build a dream house on a leafy

PHOTOGRAPHS BY RICHARD FREEDA/AURORA



Castle

the music—even from half a world away. **BY STEVE HAMM**

lane a few miles away, Patrick went into full propeller-head mode. “I wanted to automate everything that could be automated, as long as it was practical,” he says. It took two years to see his scheme to fruition. The Patricks moved into their new home in April, 2002.

GADGETRY OVERLOAD

THIS WASN'T A ONE-MAN JOB. Patrick was assisted by Rob Gerhardt, a sales engineer from Phoenix Audio Video, an electronics contractor; a team of networking and electronics experts, as well as a software programmer. They put their heads together to design the system and customize the touch pads mounted on walls around the house.

A project like this can create serious headaches for homeowners. Patrick warns people not to make things overly complex. They might be too difficult to use,

especially for family members who don't appreciate gadgetry. Also, it's hard to find contractors with a holistic view. Most know one thing well—say, security. This stuff can be frightfully expensive. And while Patrick declines to say what he spent on gadgetry, experts say automation can run to 10% of the cost of a new home. But if you do a few simple things, such as lighting, it won't cost that much. Much of the gear is available at electronics stores.

My tour of Patrick's digital life started at a touch pad on the kitchen wall, one of seven of these 5-inch-square pads strategically placed around the house. The ultra-simple interface looks and works like a Web page. There's a menu of services on the left including climate control, security, lighting, and vacation mode. On the right: musical choices selected by artist, album, or genre come from cable, radio tuner, Internet, satellite radio, and

CDs. You can control any electronic system in the house from any pad. “I'm not too technical,” says Joanne Patrick. “I don't know how to program a VCR, but I can operate these wall panels.”

In addition to the touch pads, every room in the house has a 16-button lighting control panel. Besides switching on or off individual lights or clusters, the controls can activate what Patrick calls “scenes.” Press the “Go to Bed” button, for example, and the path to the master bedroom upstairs is illuminated, while downstairs lights are turned off.

Not all the features demand human intervention. Patrick scattered 50-or-so electronic sensors around the house and grounds to monitor the property. There's one in every door and window. Sensors detect whether the sun is out and at what angle it strikes the house so shades are automatically drawn or opened. If a car pulls into the back driveway, a “beep-beep” sounds at each touch pad. From his office desk, Patrick can flip on his TV and tune to the “courtyard cam” channel, which shows the driveway. If he likes what he sees, he'll press a button on the touch pad to open a garage door. Each of the household's cars and motorcycles is rigged with a radio-frequency ID tag so when one pulls into the driveway, the proper garage door opens.

Patrick's outdoor spa, set in a backyard deck and surrounded with shrubs, may be the home's coolest feature. From a comfortable spot in the water, you can easily reach a touch pad that's embedded in a fake rock to control the jets, water temperature, and a mini-waterfall, and to adjust the volume on audio speakers hidden in other fake rocks. (Hey, they're good fakes.) Sensors can also detect snow on the deck and automatically turn on heating elements to melt it.

Patrick can control his home automation gear from his laptop, via the Net, when he's on the road. Once, when his alarm went off and the police paid a visit, he reset the security system from New Zealand. That's the ultimate kick for Patrick: He sees his home as just another stop on the Internet. ■

PATRICK'S PAD One-touch digital panels throughout his house, and handheld remotes, give John Patrick control of everything from window blinds to satellite radio



BusinessWeek.com

To see a video report on the wired home featured in this story, go to www.businessweek.com/go/tv/wiredhome.



BY MIKE MARRONE

The One Album I Can't Stop Playing

BEFORE WE CHARGE into a brand new year of music, I want to spend one more column on an album that was released in 2006—October, to be exact. Although I am often asked what my real personal favorites are, I rarely make lists because I'm always afraid of leaving something off. But I can safely attest that *Live A Little* (Ashmont), the sixth full-length release from the Pernice Brothers, is not only my absolute favorite album of 2006 but will unquestionably reside on

my list of Best Pop Albums of all time.

Now, there are countless genres and subgenres of rock music, so what exactly is pop rock? By strict definition it means "popular music," but to me it's a style of rock sometimes called "power pop" that is best exemplified by songs like *No Matter What* by Badfinger, *Time Of The Season* from the Zombies, or even the Grass Roots' classic *Bella Linda*. Think of Beatles' tunes like *And Your Bird Can Sing*, *Girl*, and especially *I'll Be Back*, or the Beach Boys' *In My Room*. To someone in my age group (50s), it's the sound of days gone by, of playing your 45s outside on a summer afternoon. Even the sad songs make

you feel as if the sun is shining.

Live A Little contains elements of each of the songs mentioned above, but the Pernice Brothers are not mere nostalgia practitioners living off the sounds of rock's golden age. Joe Pernice—the songwriter, lead singer, and co-owner of the Ashmont record label with the band's manager, Joyce Linehan—is a literate songwriter who has managed to incorporate such classic pop influences along with those of lesser-known pop gems such as *Hand In Glove* by the Smiths, *All Going Out Together* from Big Dipper, the Cure's *Boys Don't Cry*, and *Senses Working Overtime* from XTC, to name but a few. Acoustic and electric

6- and 12-string guitars, piano and organ, drums and analog synths play with lovely harmonies, real strings and horns, and masterful songwriting.

Zero Refills is a highlight, with Joe Pernice's angelic falsetto displaying a hint of rasp. The guitar hook made me think of an old Gilbert O'Sullivan song that I'm almost embarrassed to admit remembering, *Alone Again (Naturally)*, but I'm not sure why since there was no guitar to speak of in that song. There are even real strings and a trumpet solo.

My personal favorite from the album finds Joe going back to an older song from his days in the Scud Mountain Boys (1994-1997) and reinventing it as *Grudge F---* (2006). Think of *Let It Be* by the Beatles mixed with Badfinger's *Maybe Tomorrow* and Bread's *Make It With You*, and add more strings and lyrics so true they may make you cry. Even though the title suggests it, there's nary a curse word to be found.

Head to pernicebrothers.com for the full back story on the band and plenty of audio and video samples. For the past three months I have been unable to file this album away. I play it every day, on the radio, in my car, or at home. Every song sparkles, and like only the best albums, it's over far too soon. ■

Mike Marrone is program director of XM Satellite Radio's *The Loft*, a channel that focuses on an eclectic mix of singer-songwriters from the 1970s through the present.



PERNICE BROTHERS
Peyton Pinkerton,
James Walbourne,
Joe Pernice, and
Patrick Berkery

(TOP TO BOTTOM) BRAD TRENT; SETH KAYE



BY ROBERT PARKER

These Pinot Noirs Live Up to the Hype

THANKS TO THE 2004 MOVIE *Sideways*, pinot noir has become absurdly popular. Truth be told, most of this wine, whether domestic or imported, is of little interest and often overpriced. The following wineries' pinot noirs, however, display the true glories of this grape. All are from the 2004 vintage in California's Santa Rita Hills, the wine country northwest of Santa Barbara where the film takes place.

Sea Smoke Cellars

Botella

92 points. A dense ruby/purple hue is accompanied by aromas of black currants, black cherries, and a hint of flowers. Full body, sweet tannin, enough acidity to provide freshness and definition, and a textured, savory mouthfeel give this wine an early charm that makes it enjoyable now. Still, this pinot noir possesses enough concentration and length to last for a decade. \$30



long haul. Tremendous opulence, richness, and intensity in addition to a dazzling finish with great flavor precision result in one of the finest Central Coast pinot noirs I have ever tasted. It can be enjoyed over the next decade. \$64

Brewer-Clifton Melville Vineyard

95 points. First you notice a deep ruby color, and then you pick up wonderful aromas of forest floor, strawberry jam, black cherries, and flowers. In the mouth, notions of plums, cloves, and sweet cherries are presented in a broad, savory style with enormous richness and concentration but no sense of heaviness. This offering should drink well for 10 or more years. \$64

Foley Estate Rancho Santa Rosa

90 points. Cherry, plum, and pomegranate characteristics are present in this well-made, medium-bodied effort. With an enticingly plush texture, it represents California's version of a top-notch Beaune premier cru from Burgundy. \$38

Hartley-Ostini Hitching Post Rio Vista Vineyard

92 points. This pinot noir is a brilliant effort exhibiting aromas of flowers and forest floor intermixed with black cherries, plums, and currants. It's a complex, medium- to full-bodied wine with a deep ruby/purple color, sweet tannin, and enough acidity to provide zest and focus. It is a charming, seductive beauty to enjoy over the next five to seven years. \$40

Melville Clone 115 Indigène

95 points. Sweet forest floor, jammy cherry, strawberry, and a hint of blueberry-like aromas roar from the glass of this full-bodied wine. With fabulous intensity, as well as purity, and brilliant nuances, richness, and depth, it is a classic Santa Rita Hills pinot noir to drink over the next five to six years. \$42

Foxen Vineyard Sea Smoke Vineyard

96 points. This pinot noir's ruby/purple color and its intense, glorious perfume of sweet kirsch, black currants, flowers, and underbrush suggest a wine built for the

Sine Qua Non Covert

Fingers Arita Hills Vineyard

95 points. A knockout effort, this deep ruby/purple/plum-tinged pinot exhibits a slightly restrained nose, revealing sweet cranberry and cassis aromas interwoven with hints of flowers, charcoal, and oak, a savory, broad texture, and an opulent, voluptuous finish. This beauty should drink well for at least a decade, probably longer. \$75

Robert Parker is the world's most influential wine critic. Visit eRobertParker.com to see tens of thousands of tasting notes, buy his books, or subscribe to his newsletter, The Wine Advocate.

(PHOTO) JEROME REY/LA PROVENCE; (ILLUSTRATION) JASON SCHNEIDER

Wines rated from 96–100 are extraordinary; 90–95, excellent; 80–89, above average to very good. For more Parker picks, go to businessweek.com/extras

Meet the Funds That Perform

BusinessWeek's Scoreboard takes the guesswork out of picking mutual funds. **BY LAUREN YOUNG**

WHAT DO HUNTING DEER, PLAYING HOCKEY, and picking stocks have in common? They're all about taking the right shots. James Diedrich and Hal Goldstein, the 48-year-old co-managers of the \$1.6 billion First American Mid Cap Growth Opportunity Fund, always aim carefully. Diedrich journeys to the woods of Wisconsin to hunt deer with a bow and arrow. Since state game laws allow a bow hunter only one buck a year, "I see many deer before taking a shot," he says. Goldstein dons 10 pounds of gear to play wing in a hockey league. "I'm playing hockey for the fun and camaraderie," he says. "But when I get on the ice, I want to win." ♣ At their day jobs, the duo

applies the same kind of discipline to managing their investors' money. They zoom in on high-quality companies that are historically cheap yet show above-average earnings and revenue growth and strong cash flow. Instead of taking big bets on hot stocks, they spread their risk among 80 companies. When a stock hits its price target, these managers simply sell. Because of this disciplined investment strategy, First American Mid Cap Growth delivered an 11.2% average annual total return for the five years ending Dec. 31, vs. 6.4% for the typical mid-cap growth fund. That earned Diedrich's and Goldstein's fund an A rating from the *BusinessWeek* Mutual Fund Scoreboard

in the mid-cap growth fund category.

There may be mid-cap funds with better returns in any given year. But the scoreboard, which we've been publishing for more than 20 years, doesn't give much credibility to one-year wonders. Instead, it highlights funds that take the right shots again and again, year after year.

From a list of 6,061 stock and bond funds, the scoreboard identifies a select group that earned the best risk-adjusted returns in the past five years. That's why the scoreboard, available at businessweek.com/extras and updated monthly, is an ideal place to get fresh investment ideas or check up on what you already have in your portfolios.

In addition to turning up some unknown names, the scoreboard highlights dozens of standouts at giant mutual fund companies such as Vanguard, Fidelity Investments, T. Rowe Price, and American Funds. The scoreboard also includes exchange-traded funds so you can check on their track records and see how they measure up to their mutual fund rivals.

DRILLING DOWN

TO GET A RATING, a fund must have a performance history of at least five years. With data prepared for *BusinessWeek* by Standard & Poor's, which is also a unit of The McGraw-Hill Companies, we measure each fund's monthly performance for the past 60 months. When a fund fails to beat the return of risk-free 90-day U.S. Treasury bills, it earns negative marks, which are subtracted from the total return to come up with a risk-adjusted return. Funds are then ranked by their risk-adjusted returns from A (superior) through F (very poor). While the A funds are best, B+ or even B funds are still worth a serious look.

BusinessWeek awards two ratings to each fund. An overall rating evaluates the performance of equity funds against all other stock funds. (For bond funds, we compare taxable to other taxable bond funds, and do likewise with tax-free funds.) You'll find plenty of emerging-market and natural-resource funds among the 216 earning overall A ratings, which isn't a surprise given worldwide demand for commodities in the past few years. But to build a diversified portfolio, you need a lot more than investments based on emerging markets and natural resources.

That's where the category ratings come in handy. These are especially useful when you're trying to find a good fund in a sector that has been out of favor, such as large-cap growth or health care, and is unlikely to show up in the overall ratings. The scoreboard features ratings in more than 50 stock and bond categories, many of which you can find in the tables on pages 88 and 90. The rest is online at businessweek.com, along with data on 1-, 3-, 5-, and 10-year returns; sales charges; and expense ratios. To drill down further, you can examine portfolio data on a fund's risk and cash levels to unearth some real gems.

One common theme many A-rated funds share is a buy-and-hold philosophy, and the scoreboard also can help you identify funds with low portfolio



turnover. A good example is Baron Asset, a mid-cap growth fund with \$3.5 billion in assets, which delivered an admirable 10.8% annualized return in the past five years. Manager Andrew Peck takes a long-term view. "We're known for inquiring about earnings projections in 2011," Peck says. The purchase dates of some of the fund's top holdings are truly astounding: Manor Care in 1989, Charles Schwab in 1992, and Vail Resorts in 1997.

By sifting through the portfolio data, the scoreboard also helps you pinpoint funds that keep a lid on risk. (You can find a fund's risk level by clicking on "risk" at the top of the scoreboard.) Two standouts include AIM European Growth, which has an overall rating of A and an annualized 21.6% return during the past five years, and AIM Interna-

tional Small Company Fund, which has a category rating of A and a five-year annualized return of 33.4%. Both funds are designated by the scoreboard as "low-risk" offerings.

SMOOTHER SEAS, LOWER TAXES

CLAS OLSSON oversees AIM's international growth group from an unlikely perch: Austin, Tex. Considering that Olsson was once a naval officer in his native Sweden, it makes sense that he tries to provide returns that mimic smooth seas. One smart bet has been Puma, the German sports apparel manufacturer. At the start of the decade, Puma was an underutilized brand, though Olsson recognized its value as a fashion powerhouse. Instead of going head to head with Reebok and Nike in categories like basketball and running, Puma focused on the fash-



Tops In Equity Funds

BusinessWeek's Mutual Fund Scoreboard rates funds based on the past five years' pretax total returns, adjusted for risk. Here we show the equity funds that received A ratings for the best risk-adjusted returns against similar funds. You can find more categories, plus overall equity ratings at businessweek.com/extras.

FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*
» All-Cap					
CGM FOCUS CGMFX	17.2	SSGA LIFE SOLUTIONS GROWTH SSLGX	9.0	FIDELITY EXPORT & MULTINATIONAL FEXPX	8.9
FAIRHOLME FAIRX	15.1	T. ROWE PRICE CAPITAL APPRECIATION PRWCX	12.2	FIDELITY FIFTY FFTYX	9.9
HODGES HDPMX	18.0	T. ROWE PRICE PERSONAL STRATEGY BALANCED TRPBX	9.0	FORT PITT CAPITAL TOTAL RETURN FPCGX	13.2
KINETICS PARADIGM WWNPX	20.4	T. ROWE PRICE PERSONAL STRATEGY GROWTH TRSGX	9.9	GARTMORE NATIONWIDE LEADERS A GULAX	11.9
TEXAS CAPITAL VALUE & GROWTH TCVGX	15.5	VALUE LINE INCOME & GROWTH VALIX	8.9	GOLDMAN SACHS GROWTH & INCOME A GSGRX	10.5
THIRD AVENUE VALUE TAVFX	14.5	VANGUARD WELLINGTON INV. VWELX	8.9	HARTFORD CAPITAL APPRECIATION A ITHAX	11.2
YACKTMAN YACKX	13.3	» Foreign			
YACKTMAN FOCUSED YAFFX	13.7	AIM INTERNATIONAL SMALL COMPANY A IEGAX	33.4	HILLMAN ADVANTAGE EQUITY HCMTX	10.1
» Domestic Hybrid					
ALPINE DYNAMIC BALANCE ADBYX	9.6	AMER. CENTURY INTL. DISC. INV. TWEQX	21.5	LIFETIME ACHIEVEMENT LFTAX	12.8
AMER. BEACON BALANCED PLANAHEAD AABPX	9.2	AMER. CENTURY INTL. OPPORT. INV. AIOIX	28.7	MANAGERS AMG FIRST QUAD. TAX-MGD. U.S. EQ. I MFQTX	8.9
BRUCE BRUFX	29.4	ARTISAN INTERNATIONAL SMALL CAP INV. ARTJX	27.5	MANNING & NAPIER PRO BLEND MAX. TERM A EXHAX	9.7
CGM MUTUAL LOMMX	9.3	BLACKROCK INTL. OPPORTUNITIES INV. A BREAX	25.2	MANNING & NAPIER TAX-MANAGED SERIES A EXTAX	9.4
DELAWARE DIVIDEND INCOME A DDIAX	11.1	BOSTON COMPANY INTL. SMALL CAP SDISX	28.7	MARATHON VALUE MVPFX	8.7
DODGE & COX BALANCED DODBX	10.7	DREYFUS FOUNDERS PASSPORT F FPSSX	22.1	MASTERS SELECT VALUE MSVFX	9.6
FMI PROVIDENT TRUST STRATEGY FMIRX	9.1	DRIEHAUS INTERNATIONAL DISCOVERY DRIDX	21.6	MORGAN STANLEY EQUALLY WEIGHTED S&P 500 A VADAX	10.6
FIDELITY BALANCED FBALX	10.0	FIDELITY CANADA FICDX	21.5	NEUBERGER BERMAN SOCIALLY RESPONSIVE INV. NBSRX	10.3
FRANKLIN CUSTODIAN INCOME A FKINX	12.0	ISHARES MSCI AUSTRALIA INDEX EWA	24.5	PENN STREET ADV. SECTOR ROTATIONAL PORT. A PSRPX	12.2
GOLDMAN SACHS GR. & INC. STRATEGY A GOIAX	10.2	LAUDUS ROSENBERG INTL. SM. CAP INV. RISIX	27.2	RUSSELL LIFEPOINTS EQUITY GROWTH STRATEGY C RELCX	9.4
GOLDMAN SACHS GROWTH STRATEGY A GGSAX	11.5	OAKMARK INTL. SMALL CAP I OAKEX	25.0	SCHWAB MARKETTRACK ALL EQUITY SWEGX	9.0
GREENSPRING GRSPX	9.9	OPPENHEIMER INTL. SMALL COMPANY A OSMAX	32.1	TCW FOCUSED EQUITIES N TGFVX	8.9
INCOME FUND OF AMERICA A AMECX	11.0	QUANTITATIVE FOREIGN VALUE ORD. QFVOX	23.6	» Large-Cap Growth	
IVY ASSET STRATEGY A WASAX	13.7	T. ROWE PRICE INTL. DISCOVERY PRIDX	22.8	CALVERT LARGE CAP GROWTH A CLGAX	8.1
JAMES BALANCED GOLDEN RAINBOW GLRBX	9.2	THIRD AVENUE INTERNATIONAL VALUE TAVIX	21.5	COLUMBIA MARSICO 21ST CENTURY A NMTAX	15.9
LEUTHOLD CORE INVESTMENT LCORX	13.0	TOCQUEVILLE INTERNATIONAL VALUE TIVFX	21.9	COLUMBIA MARSICO FOCUSED EQUITIES A NFEAX	7.8
MANNING & NAPIER PRO BLEND EXT. TERM A MNBAX	9.0	VANGUARD INTERNATIONAL EXPLORER VINEX	22.9	FIDELITY ADV. DYNAMIC CAP. APPREC. T FRGTX	8.6
OAKMARK EQUITY & INCOME I OAKBX	9.9	» Large-Cap Blend			
PERMANENT PRPFX	13.6	BLACKROCK LARGE CAP CORE INV. C MCLRX	8.8	FIRST AMERICAN STRAT. AGGR. GR. ALLOC. Y FSAYX	8.1
		BRANDYWINE BLUE BLUEX	9.9	GARTMORE U.S. GROWTH LEADERS A GXXAX	8.1
		FIDELITY CAPITAL APPRECIATION FDCAX	9.9	GROWTH FUND OF AMERICA A AGTHX	8.0
				IVY CAPITAL APPRECIATION A WMEAX	8.0
				JANUS ADVISER FORTY S JARTX	8.3



PATIENT HUNTER
First American's
Diedrich takes a
long, hard look
before he shoots

ionable side of footwear, and now it is the epitome of cool. "Market share in the U.S. has risen from 1% to over 3%—that's still tiny, but there's a lot more room to go," Olsson says.

Another key component of the scoreboard is aftertax returns, which are much harder to identify than total returns. Our calculations are based on each year's highest federal tax rates for dividends and capital gains. For those trying to minimize the tax bite of their fund holdings, this information is especially useful.

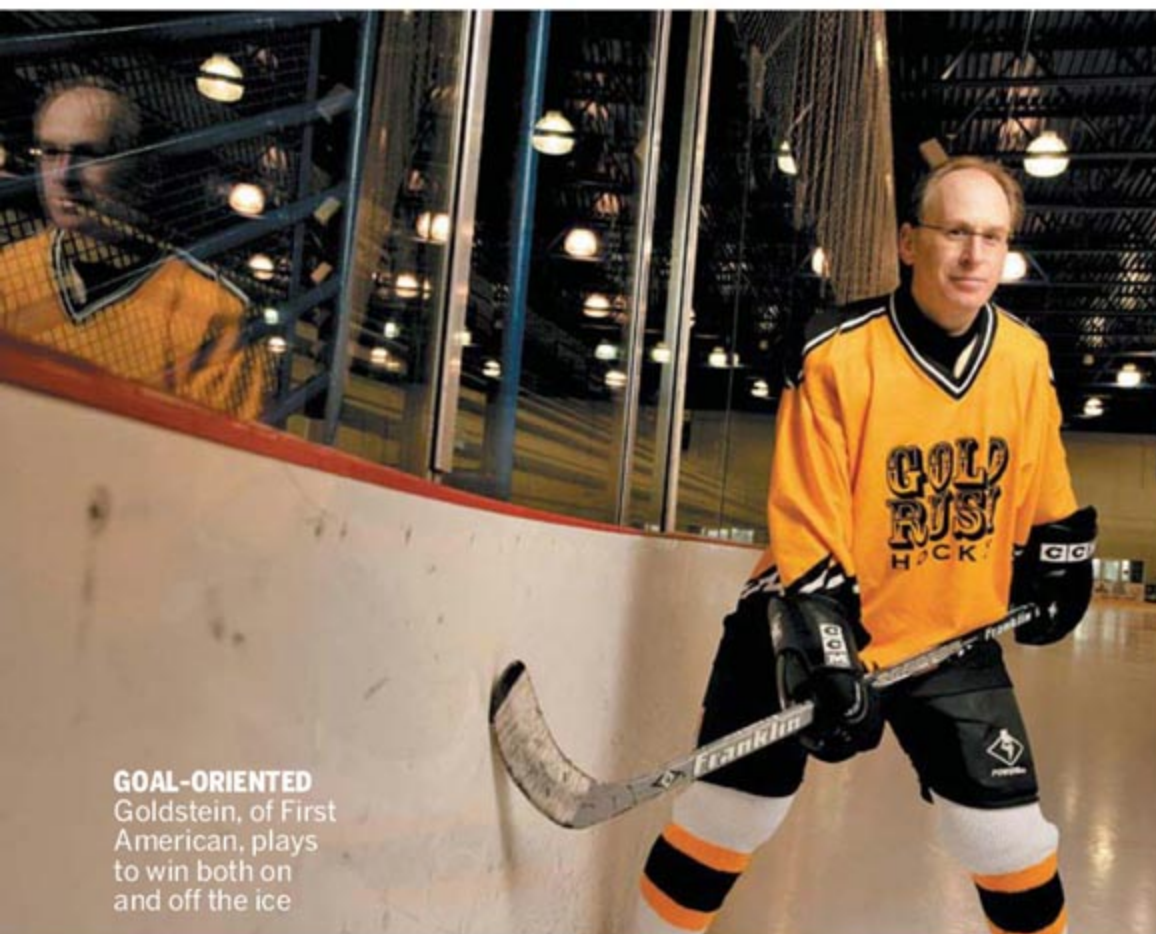
Investors have not sacrificed performance for a better tax bill at the A-rated Managers AMG First Quadrant Tax-Managed U.S. Equity Fund, a large-cap blend fund with \$85 million in assets. It has an 8.9% five-year annualized total return before taxes, and 8.8% after taxes. (The

typical large-cap blend fund delivered an annualized total return of 5.7% in the same time period.) The fund sells its losers in order to "harvest" losses to offset gains. "The fund has not distributed capital gains in the six years I've managed it," says manager Christopher Luck. Because the fund still has \$52 million in losses on its books, he doesn't expect to distribute a capital gain in the next three years, either.

The scoreboard will also guide you to the best bond fund opportunities. Under taxable funds, you'll find government funds, which own U.S. Treasury and agency-issued securities. General bond funds are covered, too, holding mainly corporate and government debt. Our more specialized fixed-income categories include high-yield and international bonds. The tax-exempt funds are

FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*
JANUS ASPEN FORTY INSTL. JACAX	7.9	» Mid-Cap Blend		BRIDGEWAY MICRO-CAP LIMITED BRMCX	12.8
JANUS TWENTY JAVLX	7.7	DELAWARE AMERICAN SERVICES A DASAX	15.2	BRIDGEWAY ULTRA SMALL COMPANY BRUSX	24.8
LEGG MASON GROWTH TRUST PRIMARY LMGTX	10.5	IMS CAPITAL VALUE IMSCX	14.2	COLUMBIA ACORN Z ACRNX	14.7
MARKMAN CORE GROWTH MTRPX	8.9	VANGUARD STRATEGIC EQUITY VSEQX	13.4	DREYFUS PREMIER ENTERPRISE A DPMGX	16.2
MARSICO 21ST CENTURY MXXIX	15.8	N/I NUMERIC INVESTORS MIDCAP NIGVX	13.8	FBR SMALL CAP FBRVX	20.8
MARSICO FOCUS MFOCX	7.8	» Mid-Cap Growth		HENNESSY CORNERSTONE GROWTH HFCGX	14.9
MARSICO GROWTH MGRIX	7.4	BARON ASSET BARAX	10.8	N/I NUMERIC INVESTORS EMERGING GROWTH NIMCX	15.0
RS GROWTH A RSGRX	7.6	COLUMBIA ACORN SELECT A LTFAX	13.3	OBERWEIS MICRO CAP OBMCX	15.1
RUSSELL TAX MANAGED GLBL. EQUITY S RTGSX	8.7	DREYFUS FOUNDERS MID CAP GROWTH F FRSPX	11.3	PERRITT MICRO CAP OPPORTUNITIES PRGX	20.2
STRATEGIC PARTNERS CAPITAL GROWTH M MARBX	6.7	FIRST AMERICAN MID CAP GROWTH OPPORT. Y FISGX	11.2	WASATCH MICRO CAP WMICX	13.5
TRANSAMERICA PREMIER EQUITY INV. TEQX	7.2	HUNTINGTON NEW ECONOMY HNETX	11.7	WILLIAM BLAIR SMALL CAP GROWTH N WBSNX	14.5
VANGUARD MORGAN GROWTH INV. VMRGX	6.5	LEGG MASON OPPORTUNITY TRUST PRIMARY LMOPX	14.3	» Small-Cap Value	
VANGUARD PRIMECAP VPMCX	8.4	MUNDER MID CAP CORE GROWTH A MGOAX	12.2	FIFTH THIRD MICRO CAP VALUE INSTL. MXAIX	18.7
WELLS FARGO ADVANTAGE CAPITAL GROWTH INV. SLGIX	6.6	RYDEX MID-CAP ADVANTAGE H RYMDX	11.0	GARTMORE SMALL CAP A GSXAX	19.1
» Large-Cap Value		USAA EXTENDED MARKET INDEX USMIX	11.9	HOTCHKIS & WILEY SMALL CAP VALUE I HWSIX	18.6
ALLIANZ NFJ DIVIDEND VALUE A PNEAX	12.9	VANTAGEPOINT MID/SMALL CO. INDEX II VPMSX	11.7	JAMES ADVANTAGE SMALL CAP JASCX	18.0
AMANA MUTUAL FUNDS TRUST INCOME AMANX	12.2	» Mid-Cap Value		MAINSTAY SMALL CAP OPPORTUNITY I MOPIX	18.6
AMER. BEACON LARGE CAP VALUE PLANAHEAD AAGPX	12.0	ARTISAN MID CAP VALUE ARTQX	17.0	N/I NUMERIC INVESTORS SMALL CAP VALUE NISVX	19.5
BLACKROCK LARGE CAP VALUE INV. A MDLVX	13.2	FIDELITY ADV. LEVERAGED CO. STOCK A FLSAX	26.0	PACIFIC ADVISORS SMALL CAP A PASMIX	20.0
DODGE & COX STOCK DODGX	12.8	HOTCHKIS & WILEY MID-CAP VALUE I HWMIX	17.9	RS PARTNERS A RSPFX	22.4
EXCELSIOR VALUE & RESTRUCTURING UMBIX	11.3	OPPENHEIMER SMALL & MID CAP VALUE A QVSCX	17.2	ROYCE VALUE PLUS SVC. RYVPX	21.6
FMI LARGE CAP FMIHX	10.8	RS VALUE A RSVAX	23.1	SCHNEIDER SMALL CAP VALUE SCMVX	24.3
HILLMAN FOCUSED ADVANTAGE HCMAX	13.9	» Small-Cap Blend		» World	
HOTCHKIS & WILEY LARGE CAP VALUE A HWLAX	14.0	AMER. CENTURY SMALL COMPANY INV. ASQIX	16.5	DWS GLOBAL OPPORTUNITIES S SGSCX	16.4
ING CORPORATE LEADERS TRUST SERIES B A LEXCX	11.5	BRIDGEWAY ULTRA SMALL COMPANY MARKET BRSIX	21.1	DELAWARE GLOBAL VALUE A DABAX	18.5
ISHARES RUSSELL 3000 VALUE INDEX IWW	10.9	CENTURY SMALL CAP SELECT INSTL. CSMCX	13.7	OAKMARK GLOBAL I OAKGX	18.8
JOHN HANCOCK CLASSIC VALUE A PZVFX	13.1	LAUDUS ROSENBERG U.S. DISCOVERY INV. RDIVX	14.4	PEARL AGGRESSIVE GROWTH PFAGX	16.1
LOOMIS SAYLES VALUE INSTL. LSGIX	11.2	MORGAN STANLEY INSTL. SMALL CAP VALUE MPSCX	14.1	POLARIS GLOBAL VALUE INVESTOR PGVFX	21.0
MUTUAL BEACON Z BEGRX	11.8	SATUIT CAPITAL MANAGEMENT MICRO CAP SATMX	16.7	TEMPLETON GLOBAL SMALLER COMPANIES A TEMGX	18.8
MUTUAL SHARES Z MUTHX	10.9	» Small-Cap Growth		VANGUARD GLOBAL EQUITY VHGX	17.7
PIONEER CULLEN VALUE A CVFCX	13.9	BOGLE SMALL CAP GROWTH INV. BOGLX	14.4		
RIVERSOURCE DIVERSIFIED EQUITY INCOME A INDZX	13.2				
TCW DIVIDEND FOCUSED N TGIGX	11.2				
TOUCHSTONE VALUE OPPORTUNITIES Z CCEVX	12.1				

*Appreciation plus reinvestment of dividends and capital gains before taxes. Jan. 1, 2002-Dec. 31, 2006 Data: Standard & Poor's



GOAL-ORIENTED
Goldstein, of First American, plays to win both on and off the ice

categorized by maturity, and whether they are national in scope or focused on a single state.

Since bond returns can be puny, pay careful attention to funds with low expenses, such as the A-rated \$4 billion Vanguard Intermediate Term Treasury Fund (Admiral Shares), which costs just \$10 for every \$10,000 invested. The flat yield curve has been a big challenge for fixed-income investors, which is why the fund has been buying shorter-term bonds to lower its sensitivity to interest rates. "With yields so low, there is less margin for error," says Robert Auwaerter, Vanguard's head of fixed income portfolio management.

As you may have heard, past results are no guarantee of future returns. But by using the scoreboard to find funds with higher ratings, lower risk, and minimal expenses, you can improve your odds for success. ■

BusinessWeek.com For more on the Mutual Funds Scoreboard, watch our weekly TV show, *BusinessWeek Weekend*.



To use our interactive fund table, go to businessweek.com/extras.

Tops In Bond Funds

Here we show the bond funds that received A ratings for the best risk-adjusted returns against similar funds. You can find more categories, plus overall bond fund ratings, at businessweek.com/extras.

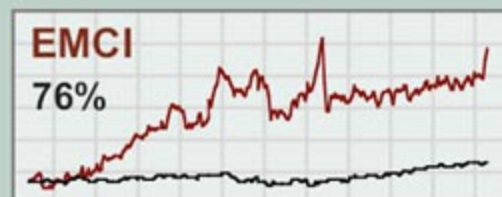
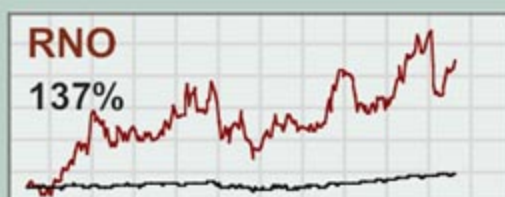
FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*	FUND/SYMBOL	AVERAGE ANNUAL TOTAL RETURN (%)*
» High-Yield		WESTCORE PLUS BOND WTIBX		» Municipal National-Long	
DELAWARE DELCHESTER A DETWX	12.0	WESTERN ASSET CORE BOND I WATFX	6.0	EATON VANCE NATIONAL MUNICIPALS A EANAX	8.9
DELAWARE HIGH YIELD OPP A DHOAX	11.7	WESTERN ASSET CORE PLUS BOND I WACPX	6.9	FIDELITY TAX FREE BOND FTABX	6.0
FIDELITY ADVISOR HIGH INCOME ADVANTAGE T FAHYX	14.0	» Intermediate Government		OPPENHEIMER AMT FREE MUNICIPAL BOND A OPTAX	7.9
FIDELITY CAPITAL & INCOME FAGIX	13.2	AMER. CENTURY TARGET MATURITY 2010 INV. BTTNX	5.7	T. ROWE PRICE SUMMIT MUNI INCOME PRINX	6.0
JOHN HANCOCK HIGH YIELD A JHHBX	13.8	FIDELITY MORTGAGE SECURITIES FMSFX	4.9	USAA TAX EXEMPT LONG-TERM USTEX	6.2
MAINSTAY HIGH YIELD CORP. BOND A MHCAIX	12.1	JPMORGAN MORTGAGE-BACKED SEC. SEL. OMBIX	5.0	» Short (General)	
REGIONS MORGAN KEEGAN SELECT HIGH INC. A MKHIX	12.2	PAYDEN GNMA R PYGNX	4.9	LEGG MASON PARTNERS LIFESTYLE INCOME A SCAAX	5.5
WM HIGH YIELD A CPHYX	12.5	TCW TOTAL RETURN BOND I TGLMX	5.5	PHOENIX MULTI-SECTOR SHORT-TERM BOND A NARAX	5.6
» Intermediate (General)		VANGUARD INTERM. TREASURY ADMIRAL VFILX	5.1	THOMPSON PLUMB BOND THOPX	4.7
BAIRD CORE PLUS BOND INV. BCOSX	5.9	» International Bond		VANTAGEPOINT MODEL SAVINGS ORIENTED GROWTH VPSOX	4.8
COLUMBIA INCOME Z SRINX	6.4	OPPENHEIMER INTERNATIONAL BOND A OIBAX	14.5	SCHWAB INV. YIELD PLUS SELECT SWYSX	3.4
CROFT-LEOMINSTER INCOME CLINX	7.0	PIONEER GLOBAL HIGH YIELD A PGHYX	15.3	» Short Government	
DELAWARE CORP. BOND A DGCAIX	7.8	TEMPLETON GLOBAL BOND A TPINX	12.9	ALLEGIANT GOVERNMENT MORTGAGE I AUSIX	4.3
JULIUS BAER TOTAL RETURN BOND A BJBGX	7.2	» Municipal National-Intermediate		DWS GNMA S SGINX	4.2
LEGG MASON INCOME INV. GRADE PRIMARY LMIGX	6.4	OPPENHEIMER LIMITED TERM MUNICIPAL A OPITX	7.1	MANAGERS INTERM. DURATION U.S. GOVT. MGIDX	4.4
MANAGERS BOND MGFIX	7.4	USAA TAX EXEMPT INTERMEDIATE-TERM USATX	4.9	PIMCO TOTAL RETURN MORTGAGE D PTMDX	4.9
MANAGERS FIXED INCOME INSTL. MFDYX	6.6	VANGUARD HIGH YIELD TAX-EXEMPT ADMIRAL VWALX	5.8	SENTINEL GOVERNMENT SECURITIES A SEGSX	4.9
PIMCO INVESTMENT GRADE CORPORATE BD. INSTL. PIGIX	6.9	VANGUARD INS. LONG-TERM TAX-EXEMPT ADMIRAL VILQX	5.6	» Ultrashort	
PARNASSUS FIXED INCOME PRFIX	5.8	WELLS FARGO ADVANTAGE INTERM. TAX-FREE INV. SIMBX	5.8	DWS SHORT DURATION PLUS INV. DBPIX	4.8
PIONEER BOND Y PICYX	6.3	WELLS FARGO ADVANTAGE MUNICIPAL BOND INV. SXFIX	6.8	SCHWAB INV YIELD PLUS SELECT SWYSX	3.4
REGIONS MORGAN KEEGAN SEL. INTERM. A MKIBX	6.8				
T. ROWE PRICE CORPORATE INCOME PRPIX	6.3				

*Appreciation plus reinvestment of dividends and capital gains before taxes, Jan. 1, 2002-Dec. 31, 2006 Data: Standard & Poor's

4 TOP COMPANIES: AVERAGE 141% RETURN

Equity Investor's Small-Cap Review

The companies featured were among America's top domestically traded, with market capitalizations from \$400 million to \$2 billion, in terms of 12-month share price performance for the period ending 11/30/06. While past performance is never a guarantee of future results, these companies represent investment opportunities worthy of any Small-Cap investor's close consideration.



12-Month Share Price Performance for the period ending 11/30/06

● Stock

● S&P500

Fuel Tech, Inc.

Symbol: FTEK

Industry: Energy

IR Contact: Tracy H. Krumme
tkrumme@fueltechnv.com

Fuel Tech is engaged in the development of environmentally sustainable technologies designed to optimize processes and improve efficiencies in air pollution control and energy production. Using proprietary software, chemical injection strategies are formulated to treat the liquid/solid fuels combusted by utilities and industrial plants.



- MARKET CAPITALIZATION: \$538 mil.
- 12-MO REVENUE GROWTH: 65%
- 12-MO PRE-TAX INCOME GROWTH: 152%
- LOW CAP EX & HIGH MARGINS
- CASH ON HAND: \$26 mil.

CDC Corporation

Symbol: CHINA (NASDAQ)

Industry: Enterprise Software

IR Contact: Monish Bahl
monishbahl@cdcsoftware.com

The CDC family of companies includes the following business units: CDC Software, a provider of enterprise software applications and services; CDC Mobile, a provider of mobile applications; CDC Games, a provider of online games; and China.com, a provider of Internet services for the greater China markets.



- SOFT. LIC. REV (SLR): \$11.9 mil. up 35% y/y
- SLR FROM NEW CUSTOMERS: 46%
- GUIDANCE REV FOR '07: \$401-\$411 mil.
- 3RD QTR '06 REV: \$78 mil.
- 3RD QTR ADJ. NET INCOME: \$10.1 mil.

Rio Narcea

Symbol: RNO (Amex)

Industry: Mineral Resources

IR Contact: Michelle Roth
michelleroth@rothir.com

Rio Narcea is a growing Canadian mineral resource company with operations, development projects and exploration activities in Spain, Mauritania and Portugal. The Company's Aguablanca nickel-copper mine is located in southern Spain. Its Tasiast gold project, in Mauritania, will be in production second half of 2007.



- MARKET CAPITALIZATION: \$413 mil.
- SHARE PRICE: \$2.63
- '06 9 MONTH NICKEL PROD.: 10.5 mil. lbs.
- EXPLORATION EXPENDITURES: \$8 mil.
- ADDED TO S&P/TSX GLOBAL GOLD IND.

EMC Insurance Group Inc

Symbol: EMCI (Nasdaq)

Industry: Insurance (P&C)

IR Contact: Anita Novak
anita.l.novak@emcins.com

EMCI owns subsidiaries with operations in property and casualty insurance and reinsurance and is the publicly-held insurance holding company of EMC Insurance Companies. Products are marketed through independent insurance agencies in 41 states.



- MARKET CAPITALIZATION: \$473 mil
- DIVIDEND YIELD (11/30/06): 1.9%
- PRICE TO EARNINGS (9/30/06): 6.5 TIMES
- ROE (9/30/06): 20.0%
- TOTAL ASSETS (9/30/06): \$1.2 bil



BY GENE G. MARCIAL

NO DEFENSE CUTS LOOM ON LOCKHEED MARTIN HORIZONS.

SEMPRA ENERGY IS FEELING A SURGE FROM ITS ACQUISITIONS.

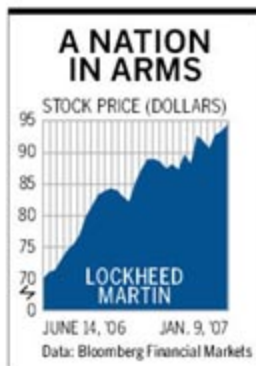
HOW THE THERMACOOL SKIN THERAPY FIRMS UP THERMAGE.

Lockheed: Rocketing Up

WORRIES THAT DEMOCRATS in Congress may roll back defense outlays doesn't faze fans of Lockheed Martin (LMT), the No. 1 maker of military weapons.

Although the Street has been cautious, with just 9 of 22 major analysts who track Lockheed bullish, the stock has rocketed from 72 in July to 94.66 on Jan. 10. One bull is Standard & Poor's Richard Tortoriello: The U.S. is "phasing out aging equipment," and Lockheed will benefit immensely, he says. Moreover, the threats from Iran and North Korea, plus the Iraq crisis, will make it tough to cut spending, he adds. The Defense Dept. has rejected plans of the Navy and Air Force to reduce the number of Lockheed F-35 Joint Strike Fighters they're buying.

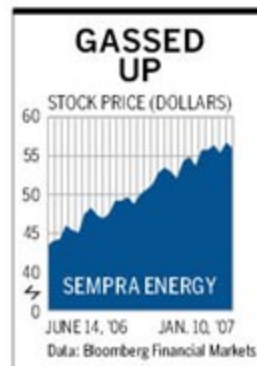
Lockheed primarily makes fighter planes, including the new F-35s that are to replace the aging planes such as F-16s. The F-35 program "will be the biggest, costing \$276 billion," says Tortoriello. Lockheed spokesman Tom Jurkowski says the F-35s will be operational, initially for the Marines, by 2012. Lockheed also makes space satellites, land-sea missiles, and electronic surveillance systems. "Lockheed's return on invested capital is solid," notes Tortoriello. It zoomed from 0.4% in 2000 to 17.5% in 2006. He sees earnings of \$5.50 a share for 2006 and \$5.75 in 2007. Goldman Sachs, which put Lockheed on its primary, "conviction" buy list, with a six-month target of 102, says the Defense budget for fiscal 2008 will boost the stock because it "will be favorable to Lockheed's programs."



Why Sempra Energy Is Electrified

SEMPRA ENERGY (SRE) is a utility in motion: It's partly switching from a utility into an acquirer and developer of energy assets. And its stock is energized, climbing from 43 in mid-June to 55.64 on Jan. 10. Michael Heim of A.G. Edwards, which has done business with Sempra, rates it a "buy," with a 12-month target of 60, and he believes the makeover should push the price higher. Currently, the stock is trading below its peer group. But Heim sees forces that could further lift Sempra. It owns San Diego Gas & Electric, with 1.3 million customers, and Southern California Gas, a distributor, with 6.4 million. Its other operations are unregulated, including energy trading,

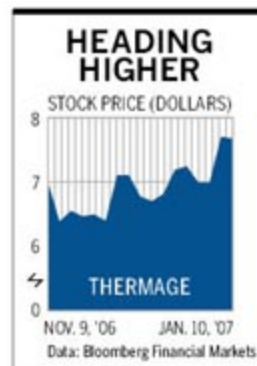
liquefied natural gas (LNG) terminals in North America, and gas pipelines and storage facilities in the U.S. and Mexico. Sempra may form a master limited partnership for these, he says. Paul Justice of Morningstar says: "We're particularly excited" by its entry into LNG and partnership with Kinder Morgan to build a pipeline from the Rockies to the Midwest. Both ventures should provide stable cash flow for years, he says.



Thermage's New Lift For Cosmetic Treatments

THERMAGE (THRM), a provider of noninvasive, tissue-tightening cosmetic treatments, has zigzagged since its initial trading on Nov. 9 at 7 a share; it is now at 7.66.

But some pros expect the stock will soar when Thermage's next-generation ThermoCool system is launched. CEO Stephen Fanning won't say exactly when the new version will come out, but he insists it will let cosmetic physicians do treatments much faster and more efficiently. With an O.K. from the Food & Drug Administration, ThermoCool, sold in 70 countries, uses a radio frequency (RF) generator that, through special tips, heats and shrinks collagen—tightening the epidermis and subcutaneous tissue—while cooling the skin's surface. The tips deliver the RF energy, cool the skin surface, and monitor skin temperature. Katherine Owen of Merrill Lynch, who rates Thermage a "buy," with a price target of 12, in a report describes the stock as a "pure play investment in the noninvasive aesthetic market." Key Nakae of C.E. Unterberg Towbin, also with a "buy," says the technology penetrates more deeply than laser and is better suited for other uses, such as body shaping and contouring. One treatment lasts two to three years, he says. ■



BusinessWeek.com Gene Marcial's Inside Wall Street is posted at businessweek.com/investor at 5 p.m. EST on the magazine's publication day, usually Thursdays.

Note: Unless otherwise noted, neither the sources cited in Inside Wall Street nor their firms hold positions in the stocks under discussion. Similarly, they have no investment banking or other financial relationships with them.

STOCKS



COMMENTARY

Stocks drooped a bit in the year's first full week of trading. While Apple's shares rose on its iPhone introduction, that news wasn't so good for cell-phone maker Motorola, which fell 11.7%. Goodyear Tire & Rubber rose after it settled its strike. Earnings season also started to warm up; Sprint Nextel shares fell as its 2007 sales forecast was below expectations.

Data: Bloomberg Financial Markets, Reuters

U.S. MARKETS

	JAN. 10	WEEK	% CHANGE YEAR TO DATE	% CHANGE LAST 12 MONTHS
S&P 500	1414.9	-0.1	-0.2	9.7
Dow Jones Industrials	12,442.2	-0.3	-0.2	13.0
NASDAQ Composite	2,459.3	1.5	1.8	6.0
S&P MidCap 400	806.1	-0.1	0.2	4.5
S&P SmallCap 600	395.1	-1.0	-1.2	7.0
DJ Wilshire 5000	14,187.0	-0.1	-0.2	9.5

SECTORS

	JAN. 10	WEEK	% CHANGE YEAR TO DATE	% CHANGE LAST 12 MONTHS
BusinessWeek 50*	796.3	0.3	-0.3	2.5
BW Info Tech 100**	446.4	-1.6	-0.2	11.0
S&P/Citigroup Growth	652.9	0.3	0.1	5.8
S&P/Citigroup Value	760.2	-0.5	-0.5	13.8
S&P Energy	421.8	-3.9	-7.4	5.7
S&P Financials	494.2	-0.5	-0.2	12.8
S&P REIT	200.9	1.0	1.0	23.3
S&P Transportation	260.2	-1.6	-1.4	4.6
S&P Utilities	183.7	-2.0	-1.6	12.9
GST Internet	201.2	0.4	0.7	-7.1
PSE Technology	898.7	2.6	2.7	2.0

*March 19, 1999=1000 **February 7, 2000=1000

GLOBAL MARKETS

	JAN. 10	WEEK	% CHANGE YEAR TO DATE	% CHANGE LAST 12 MONTHS
S&P Euro Plus (U.S. Dollar)	1941.4	-3.5	-2.4	23.8
London (FT-SE 100)	6160.7	-2.5	-1.0	8.3
Paris (CAC 40)	5502.0	-1.9	-0.7	13.2
Frankfurt (DAX)	6566.6	-1.9	-0.5	19.5
Tokyo (NIKKEI 225)	16,942.4	-1.6	-1.6	5.1
Hong Kong (Hang Seng)	19,568.3	-4.1	-2.0	25.7
Toronto (S&P/TSX Composite)	12,457.6	-1.9	-3.5	7.4
Mexico City (IPC)	25,885.8	-2.8	-2.1	36.9

FUNDAMENTALS

	JAN. 9	WEEK AGO	YEAR AGO
S&P 500 Dividend Yield	1.79%	1.79%	1.75%
S&P 500 P/E Ratio (Trailing 12 mos.)	17.7	17.8	18.2
S&P 500 P/E Ratio (Next 12 mos.)*	14.7	15.4	15.0
First Call Earnings Surprise*	8.37%	8.10%	9.13%

*First Call Corp.

TECHNICAL INDICATORS

	JAN. 9	WEEK AGO	YEAR AGO
S&P 500 200-day average	1321.0	1318.3	Positive
Stocks above 200-day average	67.0%	74.0%	Neutral
Options: Put/call ratio	0.78	0.79	Positive
Insiders: Vickers NYSE Sell/buy ratio	6.41	6.47	Negative

BEST-PERFORMING GROUPS

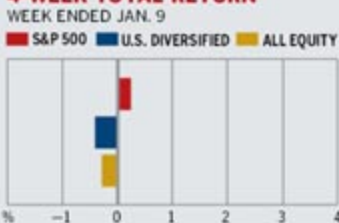
	LAST MONTH %		LAST 12 MONTHS %
Tires & Rubber	40.1	Steel	61.7
Real Estate Mgt. & Dvpt.	8.5	Tires & Rubber	40.0
Forest Products	7.0	Investmt. Bnkg. & Brkrge.	37.4
Computer Hardware	6.2	Broadcasting	37.2
Health-Care Supplies	5.4	Intgrd. Telecmms. Svcs.	35.6

WORST-PERFORMING GROUPS

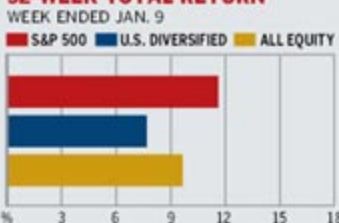
	LAST MONTH %		LAST 12 MONTHS %
Coal	-19.6	Education Services	-35.0
Oil & Gas Equipment	-14.1	Homebuilding	-32.5
Oil & Gas Refining	-12.7	Gold Mining	-27.3
Steel	-12.4	Internet Software	-23.8
Oil & Gas Exploration	-11.6	Oil & Gas Refining	-19.9

MUTUAL FUNDS

4-WEEK TOTAL RETURN



52-WEEK TOTAL RETURN



Data: Standard & Poor's

EQUITY FUND CATEGORIES

4-WEEK TOTAL RETURN	%	52-WEEK TOTAL RETURN	%
LEADERS			
Pacific/Asia ex-Japan	4.4	Pacific/Asia ex-Japan	32.6
Diversified Pacific/Asia	1.0	Latin America	28.1
Technology	0.9	Europe	26.4
Japan	0.8	Real Estate	24.8
LAGGARDS			
Natural Resources	-7.3	Japan	-5.3
Precious Metals	-6.4	Natural Resources	1.0
Utilities	-2.1	Health	1.6
Small-cap Value	-1.2	Technology	2.3

EQUITY FUNDS

4-WEEK TOTAL RETURN	%	52-WEEK TOTAL RETURN	%
LEADERS			
Dreyfus Prem. Grtr. China A	13.3	Dreyfus Prem. Grtr. China A	76.8
iShares FTSE Xha. Ch. 25Idx.	10.3	Oberweis China Opport.	69.4
PowerShares Gldn Drgn China	10.0	Old Mut. Clay Finlay Ch. A	68.3
Matthews China	9.4	iShares FTSE Xha. Ch. 25Idx.	64.5
LAGGARDS			
Dunham Real Estate Stock C	-21.1	Ameritor Investment	-85.7
Dunham Small Cap Value C	-17.0	DireXn. Emrg. Mkts. Short	-37.2
ProFunds Oil Equip., Svcs.	-16.0	Fidelity Japan Small Co.	-26.1
Dunham Emrg. Mkts. Stock C	-15.0	American Heritage Grth.	-25.0

INTEREST RATES

KEY RATES

	JAN. 10	WEEK AGO	YEAR AGO
Money Market Funds	4.86%	4.87%	3.83%
90-Day Treasury Bills	5.09	5.05	4.29
2-Year Treasury Notes	4.81	4.76	4.40
10-Year Treasury Notes	4.69	4.66	4.43
30-Year Treasury Bonds	4.77	4.76	4.61
30-Year Fixed Mortgage†	6.02	6.04	6.08

† BancQuote Inc.

BLOOMBERG MUNI YIELD EQUIVALENTS

Taxable equivalent yields on AAA-rated, tax-exempt municipal bonds, assuming a 30% federal tax rate.

	10YR. BOND	30YR. BOND
General Obligations	3.77%	4.14%
Taxable Equivalent	5.39	5.91
Insured Revenue Bonds	3.94	4.44
Taxable Equivalent	5.63	6.34

THE WEEK AHEAD

PRODUCER PRICE INDEX

Wednesday, Jan. 17, 8:30 a.m. EST

» Producer prices are forecast to have grown 0.5% in December, after a 2% surge in November. That's the consensus among economists surveyed by Action Economics. Minus food and energy, prices likely inched up 0.1%, following a 1.3% jump.

INDUSTRIAL PRODUCTION

Wednesday, Jan. 17, 9:15 a.m. EST

» December factory output

probably rose 0.2% for a second straight month. The utilization rate very likely edged up to 81.9%, from 81.8% in November.

BEIGE BOOK

Wednesday, Jan. 17, 2 p.m. EST » Federal Reserve releases its overview of economic conditions before the Jan. 31 monetary policy meeting. Economists fully expect the Fed to hold interest rates at 5.25%.

CONSUMER PRICE INDEX

Thursday, Jan. 18, 8:30 a.m. EST

» In December, consumer prices most likely increased 0.3%, after holding steady in November. Minus energy and food, the index probably climbed 0.2% after no change in the prior month.

RESIDENTIAL CONSTRUCTION

Thursday, Jan. 18, 8:30 a.m. EST » December housing starts probably eased to an annual rate of 1.55 million. Starts in November rebounded slightly, to an annual pace of 1.59 million.

The *BusinessWeek* production index improved to 286.2 for the week ended Dec. 30, a 6% increase from a year ago. Before calculation of the four-week moving average, the index eased to 289.3.

BusinessWeek .com

For the BW50, more investment data, and the components of the production index visit www.businessweek.com/extras

**It's about money.
Earning it.
Investing it.
Spending it.**



**Check out this weekend's show
January 13 and 14:**

Consumer Electronics Show: Content from media companies is driving the introduction of all-in-one tech devices.

Hottest Gadgets: The best new offerings straight from CES.

Detroit Auto Show: Highlights include latest models, concept cars, and eco-friendly vehicles.

Car Shopping Online: Why people use the Internet to search, but buy on the lot.

Mutual Fund Scoreboard: How to pick the right funds for your portfolio.

BusinessWeek weekend

Airs Saturday/Sunday nationwide.
Find your local station and airtime by
zip code at businessweekweekend.com

Company Index

This index gives the starting page for a story or feature with a significant reference to a company. Most subsidiaries are indexed under their own names. Companies listed only in tables are not included.

A

A.G. Edwards (AGE) 92
AIM European Growth (AEDAX) 86
AIM International Small Company Fund (IEGAX) 86
Aishin Seiki 54
Amazon.com (AMZN) 58, 64
America Móvil (AMX) 34
American Funds 86
AOL (TWX) 58
Apple (AAPL) 10, 22, 26, 28, 34, 40, 64
AstraZenica (AZN) 36
Avenue A/Razorfish 75

B

BabyAge.com 75
Barclays (BCS) 58
Baron Asset (BARAX) 86
Baugur 64
Best Buy (BBY) 75
Black & Decker (BDK) 64
Blackstone Group 46
BP (BP) 52
Burger King (BKC) 34

C

Calvert 39
Canberra Industries 73
CANTV (VNT) 34
Carlyle Group 46
CBS (CBS) 28
C.E. Unterberg Towbin 92
Charles Schwab (SCHW) 86
Christian & Timbers 64
Cingular Wireless 40
Citigroup (C) 52
CNBC 34
Coca-Cola (KO) 51
Computer Sciences (CSC) 76
Consolidated-Tomoka Land (CTO) 39
Continental (CAL) 34
Converse (NKE) 80
Cooltrader 64
Cypress Semiconductor 64

D

DaimlerChrysler (DCX) 19
DC Shoes 80
Delphi (DPHIQ) 22
Delta Air Lines (DALRQ) 34
Denso (DNZOY) 54
Deutsche Bank (DB) 39
Digitas (DTAS) 19
Domino Foods 72
DoubleClick 75

E

eBags 75
eCost.com 75
Exelon (EXC) 78

Expedia (EXPE) 76
Exxon Mobil (XOM) 52, 36

F

Fidelity Investments 34, 86
First American Mid Cap Growth Opportunity Fund (frslx) 86
First Multiple Listing Service 44
FKF Applied Research 19
Florida Crystals 72
Ford (F) 19
Franklin Mutual Advisers (BEN) 39
Frankly Real Estate 44

G

Gap (GPS) 34, 64
GE (GE) 34, 73, 78
Genentech (DNA) 34
Gimme Credit 76
Glocap Search 46
GM (GM) 22, 54, 75
Goldman Sachs (GS) 34, 36, 39, 58, 92
Google (GOOG) 14, 28, 75
GramT 56
Guerite Advisors 13

H

HarperCollins (NWS) 16
Heidrick & Struggles (HSII) 36
Hershey (HSY) 76
Hewlett-Packard (HPQ) 36, 64
Highland Capital Management 22
Home Depot (HD) 22, 36, 39, 64, 76
Honeywell (HON) 73
Huntington New Economy (HNEAX) 86
Hurley 80

I

IBM (IBM) 82
ICE.com 75
Iceland Foods 64
Ingres 64

J

Javelin Group 80
J. Crew (JCG) 64
JPMorgan Chase (JPM) 32

K

Katzenbach Partners 46
Kinder Morgan (KMI) 92

L

Liberum Research 16
Lockheed Martin (LMT) 36, 92
Logitech (LOGI) 26

M

Manor Care (HCR) 86
MarketingPilgrim 75
McAfee (MFE) 14
McDonald's (MCD) 19
McGraw-Hill (MHP) 58
MedImmune (MEDI) 34
Medtronic (MDT) 36
MEMC Electronic Materials (WFR) 86
Merrill Lynch (MER) 39, 92
Methode Electronics (METH) 36
Metropolitan Regional Information Systems 44
Microsoft (MSFT) 10, 26, 58, 82
MLS Property Information Network 44
M:Metrics 40
Morgan Keegan 73
Morgan Stanley (MS) 36, 39, 52, 58, 76
Morningstar (MORN) 92
Motorola (MOT) 40
MTV Networks (VIA) 28
Munder Mid Cap Core Growth (MGOAX) 86
MySpace.com (NWS) 75

N

NASDAQ (NDAQ) 13
NBC (GE) 51
NetSuite 14
Newell Rubbermaid (NWL) 64
New York Times (NYT) 39
Nike (NKE) 80, 86
Northwest (NWACQ) 34
Northwest Multiple Listing Service 44
Novartis (NVS) 36
NPD Group 80
NYSE (NYSE) 13, 64

O

Omnivat Properties 16
Option One Mortgage 22
Oracle (ORCL) 64

P

Palm (PALM) 40
Payless ShoeSource (PSS) 80
Phoenix Audio Video 82

Q, R

Qihoo.com 22
Quiznos 34
Raytheon (RTN) 73
Re/Max 100 44
Reebok 86
Research In Motion (RIMM) 10, 40
Royal Dutch Shell (RDS) 52

S

salesforce.com (CRM) 14

Satyam Computer (SAY) 56
Sempra Energy (SRE) 92
Shutterfly (SFLY) 36
Sirius Satellite Radio (SIRI) 34
Skechers (SKX) 80
Sling Media 28
SportScanINFO 80
Standard & Poor's (MHP) 76, 92
Steve & Barry's 80
Sumitomo Titanium 58

T

Techtronic Industries 64
Teléfonos de Mexico (TMX) 34
Tenet Healthcare (THC) 95
Texas Pacific 64
Thermage (THERM) 92
Thermo Fisher Scientific (TMO) 73
Time Warner (TWX) 39
TiVo (TIVO) 28
Toyota (TM) 19, 54
T. Rowe Price (TROW) 86
Tupperware Brands (TUP) 36

U, V

UBS (UBS) 39
United Air Lines (UAUA) 34
US Airways (LCC) 34
U.S. Sugar 72
Vail Resorts (MTN) 86
Vanguard 86
Vans (VFC) 80
Verizon (VZ) 34

W

Wal-Mart (WMT) 14, 22, 34, 58, 75, 98
Warner Books 16
Warner Music (WMG) 36
Wells Fargo (WFC) 58
Westinghouse 78
Weyerhaeuser (WY) 39
Wintergreen Advisers 39
Wintergreen Fund (WGRNX) 39
Wipro (WIT) 56

X, Y

XM Satellite Radio (XMSR) 34
Yahoo! (YHOO) 58, 75
YouTube 75

Z

Zale (ZLC) 75

Open-Heart Nightmare

CORONARY A True Story of Medicine Gone Awry
By Stephen Klaidman; Scribner; 303pp; \$25

Open-Heart Nightmare

CORONARY A True Story of Medicine Gone Awry
By Stephen Klaidman; Scribner; 303pp; \$25

In 2002 a Catholic priest named John Corapi had his heart checked out by Dr. Chae Hyun Moon. The celebrated cardiologist, who practiced at a Redding (Calif.) hospital owned by giant for-profit Tenet Healthcare Corp., responded to Corapi's symptoms of exhaustion and shortness of breath with five of the

scariest words in the English language: "You need a triple bypass."

Thus begins the tale of the priest, the doctor, and the multibillion-dollar hospital chain, recounted in penetrating detail in *Coronary: A True Story of Medicine Gone Awry*. Fortunately, as author Stephen Klaidman reports, Corapi then got opinions from three other doctors, all of whom said no surgery was needed since his arteries were completely healthy. The priest went to the FBI. An ensuing investigation and a raft of civil lawsuits turned up more than 600 patients who were allegedly subjected to unnecessary heart procedures by Moon and a colleague, Dr. Fidel Realyvasquez. The scandal, along with simultaneous revelations that Tenet may have improperly billed Medicare by as much as \$760 million a year, brought what was the nation's second-largest hospital chain to its knees. And it provided forceful evidence that the drive for profits can put patients in mortal danger.

Klaidman, an ex-reporter at *The New York Times* and *The Washington Post* and a former health-policy researcher, deftly intertwines elements of a medical mystery story with disturbing details about corporate greed. So profit-focused was Tenet, Klaidman discovered, that it required each hospital CFO to submit monthly reports on individual doctors' contributions to the bottom line. Redding Medical Center (RMC), home base to Moon and Realyvasquez, was a cash cow, generating \$3,181 in revenue per patient per day, or twice Tenet's average. What's more, in 2002 its pretax income soared 31%, to \$93.6 million. Drawing on medical records, depositions, FBI files, and interviews, Klaidman brings this culture to life, offering vivid dialogue and scene-setting.

A novelist would be hard-pressed to invent more outsize characters. Colleagues and other doctors portray Moon and Realyvasquez as egomaniacs who battled with each other and didn't win many friends among their patients, either. Realyvasquez was so foul-mouthed that RMC's CEO felt compelled to report him to Tenet's top brass. And more than

once, a nurse recalled, Moon rattled his terrified patients by remarking: "I'm going to save your life. This is your lucky day." Then there's the whistleblowing priest, whose story provides one of the book's most fascinating chapters. A former accountant and real estate broker, Corapi got caught up in the Los Angeles drug scene in the 1970s, even attending the party where comedian John Belushi was on the night he died. Homeless and strung out on cocaine, Corapi decided to turn his life around and entered the priesthood at age 37.

Equally compelling are Klaidman's stories of patients who weren't so lucky. There was the ex-railroad worker who had lost part of one leg in a boxcar accident and had to have a vein taken from his good leg for a quadruple bypass. Then there was the grandmother who suffered debilitating strokes after her heart surgery. Later, physicians hired by a personal-injury lawyer determined that both patients' procedures were unnecessary.

In the midst of such gripping drama, Klaidman never forgets that, at its core, this is a tale of a company that seems to have cracked under pressure from Wall Street to continually boost profits. Just one day before the FBI raided RMC to collect evidence on Moon and Realyvasquez, an analyst reported that Tenet had been raising prices in order to benefit from the extra fees Medicare paid for "outliers"—patients who have extraordinarily expensive procedures such as those performed by RMC's cardiac unit.

The coincidence is not lost on Klaidman: He says RMC was near the top of the list of outlier abusers, generating 59% of its pretax income from the fees.

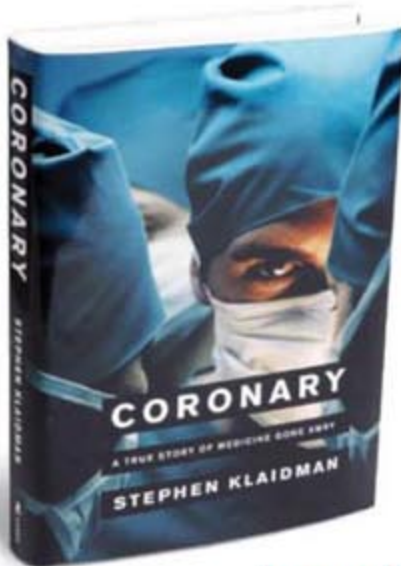
Coronary's only failing may be the ending of its story. After hearing so many shocking tales, we expect the hand of justice to crush Moon and Realyvasquez. In fact, the U.S. Justice Dept. did not bring criminal charges against the pair. They and Tenet settled the civil cases for \$450 million.

A medical mystery—and a shocking account of corporate greed

Moon and Realyvasquez left medicine. Tenet also paid the U.S. government \$900 million to settle claims regarding alleged improper financial activities. The company, now a shadow of its former self, "has taken many steps to improve clinical quality and compliance oversight," says a Tenet spokesman.

Klaidman succeeds at casting a light on the all-too-frequent association of medicine and profit-mongering. And he leaves readers with a stark and enduring lesson: Never underestimate the importance of a second opinion. ■

—By Arlene Weintraub





Earmarking the Earmarks

The new Congress has agreed to take action on earmarks, the budget items better known as “pork projects.” Think, for instance, of the \$13.5 million that helped subsidize 2005’s World Toilet Summit in Northern Ireland, an expenditure worthy of jests about fiscal incontinence. In a mostly party-line 280-152 vote last week, the House passed changes to rules requiring

that both the spending projects and their sponsors be disclosed on the Internet at least 48 hours before they are considered on the floor. Members of Congress will also be required to justify the public need for the expenditures and to certify that they won’t benefit financially from them.

Nobody can really object to such a reform. It’s certainly a good idea to shed some light on what the now-convicted *über*-lobbyist Jack Abramoff once called the “favor factory.” But we should be realistic about what these reforms can achieve. Sadly, their impact is likely to be minimal.

For starters, some supporters of the change hope the number of egregious earmarks will decline because members of Congress will be too ashamed to attach their names to them. But as anyone who has driven over the Senator Robert C. Byrd Bridge knows, the problem isn’t that lawmakers don’t want their names affiliated with most earmarked projects. It’s that so many of them *do*.

In the past, the sponsors behind earmarked items remained anonymous, and it was possible for congressmen all to take credit for a single project. There was no official way to verify who was telling the truth. Now there is. Think of it as intellectual-property protection for government waste. And just as intellectual-property protection for inventions presumably creates an incentive to innovate, earmark transparency might also lead to a rise in the number and cost of earmarks.

BEFORE, YOU’D OFTEN be able to figure out which member of Congress was tied to what earmark. The 2005 Highway Bill, for instance, included specific earmarks for particular cities or roadways. Some line items in the bill went so far as to identify a specific highway exit number. Any savvy reporter sitting down with a road map and a congressional district map could discover who probably delivered the earmark. Yet even that fledgling form of transparency didn’t have an overall effect on the amount of pork in the bill. For instance, once the “Bridge

to Nowhere” in Alaska was exposed and soon became synonymous with wasteful road projects, representatives of the state—particularly Republican Senator Ted Stevens—never flagged in their support of it.

Even if transparency leads to fewer earmarks, there are no promises these projects won’t reappear in other ways and other places. The congressional budget process is nothing if not a game of reinvention. You could call spending items Happy Funtime Projects instead and sock them away in another part of the budget, but they will remain the coin of the realm on K Street.

Of course, Congress could simply give a bucket of money to an agency with no strings attached. But then a member of the Appropriations Committee would write a letter to the department head suggesting something like: “Gee, wouldn’t it be nice if Project X got some of this pot of money?”

Can you really blame a government department head who reads a letter like that—from a member of Congress who controls his budget and oversees his agency—and obliges? It would strike anyone in that position as similar to Tony Soprano saying to the corner grocery store owner: “Nice little place you got here. Damn shame if anything were to happen to it.”

So we probably won’t soon see an end to federal handouts, like the half-million dollars in taxpayer cash that in 2005 went to the Sparta Teapot Museum in North Carolina. Earmark transparency is merely a beginning. A good first step for sure, but hardly the endgame of fundamental budget reform. Indeed, future reforms should create an incentive to reduce the scope of government overall. In the meantime, it’s important to remember that as long as a culture of spending persists in Washington—fueled by a budget process that allows Uncle Sam to be all things to all people—then no matter who is in power, earmarking in some form will always be with us. ■

Stephen Slivinski, director of budget studies at the Cato Institute, is author of *Buck Wild: How Republicans Broke the Bank and Became the Party of Big Government*.

Views expressed in *Outside Shot* are solely those of contributors.

From the company that pioneered
noise reducing headphones.

The next step.

NEW Bose® QuietComfort® 3 Acoustic Noise Cancelling® Headphones

Now you have a choice. We began researching noise reduction technology 28 years ago. Since then, we've been leading the industry in advancing the category we created.

New QuietComfort® 3 headphones represent the latest achievement. They rest on your ears rather than surrounding them. And while they are smaller than our highly acclaimed QuietComfort 2 headphones, there is no compromise in noise reduction, sound quality or comfortable fit. So now you have a choice: QC™2 headphones for around-ear use, and new QC3 headphones if you prefer a smaller, on-ear alternative.



QC2 headphones (left).
New QC3 headphones (right).

The challenge of reducing size. With conventional technology, smaller earcups compromise performance. So we launched a research project to explore whether it was possible to overcome the performance limitations of smaller size and on-ear design. The result is our new QC3 headphones that match the noise reduction and audio quality benefits of our award-winning QC2 headphones.

Hear the difference Bose® technology makes. You will notice a dramatic decrease in engine roar on a plane. The cabin becomes more peaceful. Connect your CD player, MP3 player, or listen to the in-flight movie. You'll hear detail you may have never experienced while flying.

But use them at home or at the office, too. Although the noise reduction will be more subtle, you should notice distractions fading softly into the background.



Fold-flat design
for easy storage.



Try them for 30 days at no risk. Choose new QC3 headphones for an on-ear fit, or QC2 headphones for an around-ear design. Both come with our 30-day Excitement Guarantee. Order now for a free MP3 player (a \$50 value) featuring music selected by Bose. Easily add/remove songs, and use it to enjoy your QuietComfort headphones even more. Take advantage of **12 easy payments**, with no interest charges from Bose.* And ask about our optional Cell Connect cable for use with select music-enabled mobile phones. QuietComfort headphones.

FREE MP3 player
when you order
by January
31, 2007.



Engineered exclusively by Bose, the
most respected name in sound.

To order or learn more about Bose headphones:
1-800-901-0256, ext. Q5354
www.Bose.com/qc3

BOSE®
Better sound through research®

*Bose payment plan available on orders of \$299-\$1500 paid by major credit card. Additional financing offers may be available for select products. See website for details. Down payment is 1/12 the product price plus applicable tax and shipping charges. Then, your credit card will be billed for 11 equal monthly installments with 0% APR and no interest charges from Bose. Credit card rules and interest may apply. U.S. residents only. Limit one active financing program per customer. ©2006 Bose Corporation. Patent rights issued and/or pending. Financing and free MP3 player offer not to be combined with other offers or applied to previous purchases, and subject to change without notice. If QuietComfort® headphones are returned, the MP3 player must be returned for a full refund. Risk free refers to 30-day trial only and does not include return shipping. Delivery is subject to product availability.



The Hot Buttons of 2006

WHEN WE STARTED THIS COLUMN A YEAR AGO, IT FELT A BIT like setting out on a journey without a map or destination. All we had to guide us, so to speak, was our collective experience and a real interest in answering questions about...well, whatever readers wanted to ask about. And ask they did. In 2006 this column received close to 10,000 e-mails from around the world with questions ranging from "Should I take a job at McKinsey or start a company doing something I really love?" to "Will the Chinese ever revalue their currency to reflect its real strength?"

But if the breadth of questions surprised us, we were even more taken aback by the impassioned reaction to some of our answers. Yes, some columns came and went without much noise. But many—four in particular—sparked exceptional sound and fury. And so before launching into another year of questions and answers, we'd like to take a look back at the tallest lightning rods of the one just past.

First, our column "What's Holding Women Back" made the case that the relatively small number of women CEOs today was not, generally speaking, the result of a cabal of sexist male executives but of biology—or put more bluntly, babies. Not that working mothers can't function; many never miss a beat. But many others intentionally remove themselves from the corporate escalator to spend more time at home. Thus, we said, there's no villain in this situation, only the reality that sometimes life requires tough choices, and with those choices, an acceptance of their personal or career consequences.

But not if you're a man, many readers quickly retorted. In fact, many of the e-mails about this column argued that there would be more women CEOs if husbands simply shared child-rearing responsibilities. Still others asserted that the problem lies not with errant husbands but with the male power Establishment, which persists in valuing exactly what working mothers are most hard-pressed to deliver: availability. "The system is rigged against women," one reader wrote. "You let it off too easy."

EMOTIONS ALSO RAN HIGH about our column "Are You a Boss Hater?" in which a reader asked why, in his long career, he had never encountered a manager he could respect. Our reply: Maybe you are just one of those diehards who constitutionally hates people in positions of authority.

Within hours our mailbox was filled with thank-you notes, mainly from managers who had struggled with "boss haters"

and were relieved to hear that the ire directed toward them was more ideological than personal. We also heard from people who identified themselves as "reformed" boss haters, or as one reader said, "I (secretly) criticized management until I was made a manager myself...and I realized most everything they did made sense in context." Still, the bulk of the responses to this column came from readers who basically said: "You must live in a bubble. Most managers are self-serving, incompetent idiots, and your so-called boss haters are the only ones out there with the guts to say so."

We were also accused of living in a fantasy world by the majority of respondents to our column on human resource departments, "So Many CEOs Get This Wrong." Yes, HR has its proponents; some even wrote in to support our assertion that HR should play an active and vital role in building great teams. But most of our mail sounded like the letter from the CEO of a small company in New York who wrote: "Where are these insightful, savvy, talented HR people you refer to? I'd have them at the table, making decisions with the CFO and me—if they existed. The truth is, most HR people are only capable of filling out benefits forms and running picnics. That's why they're marginalized."

But nothing, in terms of volume and intensity, compares with the response we received to our column "What's Right About Wal-Mart." At first, we were stunned to see how many people—about 80%—agreed with us that Wal-Mart does more good for the economy and society than most government institutions. But after a few days passed, the tone changed, and you would have thought we'd called for the canonization of Osama bin Laden. Hostile messages accused us of hating labor, poor people, and small business. As one reader wrote: "Wal-Mart destroys freedom and the American dream. What were you thinking?"

Well, not that! But we were also thinking, isn't this great? Every heartfelt question we've received and every passionate response to our answers has not only helped us crystallize our own views but helped us discover what excited, and incited, people in business in 2006.

Will 2007 bring more of the same or a whole new set of issues? We look forward to finding out—from you. ■

Jack and Suzy Welch look forward to answering your questions about business, company, or career challenges. Please e-mail them at thewelchway@businessweek.com. For their weekly podcast, go to www.businessweek.com/search/podcasting.htm.



AVALON

Serious Technology

Welcome to inner space – also known as Avalon Limited's interior. Where Dynamic Laser Cruise Control¹ automatically adjusts your speed to help keep a preset distance between you and slower traffic ahead.

A voice-activated DVD navigation system² is on board, as are heated and cooled front seats. To explore all of Avalon's luxurious features visit toyota.com

ALL THE BELLS, WHISTLES AND LASERS.

Avalon Limited shown with available equipment. ¹Dynamic Laser Cruise Control is designed to assist the driver and is not a substitute for safe and attentive driving practices. Please see your *Owner's Manual* for important cautions and instructions. Requires Vehicle Stability Control (VSC). ²The navigation system is designed to assist in locating an address or point of interest. Discrepancies may be encountered between the system and your actual location. Road system changes may affect the accuracy of the information provided. Rely on your common sense to decide whether to follow a specified route. Detailed coverage not available in every city or roadway. Periodic updates available at an additional cost. See your *Navigation System Owner's Manual* for further details. ©2007 Toyota Motor Sales, U.S.A., Inc.

 **TOYOTA**
moving forward