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meets perfect execution.
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The McGraw·Hill Companies

BusinessWeek

APRIL 3, 2006

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The Top Performers

THE BUSINESSWEEK FIFTY

50

Plus: An Investor's Guide To The Leading Companies

Wyeth

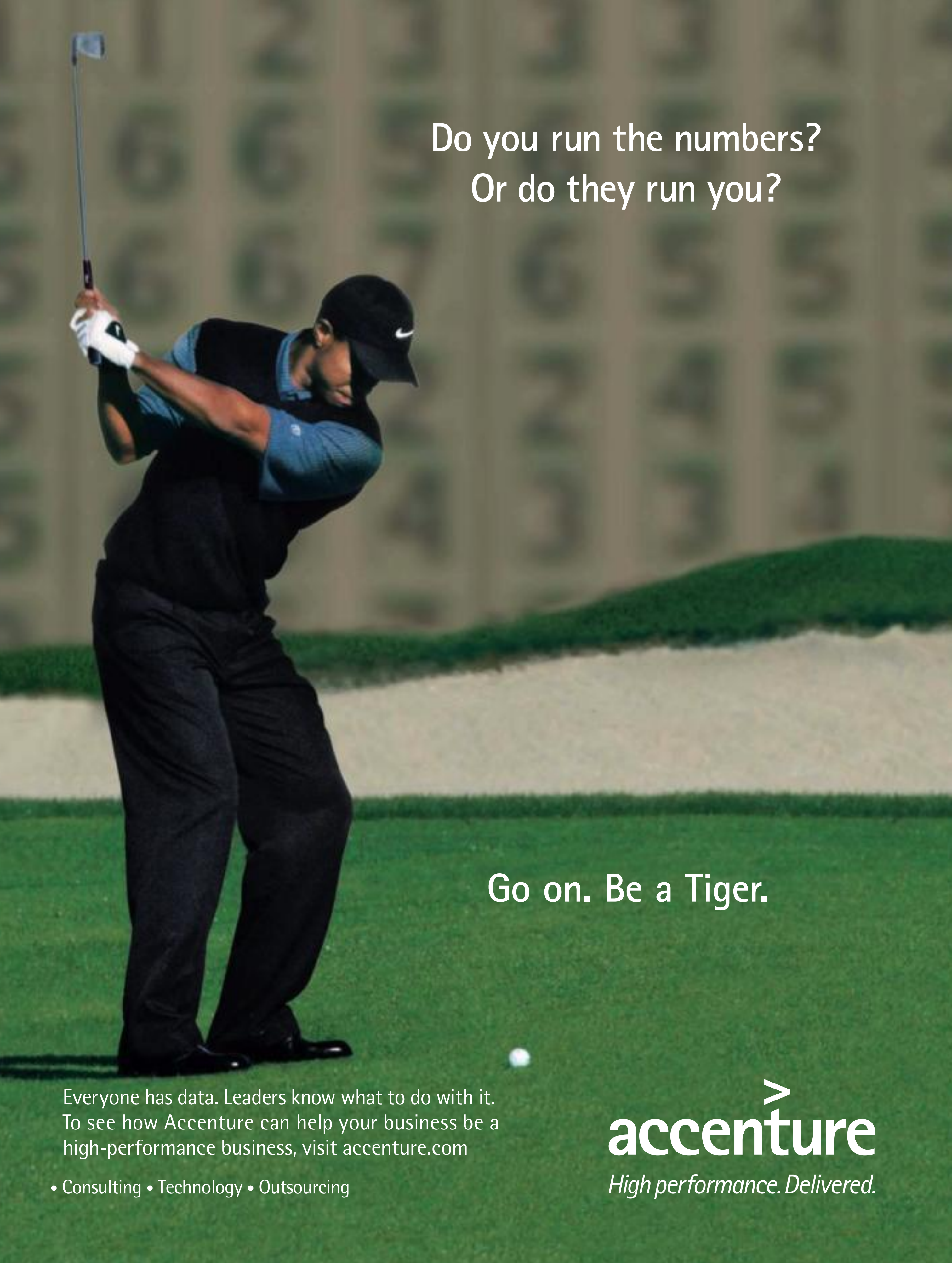
High-performance R&D, delivered.

Determined to boost its output of innovative new medicines, Wyeth's research & development leadership teamed with Accenture to reengineer the way the pharmaceutical company discovers new molecular entities and moves them through preclinical development and clinical trials. The companies designed and implemented vast changes to streamline operations and dramatically improve the effectiveness of Wyeth's proven R&D organization. Now, three years into the initiative, the productivity of Wyeth's drug discovery effort has risen 400 percent, early clinical trial cycle times have been cut by 60 percent, and a new high-performance model for outsourcing clinical data management is substantially reducing costs by about 50 percent.

Dell

High-performance supply chain, delivered.

When the world's number one computer company set out to upgrade its already world-class manufacturing infrastructure several years ago, they began with a bold, yet simple premise: "build more systems with less inventory." In about 100 days, Accenture and Dell conceived and implemented an approach that allows Dell to operate on no more than two hours of inventory at a time. Now in place in Dell's plants around the world, the program paid for itself five times over during the first 12 months of operation. Dell is able to adapt more quickly to rapidly changing technologies and maintain its position as a high-performance business.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BusinessWeek

April 3, 2006

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NICK DOLDING/PHOTODISC RED/GETTY IMAGES

Water Sparkles

Even the cold, fresh H_2O that comes flowing out of mountain springs is a hot commodity these days, according to our **Online Special Report.** That's why coffee giant Starbucks bought Ethos Water, a small purveyor of bottled water previously sold mainly in yoga studios and health food stores. Ethos founders Jonathan Greenblatt and Peter Thum discuss their plans for expansion with Innovation & Design Channel Editor Jessie Scanlon. Of course, even if Ethos is wildly successful, it's just a drop in Starbucks' massive revenue stream, so investors need to find plays that are purer. In **Dipping into Water Stocks,** we identify five companies that offer a chance to profit from collecting, distributing, and purifying the stuff. Perhaps the biggest opportunities lie in cleaning up storm water. Under a mandate from the Environmental Protection Agency, municipalities are spending billions on tunnels, tanks, and drain purifiers. To see just how wise you are about water, take our interactive quiz. You'll find all of this and more at **www.businessweek.com/go/water06**

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UP Front

"This kind of thing will undermine the deterrence idea of white-collar crime prosecution."

–University of Texas law professor Henry T. C. Hu after a federal appeals court reversed Frank Quattrone's obstruction-of-justice conviction, to The Washington Post

EDITED BY DEBORAH STEAD

PLANET GOOGLE

A REALITY CHECK FOR PRINT

GOOGLE'S EFFORT to roll its advertising juggernaut beyond digital is struggling. But that may not be good news for print media. In February, Google auctioned off ad space it had purchased

in about two dozen magazines, from **Martha Stewart Living** to **Road & Track.** The auction, the latest twist in a six-month experiment with buying and reselling print ads, was open to thousands of advertisers. But Google was forced to extend the deadline to lure more buyers.

The tepid demand was apparent in some winning bids. Nicholas Longo, CEO of **CoffeeCup Software,** which makes tools for creating Web sites, bid just $4,600 for each of three half-page ads in *Martha Stewart Living*. The magazine's rate card pegs the price of a half-page ad at more than $59,000. Longo wound up paying at least 93% less than that. Neither Google nor *Martha Stewart Living* would reveal what Google originally paid for the space, but it didn't get a similar discount.

Google can certainly digest a loss of tens of thousands of dollars. A spokesperson says the outfit is more concerned with testing the auction process than with any financial return. But the results may indicate that the true value of a page of print lags its list price, at least in the eyes of Google's advertisers, who are used to high-return search engine campaigns. *–Ben Elgin*

THE BIG PICTURE

SLIPPERS AND STUBBLE

vs. life in the cubicle: 941 telecommuters from 20 countries weighed in on whether they...

	WOMEN	MEN
FEEL MORE PRODUCTIVE	46%	52%
TAKE TIME TO BATHE	44	30
BREAK OFF TO DO HOUSEHOLD TASKS	38	18
FEEL GUILTY ABOUT NOT BEING IN THE OFFICE	11	8

Data: SonicWALL Inc.

(CLOCKWISE FROM TOP RIGHT) © ROB HOWARD/CORBIS; CHRISTOPH HITZ

FLU FEARS

I Know Why the Caged Bird Sings

SELLING ITSELF AS a haven from bird flu, the U.S. poultry industry has a point to make, but it's a tricky one: Its chickens are raised in "contained facilities." Unlike some Asian birds, they don't go outside, where they could have contact with their wild, diseased brethren. As animal rights groups have long complained, the vast majority of the 10 billion chickens produced annually are confined in so-called factory farms.

So how do you market something that conjures images you would rather avoid? Very carefully. John Lea, group vice-president at **Tyson Foods,** makes the practice sound almost benevolent. "Our commercial birds are raised in facilities that protect them from wild birds and predators," he explains, adding that the U.S. poultry industry is "the most protected in the world from accidental transmission." And Richard Lobb of the **National Chicken Council** says that "keeping flocks indoors is the best way" to avoid disease. Whether or not that's true is open to debate. Tyson, for one, is not taking any chances, having increased testing and security measures. Meanwhile, groups such as **People for the Ethical Treatment of Animals** are fuming over the efforts to promote factory farms as a form of biosecurity. *–Diane Brady*

upFront

PAY CHECK

THE WHOLE TRUTH ABOUT OPTIONS

FOR A PREVIEW of how CEO pay may be disclosed in the future, take a look at **Bank of America's** latest annual proxy. The company is one of a few listing "total compensation" for top brass ahead of new **Securities & Exchange Commission** rules expected to kick in next year. (All told, CEO Kenneth Lewis came in at $22 million in 2005.)


LEWIS

For the first time, BofA lists the dollar value of executives' stock options (page 32) as a pay-package element. And it makes quite a difference. When the current proxy looks back to 2004, it lists Lewis' pay in the new way, for a total of $22.7 million. Compare that with his 2004 pay as disclosed the old, piecemeal way in last year's proxy: $19.2 million, close to 20% lower.

The amount of salary, bonus, and restricted stock, the largest parts of Lewis' pay, are the same in both filings. But the new proxy adds in $3.2 million, the estimated value of the 500,000 shares underlying the options Lewis got in 2004. The older proxy just lists the number of options.

There are also changes in "all other compensation" for Lewis in 2004. The number is $359,223 this year, vs. $195,112 last year. The difference, says Bank of America spokesman Terry Francisco, is primarily due to BofA's now putting a dollar value on its CEO's pension accruals. *–Michelle Leder*

CYBER ARENA

IT WAS QUITE a start on the road to the Final Four. CBS' first stab at free Webcasts of the NCAA basketball tournament drew over 4 million viewers in the games' first weekend. That's a million short of the audience for same-day Webcasts of last summer's Live 8 charity concerts on AOL Music, but the 200,000 or so who logged on simultaneously to view the Madness topped the concerts' 175,000 peak audience. At one point before the first game started, 150,000 fans queued up to log on, according to CBS. A spokesman for Marriott International, whose Courtyard chain co-sponsors the Webcasts, said: "We're very pleased." *–Timothy J. Mullaney*

BLOGSPOTTING

LIFE, THE UNIVERSE, AND ALL THAT

http://scienceblogs.com

» WHY READ IT A sister project of *Seed* magazine, this blog aggregator bills itself as the Web's largest conversation about science. Its members include physicists, surgeons, and historians.

» NOTABLE POST "...If life doesn't exist on Enceladus [one of Saturn's moons]...I suggest seeding the moon with Terran organisms that might be able to survive and flourish. In a few decades genetic engineering might also progress to a point where exotic...metabolisms could be synthesized with the physiology of more complex aquatic organisms."

DRAWN & QUARTERED

(CLOCKWISE FROM TOP LEFT) MICHAEL DWYER/POLARIS; ANDY LYONS/GETTY IMAGES; JERRY HOLBERT/BOSTON HERALD/UNITED FEATURE SYNDICATE

upFront

DREAM JEANS

THE PERFECT STORM PANTS?

Always looking for a new twist, the makers of blue jeans may find one in a technology designed to keep denim dry in a downpour. Researchers at Cotton Inc., a textile industry group, have created Storm Denim, a Teflon-like fabric coating that would presumably prevent cold-and-clammy jean syndrome by causing water to bead up and run off. The trade group says that denim treated with the coating still breathes, keeping the wearer comfortable. And the finish—designed for use on fabric that's faded, whiskered, embroidered, or dyed—doesn't change the look or feel of a pair of jeans. The treatment also won't alter manufacturing costs much, the group contends, since the coating comes from readily available chemicals. No indication yet that big players in the $14 billion jeans industry are planning a line of water-resistant jeans.

–Louise Lee

BRAND THIEVES

STEALING LOGOS TO PULL SPAM SCAMS

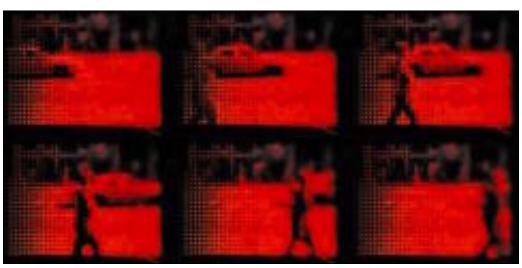
WAL-MART, Home Depot, Starbucks. The names attract millions of shoppers—and those who dwell in the ever-evolving world of computer fraud. Computer security firms are warning about a spate of "brand spam," e-mails promising a "$500 shopping card" at Wal-Mart or a "$500 Home Depot Gift Card." The offers, which use company names and logos without permission, require users to click on a link, type in personal data, and take a survey. Presto! The site says the gift will be mailed.

The offers are, of course, too good to be true. "They are using the brand name to add credibility," says Joel Smith, chief technology officer at **AppRiver,** an e-mail security firm. Smith estimates that of the 500 e-mails per second his firm filters, brand-spam offers account for about 3%. Most have complicated user agreements requiring consumers to take additional steps before getting a gift, such as signing up six others for the promo. It's unlikely, Smith says, that anyone ever receives the gift.

Like phishers trying to steal credit-card numbers, brand spammers are trolling for consumers' e-mail addresses and preferences. The reason? To sell the data to other spammers. Soon after signing up for one of these offers, a user gets spam for obscure lotteries or "free" movie tickets.

Wal-Mart spokesman Martin Heires says the company is warning consumers that it never offers freebies over the Internet. Home Depot says it has worked with law enforcement to shutter sites using its logo. Starbucks says it is aware of the Starbucks "offer," which is "definitely not a Starbucks project."

–Brian Grow



HIGHER ART Jim Campbell's *Fifth Avenue Cutaway #1*

EXHIBITIONISM

WHAT'S THE BEST WAY for little-known artists to boost the value of their work? Exhibit at the Whitney Biennial, where Wall Street collectors are part of the spectacle. Buzz generated by the Biennial, which this year runs through May 28 at New York's Whitney Museum of American Art, helps drive up exhibitors' prices. Here, according to art dealers, are three examples of artists who benefited, along with the highest price paid for their art before a biennial and the best price they got for a piece soon after the opening.

–Reena Jana

ARTIST	BIENNIAL YEAR	PRE-OPENING HIGH	POST-OPENING HIGH
Yuri Masnyj Drawing, sculpture	2006	$6,000	**$18,000**
Jim Campbell Electronic art	2002	12,000	**28,000**
Shahzia Sikander Watercolor paintings	1997	2,400	**5,000**

Data: Metro Pictures Gallery, Hosfelt Gallery

(CLOCKWISE FROM TOP RIGHT) LUBA LUKOVA; COURTESY HOSFELT GALLERY, SAN FRANCISCO; ROBERT NEUBECKER

MANUFACTURING:

Singapore's Best Kept SECRET

Belying its physical size, Singapore sports a global reputation as a compelling hub for business and investment, and a competitive manufacturing location of choice. Manufacturing has helped Singapore grow as a nation over the past 40 years.

Today, manufacturing contributes to a quarter of Singapore's economy and accounts for more than half of its exports. Its share of GDP has been trending upwards over the past 10 years.

Manufacturing Culture

Singapore's strong manufacturing culture evolved over four decades. From a labour-intensive economy, it has built on its manpower skills, infrastructure and technology. Today, manufacturing has moved up the value chain, and is complemented by robust supporting industries and a strong services sector.

Enterprise Ecosystem

In one compact location, Singapore's vibrant enterprise ecosystem provides all the resources for companies to fulfil their entire manufacturing value chain of activities – from research and development, to testbedding, design, production, supply chain management, sales and marketing, and headquarter (HQ) services. The concentration of international enterprises, HQs and startups provide the ideal platform for the meeting of global talents, ideas, funds and businesses.

Supply Chain Management

Singapore's integrated supply chain management ecosystem, which spans information technology, financial and managerial expertise, ensures optimized and cost-effective global deliveries. Its wide network of trade and mutual recognition agreements extend our reach to the world, enhancing the seamless flow of goods, funds and talents.

Emerging Areas

As Singapore continues to further develop its industry clusters, it will actively nurture manufacturing in emerging areas, such as nanotechnology, biotechnology, water technology and new materials. These new growth areas are built on a bedrock of existing strengths in multiple industries, such as electronics, chemicals, biomedical sciences and engineering.

Technology

Today, companies can be highly competitive in manufacturing when it is closely integrated with technology development. The scene in Singapore for technology is set with a stringent intellectual property environment, numerous research institutes and increased investments in research. Singapore is indeed fertile ground for R&D and innovation.

With its winning combination of technology, efficiency and reliability, companies such as Motorola and Hewlett-Packard (HP), recognize that Singapore is a cost-competitive location for manufacturing, and have been expanding their operations here. Motorola currently manufactures 60 per cent of its global 3G phones in Singapore, while HP makes its top-of-the-line servers in Singapore.

Discover Singapore's best kept secret - manufacturing. Visit www.sedb.com/edb/bw or contact any of our U.S. offices to find out why choosing Singapore for your manufacturing needs makes all the right sense.

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Singapore's Global Leadership Positions in Manufacturing Today

Position	Product	Market Share
World		
No. 1	Offshore oil rigs	70%
No. 1	Floating Production Storage Offloading (FPSO) conversion	70%
No. 1	Axial auto insertion machines	60%
No. 1	Ship repair services	20%
No. 3	Wafer foundry	10%
No. 3	Oil refining centre	
Asia		
No. 1	Aerospace maintenance, repair and overhaul	
No. 1	Oil field equipment manufacturing and services	
No. 1	Flavors and fragrances	
No. 1	Lube additives	

ReadersReport

"A permanent tax on gasoline consumption… [could] reduce net money flows to our…enemies."

–David Tolwinski
Newport, R.I.

A GUSHER OF RESPONSES TO A MIDEAST AWASH IN PROFITS

RE "THE NEW Middle East oil bonanza" (Cover Story, Mar. 13): Rather than place a permanent tax on gasoline consumption, which would allow a greater portion of these revenues to remain at home to fund domestic programs, develop alternative energy sources, and reduce net money flows to our geopolitical enemies, America's political and business leadership allow a tax, in effect, to be imposed externally for the benefit of others!

–David Tolwinski
Newport, R.I.

IF JUST 1% OF estimated 2006 gross oil revenues of $380 billion finds its way into radical Islamic schools, mosques, and in support of *jihadi* terrorists, it would be a most unfortunate payback for fueling hydrocarbon-driven Western and developing economies. It would be better for these ruler states to alleviate the poverty of their young people so these economies can be modernized, living standards raised, and women and children freed from suppression and incitement to hate.

–Jerome B. Gordon
Fairfield, Conn.

IN "DON'T UNDERESTIMATE the fear factor" (Cover Story, Mar. 13), Peter Coy cites experts who peg $15 to $30 of oil prices to "fear." Oil prices, over anything other than the very short term (days or weeks), are a function of supply and demand. Since oil is difficult to hoard and because no one drives their car more in anticipation of future supply interruptions, fear has marginal impact on demand. On the other hand, speculative short-term price bumps caused by supply fear are sustained only if supply interruptions materialize. It's the actual supply, not the fear of losing it, that drives oil prices higher.

–Mark Porst
Terrace Park, Ohio

IS IT MY IMAGINATION or is that two-page spread of Dubai completely devoid of people? What does the "real" Dubai look like? Or am I looking at a scale model?

–Vic Wan
Boca Raton, Fla.

Editor's note: It's the real Dubai.

ANTI-AGING MEDICINE: WHAT *BUSINESSWEEK* LEFT OUT

I WOULD LIKE TO clarify some inaccuracies in "Selling the promise of youth"

The McGraw-Hill Companies

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ReadersReport

(Cover Story, Mar. 20). When I introduce the field of anti-aging medicine to patients, I never "pitch" anything or tell them that they will feel younger or live longer. I ask patients what they would like to accomplish, what their concerns are, and provide information on anti-aging and preventive medicine approaches. If patients wish to pursue this route, I plan safe programs for them.

Your article does not reflect a statement I made to *BusinessWeek* that 80% of anti-aging medicine is lifestyle, virtually free of cost, and work that you have to do yourself: nutrition, exercise, and stress reduction, supplemented with vitamins, antioxidants, and neutraceuticals. If hormone replacement is medically indicated to treat a deficiency disease that happens in aging, bio-identical hormones are replaced scientifically and carefully based on diagnostic testing. Bio-identical hormone replacement is the "icing on the cake," not the foundation of anti-aging medicine.

Let me also clarify my statements on growth hormone replacement therapy to treat adult growth hormone deficiency. While you quote me as saying that "growth hormone is no worse than any drug that can be prescribed off-label," I emphatically stated in my interview and in my seminar that this hormone can only be used for an on-label indication.

Your comments regarding medicines produced by compounding pharmacies are also inaccurate. Compounding pharmacies produce medicines derived from Food & Drug Administration-approved drugs.

The goal of anti-aging medicine is simply to keep us as healthy and happy as possible for as long as possible. It is a work in progress.

–Ron Rothenberg, M.D., Founder
California HealthSpan Institute
Encinitas, Calif.

SUPERFUND SKEPTICS SEE OUTSIZE RISKS AND IFFY RETURNS

"WELCOME TO SUPERFUND" (Special Report, Mar. 6) correctly alerted readers to to look at risk. Is some or all of the added return a result of added risk (and how much), and what is the "risk-adjusted" return compared with other investments?

BusinessWeek shows the performance for one of Christian Baha's funds for approximately 12 years. Such a period is often too small to confirm that above-average returns are not due to general luck or to the specific luck of using strategies that happened to work in the given 12 years but that may not work well in other periods.

–Jacob Sacolick
Cornelius, N.C.

CORRECTIONS & CLARIFICATIONS

In "Time off" (Personal Business, Mar. 13), we mistakenly said *American Gothic* would not be part of the Grant Wood exhibition running through July 16 at the Smithsonian American Art Museum. The painting, on loan from the Art Institute of Chicago, will be in Washington through June 11.

"Filtering out the madness before a transfusion" (Developments to Watch, Mar. 6) on mad cow disease should have clarified that Pall Corp.'s device for filtering prions from blood is already available in Europe.

In "The struggle to measure performance" (News: Analysis & Commentary, Jan. 9), a source line in the table "Performance Art" attributing some of the content to Hewitt Associates was inadvertently omitted.

LET'S SEE WHAT we have here, a "new" concept: a virtual mutual fund for small, unsophisticated investors that allows them to play the way the big boys do—in other words, with secretive, risky investments for people who don't understand them and can least afford the higher risks. It seems to me that the reason the Securities & Exchange Commission usually frowns on this is to protect the public, not to keep them from making money.

In your story, Baha says the "superrich are used to going long and short," which is not accurate. The super-sophisticated hedge by going short in addition to long, but most people with extensive assets are mainly concerned with holding on to their money by using simple, safe techniques—like buy and hold.

–Ronald E. Miller
Plaatsdale Investment Advisors Inc.
Branford, Conn.

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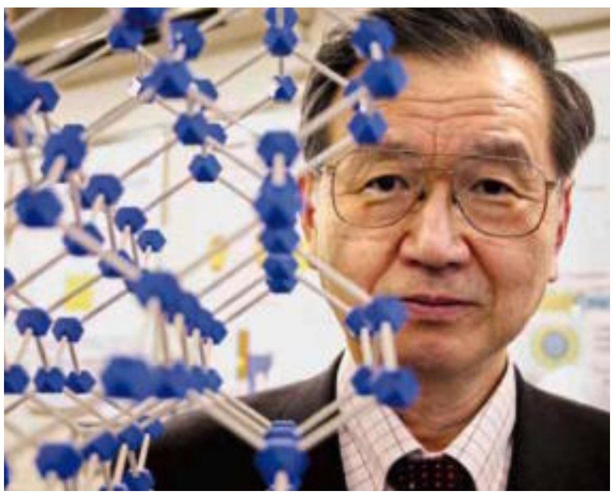
VoicesofInnovation

Thanks for the Memory

FLASH MEMORY CHIPS, which store data in cell phones, digital cameras, and music players, didn't exactly arrive in a flash. They were invented more than two decades ago by Fujio Masuoka, a midlevel factory manager at Toshiba. He was supposed to be working on chips called DRAMs (for dynamic random-access memory), which became the workhorses of the personal-computer revolution. But such semiconductors retain data only when the computer is switched on. That wasn't good enough for Masuoka. His heart was set on memory chips that would preserve the user's data whether the power was on or off, thus eliminating the need for fragile hard-disk drives.



TORIN BOYD/POLARIS

Few engineers had faith in Masuoka's ideas at the time. But the intervening years have provided sweet vindication to the circuit designer, who is now 62 and a professor at Tohoku University in the northern Japanese city of Sendai. Global demand for flash memory is poised to hit $25 billion this year, according to research from CLSA Asia-Pacific Markets, thanks mostly to fast-proliferating handheld gadgets. And on Mar. 21, Samsung Electronics unveiled the world's first 32-gigabyte drive built entirely of flash. This drive should lead to a new breed of futuristic—albeit expensive—notebooks. They'll be shock-resistant; they should boot up in seconds rather than minutes; and they could stay powered-up 50% longer than other notebook PCs between battery charges.

The flash chips Masuoka developed now store data for all sorts of electronics

Nobody anticipated such a development in the early 1980s, when Masuoka began bucking conventional wisdom on data storage. "Simply put, I wanted to make a chip that could one day replace all other memory technologies on the market," he explains. To pull it off, Masuoka drew four other engineers into an ad hoc team and came up with a blueprint. In 1981 he filed a patent for EEPROM—short for electrically erasable, programmable read-only memory. One of Masuoka's colleagues simplified that to flash memory, because the transistors' ability to erase data in a split second reminded him of a camera flash.

Despite Samsung's recent announcement, many industry experts continue to question the long-term implications of Masuoka's invention. "If you're talking about servers or desktop PCs, flash memory will never replace hard-disk drives," says Nam Hyung Kim, an analyst at market research firm iSuppli. "Hard drives are 100 times cheaper."

Price, however, depends on volume, and production of flash memory is poised for an historic growth spurt. Intel, the world's biggest chipmaker and an early proponent of one type of flash, has inked a $2.4 billion joint venture with Micron Technology to produce such chips for consumer products and for PCs.

Toshiba, meanwhile, ranks as the world's second-largest flash memory maker, after Samsung. Masuoka says he is glad the company is profiting from his brainchild, but their relations have been strained for many years. In the '80s, Toshiba was slow to realize that it was sitting on a breakthrough, Masuoka says. The truth didn't sink in until Masuoka made a presentation at an international chip conference in San Jose, Calif., in 1984. Four years later, Intel came up with a competing version that was easier to manufacture.

Intel's move finally galvanized Toshiba, and Masuoka was promoted to head one of its advanced research labs. But his bluntness made him enemies in a culture where compromise and consensus are prized. Masuoka left Toshiba in 1994, after a run-in with his boss got him transferred to a position without staff or funds. In 2004 he sued the company for what he considered his rightful cut of its profits on flash: about $9 million. The case is pending in a Tokyo court.

Masuoka now predicts that current versions of flash may reach their technological limits in a few years. But he's convinced that some type of low-cost, 3D chip will eventually chase disk-drive makers out of business. There will always be another barrier, he concedes, but "someone will come up with a breakthrough technology to get around it." ■

–By Kenji Hall

BusinessWeek online Fujio Masuoka discusses the early days of flash memory in a Q&A at www.businessweek.com/extras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Technology&You

BY STEPHEN H. WILDSTROM

Total Wi-Fi Freedom

Now that nearly every new laptop comes equipped with Wi-Fi, it seems you should be able to plunk your computer down just about anywhere, log on to a wireless network, and get to work. Alas, it's not that simple, because Wi-Fi is neither ubiquitous nor always cheap. That's why new PCs that use both very fast cell-phone networks and Wi-Fi are attractive.

These wireless services provide a broadband-like experience, with download speeds consistently topping 500 megabits per second. There are three competing offerings: Verizon Wireless BroadbandAccess, Sprint Mobile Broadband, and Cingular BroadBand Connect. A couple of years ago PC makers started providing access to such services with add-on cards. Now they're building the access right into the laptop, which is much more convenient for the user.

I tried Verizon's service on a Lenovo ThinkPad T60 and Cingular's service on Dell's forthcoming Latitude D620, both corporate workhorse notebooks. With these cell-based systems, the laptop is tied to a carrier. All manufacturers are planning to offer versions for different carriers, in the U.S. and elsewhere, but changing carriers may require that a technician yank out one radio and install another. Even if that's unnecessary, to get a decent rate you have to lock yourself into a two-year contract.

While Cingular uses a different technology than Verizon and Sprint, I found all the services comparable. But there are differences in coverage. Verizon's high-speed network is the oldest, and it's available in most major metropolitan areas. Sprint's is spottier, and Cingular is in just 16 metro areas. In each case there's backup service at dial-up speeds if the fast network is not available, but it's a painful step down.

FOR NOW, AT LEAST, VERIZON is probably the best choice in the U.S. It offers unlimited data service for $60 a month on a two-year contract, provided you also have a Verizon phone with a voice plan. If you don't have a laptop with built-in wireless, they'll sell you a PC Card radio for just $50. Sprint offers a similar deal with a free card—which you'll need since no laptops are currently sold with built-in Sprint service.

Cingular may be the best deal for the globally mobile. Unlimited U.S. service costs $80 a month (now available for $60 as a "limited time" offer) for customers with a Cingular voice plan. Its technology is compatible with the high-speed networks being rolled out in Europe and Asia. Cingular offers a $139-a-month plan that provides unlimited data in the U.S. plus 100 megabytes in monthly downloads in more than a dozen countries. If that sounds expensive, you probably have never gotten a bill for international data roaming. Cingular also offers access to several thousand Wi-Fi hotspots for an additional $20 a month.

Cell-based services for PCs connect with a click and work in moving trains

That last deal highlights the fact that phone-based wireless services should be seen as a complement to Wi-Fi rather than an alternative. Unlike Wi-Fi, these services can be used throughout the coverage area, not just in hotspots. You can connect simply by clicking, as opposed to registering separately for each hotspot. And the service works in moving trains and cars (not while you're driving, please). On the other hand, regular Wi-Fi is generally faster, especially for data uploads, such as posting your vacation pictures to a Web site. And Wi-Fi often performs better than cellular inside buildings.

Laptop makers should be doing a better job of getting Wi-Fi and cell-based wireless to work together. Lenovo at least lets you manage both using its Access Connections software, but you still have to change profiles to switch. Ideally your computer would simply connect you to the best available network without any intervention.

For people who connect away from home or the office only occasionally, these cell-based services are probably not worth the extra cash. But for a road warrior the ability to connect anywhere, anytime, will more than justify the cost.

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(TOP) PHOTOGRAPH BY ETHAN HILL; ILLUSTRATION BY MICHAEL WITTE

MediaCentric BY JON FINE

Media, Marketing, and Advertising in the 21st Century

Designs on the Disaffected

Procrastination 2.0: The business model. Don't laugh. It's driving Time Inc.'s newest and strangest launch, the Web site Office Pirates, a big-league play for a kind of disaffected young man who's glued to his office computer. ¶ This guy is a pop-culture freak who gravitates toward "crashes, explosions, girls, craziness, obscenity, blah blah blah," says Simon Assaad, CEO of heavy.com. (Heavy.com, which features short videos ranging from scabrous cartoons to swimsuit fashion shoots, has a channel entitled Crashes and Explosions.) He spends hours trolling sites like Viacom's iFilm.com, which lets users post and view video clips. When he finds something there he likes—say, *Star Trek*'s William Shatner murdering Elton John's *Rocket Man*—he sends a link to his friends.

SO RADICAL, SORT OF Can Office Pirates' videos (below) make a splash like the goofball rap video *Lazy Sunday* (left)?

Guys like him made Andy Samberg a star. Samberg became a new "featured player" on *Saturday Night Live* this season, which roughly translates as "glorified benchwarmer." Then he co-conceived and co-starred in a short, spectacularly entertaining rap video, *Lazy Sunday*. Within hours of airing last Dec. 17, it hit sites like iFilm and youtube.com and became an immediate "viral video" hit. Within weeks the video had been played more than 5 million times on youtube alone, and Samberg appeared on David Letterman and Conan O'Brien.

VIRAL VIDEOS ONCE were, you know, videos—blips of bizarreness copied and traded on VHS tapes. The Web destroyed this distribution bottleneck. That destruction enabled Samberg's fame, and it's why Time Inc. launched Office Pirates. Office Pirates is atypical for Time—launched quietly, promoted sparingly. It has but five full-time staffers. It hit the Web on Feb. 22 with exactly two advertisers, Bacardi and Dodge Caliber. No more have signed on since. It is very off-brand for the world's largest magazine publisher, which has never before targeted the ever-feel-like-killing-your-boss crowd. One short video shows a customer-service rep seated in front of a thought-bubble graffito pleading "Kill me," and another features a postcollegiate type itching to shoot his clueless boss. There are mock motivational posters and links to weird Web sites, and users can submit their own content.

It's deeply perverse (in the good way) and looks good on paper by fusing favored Web modes of the moment: communities, user-created content, and eagerly shared short-form video. The idea is that elusive young men will flock to the site and turbocharge it via their own programming and word of mouth. Low-cost means quick profit, or a fast exit. And some big-name advertisers, sweating over disintegrating ad models, are receptive to such nascent media formats. Young men "feed like sharks" on ribald, short-form online content, says Dodge marketing executive Mark Spencer. "We are there because they are there."

It's admirable for Time Inc. to try something this bizarre, so it's a drag that Office Pirates seems very version-1.0. The programming is wildly inconsistent. What's perverse for Time Inc. is not perverse for the Web, and so it lies between freer-form sharing sites like youtube and gnarlier programming plays such as heavy.com (which is also readying a community platform). Office Pirates plasters its offerings with its name and logo. But for such content to work, "it's got to be organic and be emanating from something that doesn't appear to be overly commercialized," warns Laura Desmond, CEO of media buying firm MediaVest USA.

Lazy Sunday took off organically. But when Samberg made another SNL video in March, starring Natalie Portman as a foul-mouthed gangsta rapper, it made a much smaller cultural splash. Office Pirates' "plan does not bank on the idea of becoming a serial creator of these outrageously serendipitous viral events," counters Time Inc. Interactive President Ned Desmond. Fair enough. But there's one thing about programming for procrastinators: If they don't see what they want on Office Pirates, they have all the time in the world to find it elsewhere. ■

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

(TOP) PHOTOGRAPH ETHAN HILL

BY JAMES C. COOPER

This Porridge Still Looks A Little Too Warm

Strong demand at home and abroad is heating things up at U.S. factories

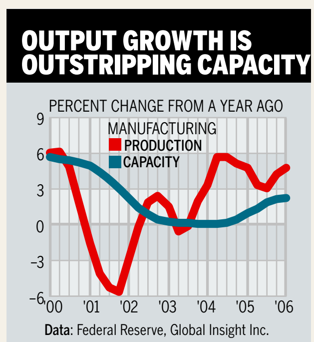
U.S. ECONOMY Goldilocks lives. The economic scenario, that is. Those who believe in her think the economy this year will be not too hot, not too cold, but just right. Currently, it's the view most widely held by economists, investors, and Wall Street pros. So, the tale goes, after the unusually warm winter heated up the economy in the first quarter, growth will cool down to a pace of about 3% that will relieve any remaining worries about future inflation and interest rate hikes by the Federal Reserve. If so, stock prices will most likely extend this year's rally, and bonds may benefit as well.

But will it really be that simple? Much will depend on market perceptions of how the economy is shaping up in the second quarter. And on that front, the recent pace of improvement in the manufacturing sector will be a key development to watch. Some regional survey results for factory activity in March have looked surprisingly upbeat, suggesting that manufacturing is ending the first quarter with a good bit of momentum. That could be an important sign. The industrial sector began gathering steam late last year, and historically when manufacturing has oomph, so does the overall economy.

The factory sector's thrust also reflects a key pattern that is driving economic growth this year. That is, the greater roles played by capital spending and exports, which are two important engines of factory activity. Through January, inflation-adjusted exports of goods are up 12% from a year ago, and exports of capital goods are up 16%. Through February, production of business equipment has grown 10%, with output in the high-tech sector up nearly 22%. Those growth rates are sharp accelerations from this time last year.

Robust factory activity also may be a sign that overall demand is not cooling. If so, the ability of manufacturers to keep up will continue to be stretched. Output is already outstripping the growth of new production capacity (chart). That's pushing up operating rates and giving companies more leeway to lift prices, a pattern the Fed is keeping a keen eye on. The dollar's surprising strength last year helped keep the prices of goods down, but that may not be the case in the coming year (page 28).

WITH THE WEATHER ALSO RUNNING hot and cold in the first quarter, making sense of the economic numbers has been more than the usual challenge. According to the Fed's latest report on industrial production, manufacturing output jumped 0.8% during balmy January, but it managed only a scant 0.1% advance in February as normal temperatures returned. The true strength is probably somewhere in the middle. Monthly gains averaged a sturdy 0.6% during the past six months. Anecdotal reports of factory activity are unambiguously upbeat. The Federal Reserve's latest roundup of economic conditions in all 12 Fed districts, prepared in advance of the Fed's Mar. 28 policy meeting, showed that manufacturing activity in almost all districts continued to expand during January and February. And in most districts, Fed banks reported that the strong demand was widespread across industries, especially in construction materials, electrical equipment, heavy machinery, defense products, tractor trailers, and heavy trucks. The concentration of strength in those industries clearly illustrates how demand for capital goods is driving factory production. [For a view on why manufacturing job growth remains weak, see page 136.]



THAT HEALTHY TREND appears to have continued in March, based on upbeat readings from separate surveys of industrial activity taken by both the New York Federal Reserve Bank and the Philadelphia Fed. Both canvasses showed particularly impressive readings for new orders.

Many businesses are running to catch up with demand, a key reason to expect that manufacturing will keep humming along in the coming months. For example, the ratio of business inventories to sales, a measure of the adequacy of current stock levels, fell sharply in December and January. Even accounting for the downtrend in this ratio in recent years, caused by generally lower holdings of inventories by businesses and the faster rates at which stocks turn over, inventories relative to sales are still well below the typical levels seen since the recession ended four years ago.

Much of the demand flowing to manufacturers is for business equipment, and it's coming from both home and

CHARTS BY ERIC HOFFMANN/BW

abroad, as growth overseas begins to show more pizzazz. Based on high readings for corporate optimism and plenty of cash to invest, U.S. businesses are set to boost their capital spending in 2006 even faster than last year's 8.7% increase. Numbers on orders and shipments in recent months suggest that outlays for new equipment got off to a booming start in the first quarter.

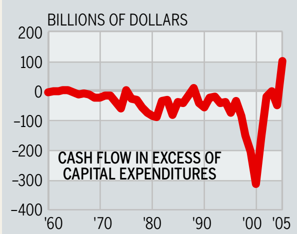
The most striking evidence of U.S. corporate health shows up in recent data on business-sector balance sheets. Through the fourth quarter of last year, the internal funds available to nonfinancial corporations for investment had exceeded the level of capital expenditures for three quarters in a row. Companies have never before shown that degree of financial flexibility (chart).

ALTHOUGH COMPANIES have been hesitant to expand after the investment bust five years ago, two things are happening right now that are affecting both manufacturing and the economy. One, businesses are rushing to expand their operations in the face of strong demand and insufficient production capacity. And two, because factory output is growing more than twice as fast as new capacity is being added, manufacturing operating rates have risen sharply during the past year.

Through February, factory output in the first quarter was up 4.8% from last year, while capacity grew only 2.3%. Consider that five years ago manufacturers were increasing their capacity at more than twice that rate. In February, factories were using 80.1% of their capacity, a level high enough to suggest that some manufacturers are starting to strain to meet demand. Seven industries in February, representing 18% of factory output, were operating in excess of 85% of capacity.

Ultimately, it will be up to the Fed to decide if the economy is cooling down enough to stop raising interest rates. Right now, though, the Fed appears to be as much in the dark as anyone about how the economy is shaping up. On Mar. 20, Fed Chairman Ben S. Bernanke gave Wall Streeters in New York an impressive analysis of why long-term interest rates were unusually low, given the Fed's series of short-term rates hikes. His conclusion: He didn't know why. He said they might be too stimulative, requiring further hikes in short rates, or they might be justified by global conditions, perhaps requiring lower short rates. It was an exercise in being noncommittal worthy of Alan Greenspan.

COMPANIES HAVE GREAT FINANCIAL FLEXIBILITY



Data: Federal Reserve

The only way to know for sure, he said, is to watch the economy and the data. Of course, investors and economists already knew that. In the coming months, they will be checking the temperature of the porridge just as intently as the Fed. But based on the heat coming from manufacturing, it still looks a little on the warm side.

INFLATION

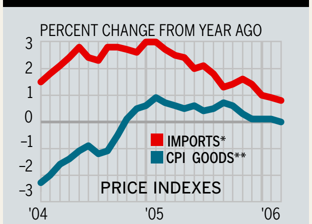
The Greenback's Gain Isn't Likely to Last

FEBRUARY CONSUMER and producer price data paint a seemingly benign outlook for price pressures. One key ingredient in the recent easing in inflation was the surprising uptick in the U.S. dollar last year. But the underpinnings for the stronger dollar are set to fade.

During 2005, the U.S. dollar defied economists' expectations and rallied. The Federal Reserve's trade-weighted index of major currencies rose 8.4% in 2005 with most of the gain coming in the first half of the year. The gains were even larger vs. the yen and euro, with 14.8% and 8.7% jumps, respectively.

The upshot is that "the rise in the dollar against these currencies appears to be translating directly into softer import prices from these regions," says Barclays Capital chief U.S. economist Dean Maki. The yearly overall pace of nonfuel import prices has eased to 0.8%, from 2.7% last February. The slowdown has been even bigger for all goods from the European Union, receding to a pace of 2.9%, from 6.3% last February. Prices of Japanese imports fell 0.9% in the past year.

HOW IMPORTS HAVE RESTRAINED INFLATION



*EXCLUDING FUEL
**LESS FOOD AND ENERGY GOODS
Data: Bureau of Labor Statistics, Global Insight Inc.

During the same period, consumer goods prices excluding food and energy were flat. That has helped pull down overall core inflation in the face of accelerating service-sector prices, which are now up 2.9%.

However, the relief from last year's higher greenback is unlikely to last. The Federal Reserve has lifted its fed funds rate 350 basis points since June, 2004. The Fed hikes pushed U.S. short-term rates past those in the euro zone and widened the gap against Japan's rates of near 0%. The result was an influx of foreign money, which helped push up the dollar.

Many economists expect the Fed to take a break by midyear. At the same time, the European Central Bank is sounding more hawkish, and the Bank of Japan is ending its ultra-accommodative experiment of quantitative easing.

What's more, global economic activity is expected to accelerate this year even as the U.S. economy settles into a more modest rate of growth. As a result, demand for the U.S. dollar should begin to wane, eliminating the inflation-dampening effects of lower import prices.

–By James Mehring in New York

The Business Week

News you need to know

EDITED BY HARRY MAURER

GM in the Garage March may not have been the cruelest month for General Motors, but it's up there. The dented auto maker (Detroit headquarters, photo) on Mar. 16 restated 2005 earnings to the tune of $2 billion in red ink, which means it lost $10.7 billion. About $1.6 billion of that has to do with costs to bail out its former parts unit, **Delphi,** and give buyouts to some of its own workers. The rest stems from rejiggered earnings at its finance arm, **GMAC.** Couple the gargantuan loss with aggressive noises coming from new board member **Jerome York,** and it's clear that **CEO Richard Wagoner's** driver's seat is mighty hot.

At least Wagoner has a pact with the **United Auto Workers** to help retool. GM said on Mar. 22 that it has agreed to a deal that will retire as many as 30,000 of its workers and more than 10,000 at Delphi. That could speed up plans to shutter or cut production at a dozen plants.

See "A Gleam of Hope for GM," www.businessweek.com/go/tbw

Bernanke-Speak "On the one hand, on the other" is the economist's stock-in-trade, as **Harry Truman** noted when he demanded a "one-handed economist." **Fed Chairman Ben Bernanke** didn't disappoint the two-handed gang in a Mar. 20 speech. Addressing puzzlingly low long-term U.S. interest rates, Bernanke came to no conclusion on whether the Fed needs to tighten or loosen in response. But he did explain the low rates as the gift of a global savings glut.

See "What you foresee is what you get," page 40

Red Faces in Redmond This is starting to resemble *Waiting for Godot.* **Microsoft** on Mar. 21 revealed that the release of its much-delayed new operating system, **Windows Vista,** would be bumped back yet again, from November until January, for the consumer version. The move ultimately may not hurt sales much, but it sure makes the Redmond (Wash.) giant look clumsy.

See "Microsoft's slo-mo scramble," page 36, and "Microsoft's receding vista," www.businessweek.com/go/tbw

So Long, Sandy **Citigroup** made it official on Mar. 21: **CEO Charles Prince** will add the post of chairman at the annual meeting on Apr. 18 as billionaire dealmeister **Sanford Weill** steps down. Weill was chairman at Citi and predecessor companies for nearly 20 years. Under Weill, Citi and its predecessor ranked No. 1 in total shareholder return in the Dow 30 for the 10- and 15-year periods ended Dec. 31, 2005. Over to you, Chuck.

See "For Citi, 'No more excuses,'" page 134

Searching for Money **Google** built its fortune by sending surfers elsewhere. But these days it's trying to keep folks glued to its sites, giving it more chances to sell ads. On Mar. 21 it unveiled Google Finance, a searchable site packed with news, charts, company profiles, and stock quotes. That moves Google into a dog-eat-dog arena, with everyone from **Yahoo!** to **Microsoft's MSN** to **Dow Jones's MarketWatch** drawing tens of millions of users. The search king hopes to win with gee-whiz features such as historic stock charts that can be dragged with a click of a mouse.

See "Google shows surfers the money," www.businessweek.com/go/tbw

Quattrone Beats the Rap Criminality is a state of mind. That's the message from a federal appeals court, which on Mar. 20 tossed out the obstruction of justice conviction of **Frank Quattrone,** a once high-flying investment banker. Prosecutors charged Quattrone for telling colleagues in an e-mail to "clean up" files at a time when the **Justice Dept.** was investigating his firm, then known as **Credit Suisse First Boston.** The appeals panel said the judge's instructions wrongly allowed jurors to convict Quattrone even if he didn't know his e-mail would affect the probe. No knowledge, no crime, the court said. Prosecutors are pondering whether to retry the case.

The Justices Plug a Loophole When was the last time a company racked up a win in a shareholder lawsuit? On Mar. 21, when a unanimous **Supreme Court** banished investor class actions from state courts. *Merrill Lynch v. Dabit* centered on a 1998 reform that sought to rein in shareholder suits by pushing claims related to "the purchase or sale" of stock into federal court. In 2002 a broker sued **Merrill** in Oklahoma, claiming that the firm misled him and others into holding on to overvalued shares. Because there was no buying or selling, the broker said, the case could be heard in a state court. The high court skewered that notion. Big losers in the case: savvy lawyers seeking to have claims heard by sympathetic state judges.

PATRICK ANDRADE/POLARIS

Japan's New Mobile Player In one fell swoop, Internet tycoon **Masayoshi Son** became a cell-phone heavyweight. Son's **Softbank** on Mar. 17 ponied up $15.5 billion to buy **Vodafone's** Japanese mobile unit. The deal, one of the largest ever in Japan, gives Softbank 15.1 million customers and a nationwide cellular network to add to its portfolio of Net, broadband, and fixed-line services. It also relieves Vodafone executives of the headache of fixing a business with shrinking profits.

See "Softbank-Vodafone deal rings true,"
www.businessweek.com/go/tbw

Insurers on the Prowl Merger mania is shaking up the sleepy world of insurance. Deal-hungry **Aviva,** Britain's largest life insurer, on Mar. 16 aimed a nearly $30 billion bid at crosstown British outfit **Prudential PLC,** which shrugged it off. The next day, *The Wall Street Journal* reported that **St. Paul Travelers,** of St. Paul, Minn., is talking with **Zurich Financial Services** of Switzerland about teaming up. (St. Paul denied it.) Meanwhile, **MetLife** is sniffing around the world for deals. Such combos could give **AIG,** a U.S. giant with major overseas operations, more muscular rivals to fret about.

A New Move for Dell For the first time ever, **Dell** is buying another PC maker—and moving upscale in the process. On Mar. 22 the maker of plain-Jane computers said it plans to acquire Miami-based **Alienware,** a privately held purveyor of high-end machines favored by gameheads and other affluent types. Terms weren't disclosed. Dell is searching for ways to revive sales growth, projecting it will reach 6% to 9% this quarter, far below the 16% posted only a year ago. Alienware boxes average $3,200, far more than Dell's.

Exit of the Week

It's the **GE** of sports leagues, but its **Jack Welch** is about to leave the game. On Mar. 20, **Paul Tagliabue** said he would step down in July after quarterbacking the **NFL** for the past 16 years and turning it into a money machine that's the envy of every sports operation. So who'll fill his cleats? Tagliabue's longtime No. 2 is **Roger Goodell,** and the job is essentially his to lose, say sports industry sources. The 47-year-old Goodell, son of former **Senator Charles Goodell** (D-N.Y.), has spent nearly his entire career at the NFL, playing major roles in negotiating TV and labor deals. Also on the depth chart is **Rich McKay,** 47, president of the **Atlanta Falcons** and son of legendary **University of Southern California** and **Tampa Bay Bucs Coach John McKay,** who serves on the league's powerful competition committee. A longer shot is **Eric Grubman,** 48, ex-**Goldman Sachs** banker who for two years has headed up finance and strategic transactions at the NFL. And two Hail Mary contenders: **Bill Clinton** and **Condi Rice.**

PAUL TAGLIABUE

RICK WILKING/REUTERS

COMPENSATION

THE BOTTOM LINE ON OPTIONS

Who are the winners in the battle over expensing? Just look in the corner office

BY MARK GIMEIN

MORE THAN ONE WAR has been fought over the fine points of religious dogma, and the narrowest differences in ideology have caused some of the bloodiest conflicts. These are the wars that sweep away everything in their path while the participants forget the reason they started fighting in the first place.

So it is—minus the blood—with the Great Options Battle. You will recall how it started, with Warren Buffett leading the charge on one side, Intel Corp.'s Andy Grove and Cisco Systems Inc.'s John Chambers waving their pennants on the other, all battling over accounting rules. Lifted on a tide of anger over ever-more-outsize executive pay packages, the corporate-governance party prevailed. Now the new rules that require U.S. companies to count stock options as an expense are in effect for nearly everyone. But it turns out CEOs might well lose little or nothing. If anyone is taking a hit, it is the professionals, engineers, and managers who hoped they too could cash in on the options boom.

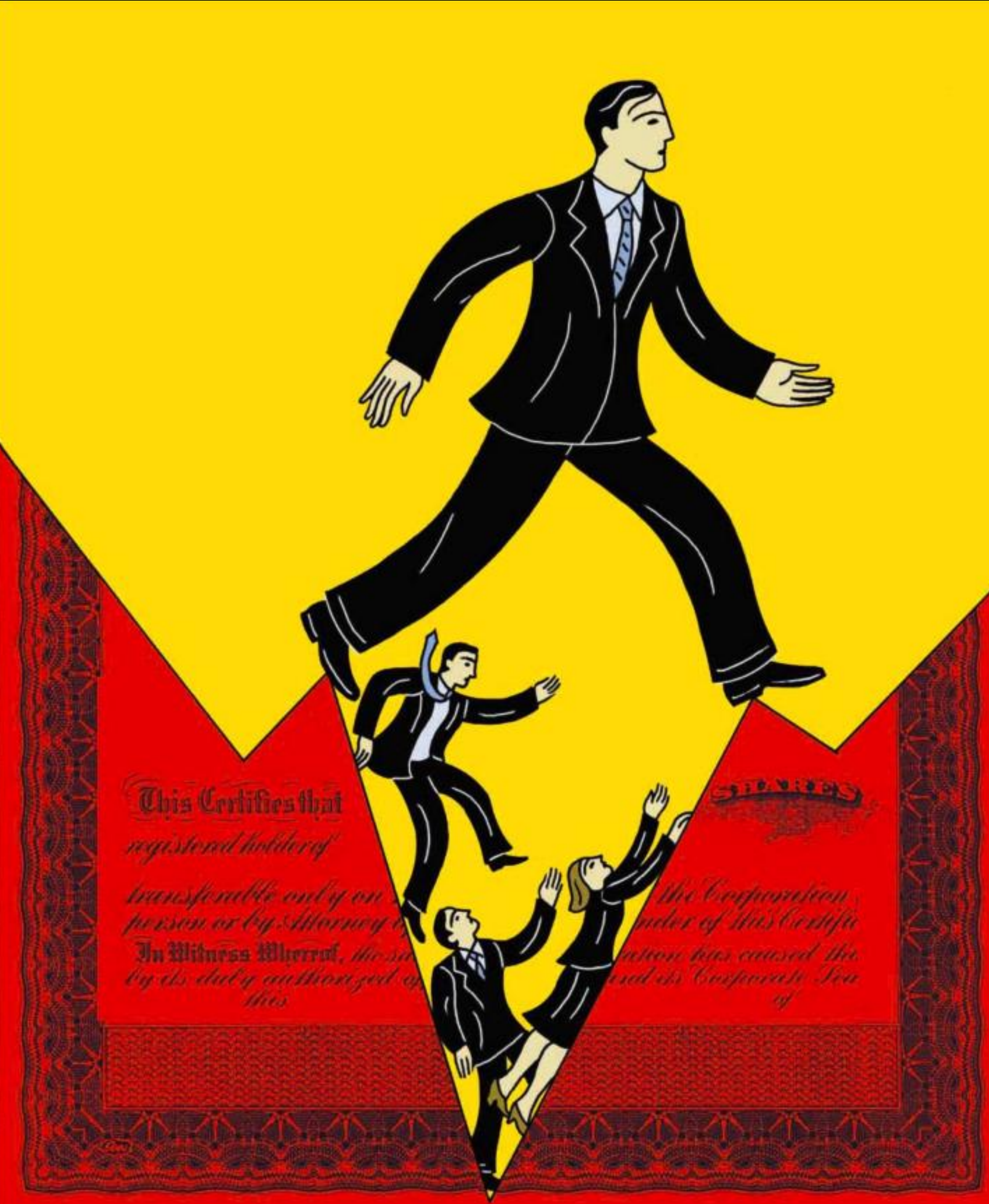
Stock options became popular in the 1990s as a tool that was supposed to "align the interests" of shareholders and management—in other words, reward CEOs for concentrating on raising their stock price. Silicon Valley, of course, seized on options as a way of attracting top engineering talent. Finally, at the height of the market boom, big companies that wanted to project an image of rapid growth and general with-it-ness started giving out options to thousands of their employees. Aetna, when it shed most of its old insurance businesses, instituted an option plan for all employees. So did Time Warner when it merged with America Online. The total number of U.S. employees who got stock options grew to roughly 10 million at the height of the options boom in 2002, according to a study by the National Center for Employee Ownership (NCEO), a think tank in Oakland, Calif.

Now the center's director, Corey Rosen, estimates the number is down to 7 million and shrinking. Before the new accounting rules kicked in, options were invisible on the corporate income statement. No matter how many a company handed out, they could tell investors that they cost nothing. Not anymore. Google, hugely generous with employee options through last year, when almost $420 million worth were handed out, this year has switched to giving out restricted stock, which vests over time. But Google's expansive stock program is the exception. Aetna, whose employees profited handsomely as its shares ran up in the five years or so that it gave options, last year replaced them for non-managers with $500 bonus checks.

"OUTLANDISH PAY"

FOR TOP EXECS who no longer get big option grants, the make-good money is far more handsome. Merrill Lynch & Co. last gave CEO E. Stanley O'Neal options in 2003. Over the past two years, it replaced his cash and options package with

ANTHONY RUSSO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BRING 'EM ON Ellison's grants rose last year

BRADLEY C. BOWER/BLOOMBERG NEWS

The Options Squeeze

As companies have moved toward reporting stock options as an expense, many cut back on the popular perk. But a few CEOs saw an increase in grants last year.

COMPANY	2005 COMPANYWIDE SHARES GRANTED (% DECREASE VS. 2004)	CEO'S TOTAL SHARES GRANTED (% INCREASE VS. 2004)
FEDEX	**2.6** million (–31%)	Frederick Smith 325,000 (+30%)
ORACLE	**42.7** million (–0.3%)	Larry Ellison 2.5 million (+177%)
SPRINT-NEXTEL	**7.1** million (–8%)	Gary Forsee 885,000 (+13.5%)

Figures for companywide option grants are calculated using data on CEO option grants disclosed in company proxies
Data: Securities and Exchange Commission filings for 2004 and 2005.

restricted stock grants of—take a deep breath and feel free to whistle—$51 million. A spokesman says O'Neal's compensation reflects the company's performance. Merrill Lynch is an extreme. But just as most big companies have cut options in some way, it's hard to find a CEO whose options weren't or won't be replaced by some other compensation.

Again, look at Aetna. It cut its broad-based option plan in 2004, anticipating the new rules, but continued giving options to top executives through last year. Starting this year, executives, including CEO John W. Rowe, will no longer get options—but they will get substantial grants of restricted stock. And in a few cases the cutting back on options simply stops at the CEO's desk. FedEx's Fred Smith, for example, went from 250,000 options in 2004 to 325,000 options last year, even as the option pool for the whole company was cut by more than 30%. The impetus for the war on options, pay expert Rosen dryly notes, was "outlandish pay packages, but the pay packages are still outlandish."

It's not all gloom for the middle tier. Some in the tech industry predicted that the new expense regime would be the end of Silicon Valley's famous options culture. Not so. Network-hardware maker Cisco, in fact, continues to hand out options at roughly the rate it did before the new changes took effect. Pfizer, an old-line drugmaker whose options plan for managers turned out to be a less than terrific deal, with its stock languishing since the mid-'90s, has cut option grants by 42% companywide. But it replaced the options with shares of restricted stock.

The brand-new startups, meanwhile, have been affected a lot less by options expensing rules than by a host of other regulatory burdens. New companies, whose options are a big gamble, continue to hand them out to lure programmers. The problems created by the requirement to estimate the value of their shares, which are not yet public, are manageable. "If [complying with] Sarbanes-Oxley was 9 on a scale of 10," says Paul Matteucci, a partner at venture-capital firm USVP, the new option accounting rules are a "3." In fact, Matteucci says that new and little-noticed rules about valuing privately held stock are a much bigger headache for venture backed startups.

There's a pattern here. Tech companies that are asking top talent to take a big gamble and hope for outsize stock bonanzas are keeping their options, other companies aren't. For many employees of big companies, once the bright euphoria of the market bubble was gone, options turned out to be less terrific than

ACCOUNTING REFORM

Earnings: It's Still Apples and Oranges

After battling for more than 12 years, the Financial Accounting Standards Board has finally come to the moment of victory in its drive to see companies record expenses for stock options paid to employees. Over the next several weeks, most companies will start factoring options expenses into their quarterly earnings results.

But investors won't suddenly get clear visions of company profitability. Resistance among technology executives and the tech stock analysts who go along with them means the phase-in is far from complete. In fact, if anything, investors comparing corporate bottom lines this year will still be looking at apples and oranges, often without realizing it. The reason: A significant minority of companies and analysts still use earnings numbers that exclude or minimize options expense.

Companies have been phasing in the rule since June. The added expense will probably reduce earnings in the aggregate by about 3% for companies in the Standard & Poor's 500-stock index, accounting analyst David Zion of Credit Suisse Group estimated late last year using 2004 data, the most recent available. But the impact could be less than that because many companies in 2005 cut back on options grants or changed terms and estimates of their value to reduce the amount they'll have to report.

The clarity the change is supposed to bring has been muddied. At least 846 companies papered over their stock option costs before coming under the rule by vesting their options grants early, according to a report by accounting analyst Jack Ciesielski in *The Analyst's Accounting Observer*. The move effectively put into the past expenses that would otherwise be counted over the next few years. It will take the hype. Options are not as attractive at companies like Microsoft, Pfizer, and Time Warner, whose stock prices have not risen in years. There, options can be a painful reminder of the might-have-beens. Companies that have eliminated options now talk about the value of cash. And they might have a point. An Aetna spokesman argued that a $500 check is a comparable replacement for a typical $40,000 a year employee who would have gotten options under the old plan for about 45 shares of stock. A Time Warner spokeswoman points out that most employees would rather get cash than stock options that over the last few years have given them little.

Which points up an unfortunate truth about options: They are a great way to let employees share in the wealth at a company whose stock is rising dramatically, but in most other cases they don't make for a very good incentive at all. When they were easy to give out, options were billed as a magic potion that would make employees come to work every day hoping to increase the stock price. But motivating employees is just not that simple.

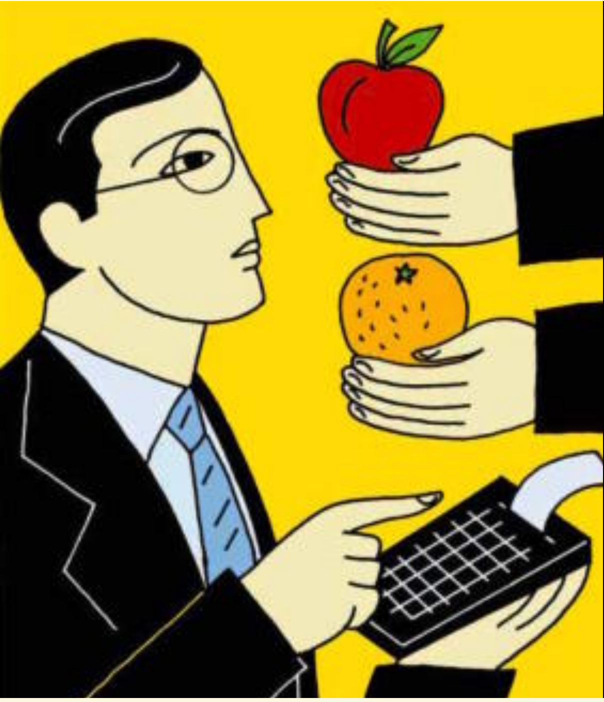
Nor, for that matter, is motivating CEOs. The history of the options boom is instructive here. The seminal moment for options was a 1990 paper by economists Michael C. Jensen and Kevin J. Murphy that argued that American companies didn't give CEOs enough incentive to worry about the stock price. Jensen and Murphy knew that giving top executives options would likely mean bigger pay packages, but they didn't anticipate how much bigger. (Murphy now says he feels like a doctor whose patient started swigging a bottle of wine a day when he prescribed a glass.)

Time Warner employees may now prefer cash over stock options

And what did the bigger pay packages accomplish? It's not clear. Murphy, now at the University of Southern California, thinks that better-designed—and, yes, bigger—executive pay packages may have helped create the stock market boom of the late 1990s. But the link between pay (options) and performance (stock boom) is tenuous. Consider this: Murphy and Jensen ended their article with a list of 25 companies that gave their CEOs the most sensibly structured package of incentives. Among their selections: Enron, Pan Am (which declared bankruptcy just months after publication), UAL, Toys 'R' Us, and others just as dreary.

Now, with the new rules in place, the options game has come full circle. First they looked like a nice incentive for CEOs. Then, when it became clear to everybody that you could give any number out and still declare profits every year, they seemed like a good idea for all. Now that they are a lot harder to give out, they don't look so irreplaceable after all. Companies have found they can live with their top tier of executives getting fewer options and the corporate middle fewer still. So some of the options have disappeared. But the outsize pay packages that options mania brought about still remain. ■

–With Louis Lavelle in New York, Amy Barrett in Philadelphia, Dean Foust in Atlanta, and bureau reports



Analyze This

Some analysts are counting options expense on their earnings estimates. Others are not. There are:

156
Companies with a majority of analysts excluding options from earnings estimates

326
Companies with a majority of analysts including options in earnings estimates

18
Companies with option impact insignificant or unknown

Data: Thomson First Call

roughly three years before that ploy plays out, says David Bianco, chief U.S. equity strategist at UBS Investment Research. Until then, earnings for those companies will look better than those of competitors that didn't use the gimmick, all else being equal.

That is just one reason why comparing price-earnings ratios across companies is perilous. For nearly one-third of the stocks in the S&P 500, a majority of analysts still exclude options expense when calculating their profit estimates, according to earnings tracker Thomson First Call, which provides the estimates used by Yahoo! Finance and other Web sites. The omission, which isn't usually flagged on free sites, makes shares of companies with a lot of stock options expense look cheaper than they really are. Shares of NVIDIA Corp., for example, traded recently for about 20 times this year's analysts' estimates but 24 times estimates counting the options expense. Victory can't be declared by accounting regulators without those basic numbers in synch. Until that happens, confusion reigns. Investors without access to expensive information services will likely suffer disproportionately.

The good news? The stock market has already taken much of its hit for the cost of options in the five years since the Enron Corp. and tech-stock collapses put options accounting front and center on the reform agenda. The debacles prodded institutional investors in many stocks, but not all, to focus on the shareholder wealth employee options were spiriting away. "The market has been resetting gradually for stock option expense," says Bianco of UBS. "At this point, the vast majority of it is already priced in." Phew.

–David Henry

ILLUSTRATION BY ANTHONY RUSSO

SOFTWARE

MICROSOFT'S SLO-MO SCRAMBLE

A new delay in its operating system signals its struggle to keep up in a Net-speed world

BY STEVE HAMM

WHEN MICROSOFT Corp. disclosed on Mar. 21 that the next upgrade to its Windows operating system, called Vista, wouldn't be available for consumers until January, the reaction was one of disbelief. After a five year wait, there would be yet another delay in the release, likely putting a damper on holiday PC sales. "They have totally lost their way," exclaims Michael A. Cusumano, a professor at Massachussetts Institute of Technology's Sloan School of Management. Some employees have lost patience, too. Mini-Microsoft, an anonymous insider, posted a blog item calling for heads to roll: "People need to be fired and moved out of Microsoft today. Where's the freakin' accountability?"

Though Microsoft isn't moving people out, it is moving them around. Sources say that Steven Sinofsky, who has run the company's Office franchise, will be tapped to oversee the next version of Windows. The news was first reported in *The Wall Street Journal*. It amounts to a demotion for Brian Valentine and Chris Jones, the two executives with hands-on responsibility for Windows Vista. Microsoft declined to comment on the move.

Yet the delay raises larger questions about Microsoft's ability to innovate at today's pace. While the company dominated the PC era, it now finds itself in a Web free-for-all. Its strategy of taking years to update its software looks positively archaic compared with fleet Internet companies such as Google Inc., which seem to unveil new software every few weeks.

Today, Microsoft's Windows is the equivalent of an unwieldy supertanker. One reason is that during the period Microsoft was being prosecuted for antitrust violations, the company integrated many new features and functions into the operating system—including its Web browser. That created a huge tangle of interdependencies. Vista is loaded with 50 million lines of computer code and has involved thousands of programmers. And even after Microsoft completes a new operating system, it needs to spend about a year testing how it will work with a dizzying array of hardware. It tests the software on hundreds of PC models and thousands of printers, keyboards, and other peripherals.

Some outsiders believe it's time for drastic action. "I'd like to see them build a new operating system from the ground up that's much simpler and smaller," says MIT's Cusumano.

Microsoft is experimenting with faster ways of developing software. Last November, Microsoft Chairman Bill Gates announced new online applications under the umbrella of Windows Live and Office Live. The company has launched test versions of a dozen services, and more are on the way. The newfound speed is evident. Its classified ad Web site was created in four months by five people. "I can do quick-twitch releases monthly," says Blake Irving, a corporate vice-president for MSN Communications.

But these are all pieces of software that run on top of Windows. Microsoft insists that it doesn't need to overhaul its approach to developing that all-important software. "Nothing about the announcement says there's something fundamentally wrong with the Windows model," says Brad Goldberg, general manager of Windows product management. Still, he says, the company plans to deliver future Windows upgrades more frequently. New releases could come out every year or two.

Yet the software giant may be forced to make more substantial changes to the way it builds Windows. Delays like those with Vista could hurt the loyalty of consumers and corporations, especially as stronger alternatives emerge from Apple Computer Co. and the Linux operating system. Unless Microsoft comes out with Windows upgrades more quickly and smoothly, it risks losing ground in the rapidly changing world of computing. ■

Vista's Long Road

Here are key milestones in Microsoft's road to delivering Vista, the next version of its Windows operating system:

OCT., 2001
The release of Windows XP, the predecessor to Vista. Development had already started on the next version, then code-named Longhorn.

AUG. 27, 2004
Microsoft says it will eliminate some of the planned features of Longhorn, renames it Vista, and says it will ship in the second half of 2006.

NOV. 1, 2005
Chairman Bill Gates announces a new generation of online software services, Windows Live and Office Live, designed to compete with Google and Yahoo! in the consumer market.

MAR. 21, 2006
Citing testing and quality reasons, Microsoft announces a delay in the release of Vista, pushing the versions for consumers and small businesses back to January, 2007.

BEBETO MATTHEWS/AP/WIDE WORLD

SCHAEFER His stock has returned 10% a year for a decade with little volatility

STOCKS

ISS LOOKS LIKE IT'S CHANNELING ICAHN

The proxy advisory firm says Fifth Third's CEO should go despite stellar governance

BY EMILY THORNTON

WHAT ARE SHAREholders supposed to do when a company with stellar corporate governance practices loses value for five years? Should they vote to reelect the CEO to the board of directors or oust him?

That's the question facing the 148-year-old Cincinnati-based retail bank Fifth Third Bancorp. On Mar. 10 proxy advisory firm Institutional Shareholder Services Inc. in Rockville, Md., advised its money manager clients to reject the bank's CEO, George A. Schaefer Jr., for reelection to the board. Why? "Consistent underperformance" of the bank's stock over the last five years, both on an absolute basis and relative to its peer group.

Yet Fifth Third is an overachiever in corporate governance. It has better practices than 99.8% of the companies in the Standard & Poor's 500-stock index, according to the ISS report. "Effective corporate governance is a key ingredient to a company's success," Schaefer boasted in 2003, when ISS scored the bank highly. "We are pleased to have these efforts recognized by ISS."

That was then. Now, shareholders may vote to get rid of Schaefer at the company's annual meeting on Mar. 28 based on the recommendation by ISS that they withhold their votes for directors up for an uncontested reelection, including Schaefer. "I have a tough time reconciling how we could get a corporate governance score better than any other bank in the universe and then [ISS advises a no-vote] based solely on share price," says Schaefer.

In the past, ISS, like other proxy advisers, considered stock performance only in the context of an overall score on corporate governance criteria ranging from board members' independence to executive compensation. Now, ISS' general philosophy is starting to resemble that of self-styled shareholder activists such as Carl Icahn and Kirk Kerkorian. Their message to corporate boards: Create value or scram.

OVERSTEPPING?

ISS IS ANSWERING the call of more investors who agree. In a survey last October, 58% of ISS' clients said long-term financial performance should be a factor in vote recommendations for or against directors. So ISS now evaluates companies' returns on a stand-alone basis over one-, three-, and five-year periods with weightings of 20%, 30%, and 50%, respectively. "Job No. 1 for the board of directors is to produce returns for shareholders," says ISS special counsel Patrick McGurn.

ISS says its clients' focus is shifting to companies' performance in part because so much progress has been made on many corporate governance fronts during the past five years. ISS is targeting only the worst performers, and even then the financial results aren't examined in a vacuum. ISS says it won't ding CEOs who are new or appear to be taking substantial actions to correct matters.

Yet the definition of sufficient corrective action is fuzzy. In Fifth Third's case, ISS said the bank lacks a "demonstrated turnaround strategy." But in 2005, Fifth Third added 63 banking centers and increased its salesforce by 1,400 positions.

Some analysts worry that ISS is overstepping its expertise by making tough calls on performance. On Mar. 16, Richard X. Bove of investment bank Punk Ziegel & Co. fired off a research note calling ISS' advice "totally inappropriate" and pointing out that Fifth Third's assets have increased tenfold since Schaefer took over in 1990. Nell Minow, a former president of ISS who now runs governance researcher The Corporate Library LLC, warns that ISS may create "incentive for earnings manipulation that may not be in the shareholders' long-term interest"—precisely the sort of activity good governance is supposed to prevent.

ISS argues that Schaefer pre-

A Lending Laggard

Fifth Third Bancorp's stock has trailed the market for five years

	PERIOD OF RETURN*		
	1-YEAR	3-YEAR	5-YEAR
Fifth Third	–17.26%	–11.22%	-6.72%
S&P 500	4.91	14.39	0.54

* Annualized returns

Data: Institutional Shareholder Services Inc.

AL BEHRMAN/AP/WIDE WORLD

sided over the erosion of nearly 7% of shareholder value over the last five years. But rival proxy adviser Glass, Lewis & Co. in San Francisco is advising clients to reelect Schaefer in part because Fifth Third has outperformed the S&P 500, with less volatility, over 10 years. "Who wouldn't like a stock that has returned 10% annually to shareholders over 10 years with very little volatility?" wonders Glass Lewis Chief Executive Gregory P. Taxin.

Schaefer will learn the answer at the bank's annual meeting. Meanwhile, ISS estimates that CEOs of as many as 70 other companies it evaluates may be on the hot seat this year. Expect sparks. ■

BusinessWeek online For more on the Institutional Shareholder Services debate, go to www.businessweek.com/extras

INFLATION

WHAT YOU FORESEE IS WHAT YOU GET

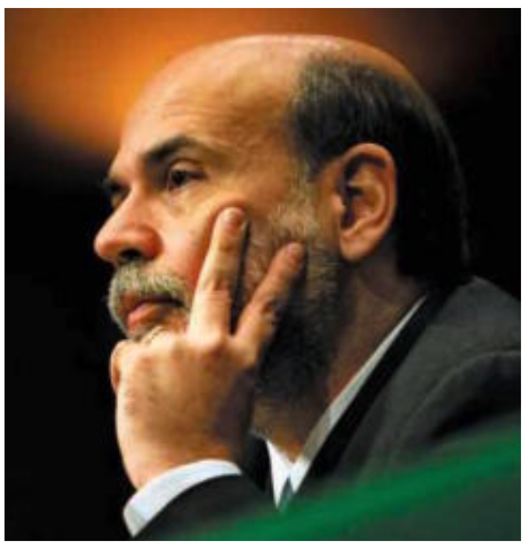
Expectations of future price hikes may play a big role in how much and how fast the Fed raises rates

BY CATHERINE YANG

WHAT THE HECK are inflation expectations, anyway? You won't find the term in any of the major economic data releases put out by the government. Yet whether inflation expectations are rising or falling may turn out to be a critical factor in determining how far and how fast the Federal Reserve raises interest rates.

That, at least, is the new line coming out of the Fed these days. Inflation expectations—a bit of a touchy-feely concept—represent the beliefs of consumers, investors, corporate execs, and economists about how fast prices will rise in the future. To new Fed Chairman Ben S. Bernanke, inflation expectations are a key indicator. If people believe inflation will stay low, the Fed can afford to relax a bit. But if the masses start anticipating faster inflation, the odds are greater that the Fed will need to hit them with higher rates even if actual price hikes remain moderate.

The good news, for now, is that "long-term inflation expectations [are] apparently anchored at low levels," as Bernanke noted in a Mar. 20 speech. By some measures, inflation expectations are a bit lower than a year ago. That suggests the Fed will be more likely to stop raising rates sooner rather than later after its expected quarter-point hike, to 4.75%, at the Mar. 27-28 meeting of the Federal Open Market Committee (FOMC).



JAY L. CLENDENIN/POLARIS

> "Long-term inflation expectations [are] apparently anchored at low levels."
>
> –*Fed Chairman Ben S. Bernanke*

Bernanke has some critical allies on the policy-setting FOMC, including Janet L. Yellen, president of the Federal Reserve Bank of San Francisco. On Mar. 13, Yellen gave an entire speech about the importance of inflation expectations. She also noted that "clear communication of a numerical long-run inflation objective"—something Bernanke supports—may help keep expectations in line.

How are beliefs about future inflation measured? One way is to ask economists what they think is going to happen. According to the Philadelphia Fed's Survey of Professional Forecasters, economists expect consumer inflation to average 2.5% over the next 10 years, only a tad above their 2.45% forecast of a year earlier. That's not very worrisome.

CREDIBILITY CUSHION

ANOTHER WAY TO JUDGE expectations is to look at the behavior of investors—in particular, the people who buy Treasury Inflation-Protected Securities (TIPS), which are indexed to inflation to give investors a fixed real return. The spread between 10-year TIPS and regular 10-year Treasuries, a measure for expected average annual inflation over the next decade, is 2.68%, according to calculations by Timothy S. Fuerst, an economics professor at Bowling Green State University in Ohio. That's slightly below the 2.72% of a year earlier.

The danger, of course, is that expectations about future prices might jump, forcing the Fed to raise rates sharply to maintain its credibility as an inflation fighter. That's what happened in the 1970s, when the public's lack of faith in the Fed's inflation-fighting resolve sent prices—and expectations of future inflation—spiraling out of control after the oil shock.

Contrast that with today. The Fed has built credibility by both aggressively fighting inflation and communicating its commitment to price stability. As a result, even as energy prices skyrocketed in recent years, inflation expectations hardly budged, and non-energy inflation stayed relatively low.

The emphasis on expectations could also be Bernanke's way of getting people used to the more controversial idea of setting inflation targets. After all, if the Fed is going to react to beliefs about future inflation, it's only natural for the central bank eventually to specify explicitly the acceptable level of inflation.

But that's a debate for later. For now, with such benign expectations for inflation all around, the Fed has finally bought itself a little breathing room. ■

GLOBAL MEDIA

AL JAZEERA MEETS AMERICAN RESISTANCE

Its English-language news channel can't find a U.S. carrier, but that won't stop its launch

BY STANLEY REED

WHEN EXECUTIVES for broadcaster Al Jazeera first planned a new 24-hour English language channel, the idea was to offer viewers an alternative to CNN, the BBC, and other Western news outlets. They hired such heavyweight talent as veteran TV host Sir David Frost to lend cachet. What they didn't prepare for was the cold shoulder they would receive in the U.S.

Just two months before its scheduled launch, Al Jazeera International still has no distributors in the important U.S. market, despite talks over the past year with nearly all the big players, from Comcast to Time Warner to DirecTV.

It's not just the controversial nature of Al Jazeera that gives distributors pause, say some cable executives privately. Whether it's a convenient cloak for them or not, they say it also makes little economic sense for them to pay a fee for yet another channel in the overly fragmented 400-channel TV universe. Satellite service EchoStar Communications Corp., the lone distributor in the U.S. of the Arabic-language Al Jazeera, is the only company expressing any interest so far. "We would be willing to consider carriage," EchoStar spokeswoman Kathie Gonzalez told *BusinessWeek* in an e-mail. She declined to comment on the status of talks.

SERIOUS BACKING

NO MATTER HOW daunting its prospects, the new channel has the enthusiastic backing of Qatar's ruling Al-Thani family. Tiny Qatar has the world's third-largest natural gas reserves and fast-accumulating foreign assets, now estimated at $30 billion. Unlike Western broadcasters facing constant financial pressure, the Qataris are willing to fund the new outlet indefinitely, executives say. But it will share some resources with the Arabic channel, with 48 million viewers.

The American snub hasn't dissuaded the Qataris from giving the new channel the money to lure such on-air personalities as Veronica Pedrosa, a CNN Asia anchor, Dave Marash, a correspondent for ABC's *Nightline*, and Rageh Omaar, the BBC's former Baghdad reporter. The attraction? Explains Frost: "I try to be where the new frontiers are if I can find them, and obviously Al Jazeera is very much the new frontier at the moment."

Few experts expect the channel to draw a mass audience. "There is a small core of news junkies in America who will be interested," says Richard Wald, the Fred Friendly Professor at Columbia University's Graduate School of Journalism. But to have a significant impact, he says, Al Jazeera will have to offer more than just Middle East expertise. Frost says he'll be featuring topical political interviews but lightening the lineup with guests such as Paul McCartney and David Beckham.

As tough as it has been in the U.S., Al Jazeera execs say they are not willing to compromise to ink a deal. Commercial director Lindsey Oliver says cable operators are in a position to drive a hard bargain, including forcing new channels to agree to skip streaming over the Internet to reduce competition. But that's not a pact worth making, she says.

Besides, Oliver contends, initial numbers in the U.S. are not crucial to Al Jazeera International, adding the channel's target is a global English-speaking audience, not just an American one. Oliver figures that the channel will have 40 million households locked up by launch time, thanks to deals with Britain's British Sky Broadcasting Group PLC, as well as distributors in India, Australia, France, and Germany. But without the U.S., Al Jazeera may not be pushing all of the frontiers Sir David had in mind. ■

HEADQUARTERS Al Jazeera's high-security Doha offices

RABIH MOGHRABI/AFP/GETTY IMAGES

Getting Snubbed In the U.S.

Al Jazeera International, the 24-hour English-language news channel, has had trouble hooking up a cable or satellite distributor. Some stats:

0
The number of distribution deals in U.S. so far

40 Million
Estimated number of households outside the U.S. that will receive the new channel

$30 Billion
The foreign assets of Al Jazeera's main backer, the tiny nation of Qatar

Data: Al Jazeera International

BusinessWeek online For an interview with David Frost on Al Jazeera International, go to businessweek.com/extras

EDITED BY RICHARD S. DUNHAM

Senator Inhofe's Climate of Confrontation

BY JOHN CAREY

THE REVEREND RICHARD CIZIK IS AN EVANGELICAL Christian and a die-hard Reaganite. So he was surprised that a closed-door meeting called late last year by conservative Senator James Inhofe (R-Okla.) was all about Cizik's evil deeds. Inhofe called Cizik, government affairs chief at the National Association of Evangelicals, a liberal wolf in sheep's clothing. "I sat there with my mouth open," recalls a meeting participant.

Cizik's sin? He believes that climate change is a growing problem, and that Christians have a duty to protect the planet by cutting emissions of greenhouse gases. In contrast, Inhofe, the chairman of the Senate Environment & Public Works Committee, has famously derided global warming as a "hoax." He has been on the offensive against those he considers heretics. That has left business in doubt about the regulatory environment.

Seeking Tax Records

LAST YEAR, Inhofe demanded six years of tax and membership records from two groups of state and local air-pollution control officials after they testified that his proposed clean air legislation was too weak. On Feb. 7, the day before evangelicals kicked off a campaign for carbon controls, Inhofe sent a preemptive letter to senators asserting "there is, in fact, no movement in that direction" among evangelicals. Now he is requesting information on all employees and projects at the National Center for Atmospheric Research. Inhofe is "using the power of government and the power of office to threaten," says Donald Kennedy, editor-in-chief of *Science*.

CHRIS MADDALONI/ROLL CALL

ON THE ATTACK Inhofe says global warming science is flawed

Inhofe's backers say he is providing a badly needed voice of reason amid environmental alarmism. Inhofe spokesman Bill Holbrook says the senator was traveling and not available to comment. But Inhofe has argued consistently that global warming science is uncertain and carbon curbs would ruin the economy.

This may sound like another inside-the-Beltway spat, but the business consequences could be huge. Adding to the scientific evidence of global warming, *Science* published two papers on Mar. 24 warning of a possible large sea level rise. Executives such as Jim Rogers, CEO of Ohio utility Cinergy Corp., believe the U.S. inevitably must join other nations in curbing carbon. They want clear rules so they can plan future power plants. "Climate change is a key issue for Corporate America," says Mindy S. Lubber, president of the Coalition for Environmentally Responsible Economies. U.S. businesses are behind overseas rivals in developing climate-friendly technologies, she adds.

Companies are caught in the middle. In this political climate, "business leaders are holding back from saying publicly what they believe privately," says William Reilly, Environmental Protection Agency chief for George H.W. Bush and a DuPont director. Adds an industry rep: "If we say anything positive, the environmentalists come after us with a vengeance. If we say anything negative, Inhofe comes after us with a vengeance."

Some green conservatives are speaking out more. "Inhofe is to the right of Attila the Hun on climate change," says the Reverend Jim Ball, director of the Evangelical Environmental Network. Meanwhile, Environmental Defense and the Ad Council were set to unveil an ad campaign on Mar. 23 aimed at boosting public awareness of climate change. If more Americans come to believe the problem is urgent, eventually even Inhofe may not be able to hold back the tide.

CAPITAL INSIDER

SMALL BUSINESSES: NO CHILL FROM SARBANES

TO HEAR BIG BUSINESS tell it, the regulatory reforms of the 2002 Sarbanes-Oxley Act are driving companies out of public financial markets and starving small businesses of capital. But that message apparently hasn't reached Little Business. A record 881 small companies filed with the Securities & Exchange Commission in 2005 to register new stock issues and raise $16.3 billion in new capital, according to a study by researchers SME Capital Markets. That's up from 435 in 2003. Critics note that the SEC has deferred SarbOx' Section 404, the internal-audit requirement that businesses consider burdensome, until 2007 for little companies. But small-business CFOs interviewed for the study say they would have gone public even if 404 applied to them, because they see no choice for raising capital.

MORE COMPANIES AGREE TO DISCLOSE DONATIONS

ADVOCATES FOR shareholders are making headway in their bid to prod companies to disclose soft-money political donations. Bristol-Myers Squibb and Staples are the latest businesses to agree to reveal and give their boards oversight on soft money donations—the large contributions that companies and individuals can make to state parties. In addition, Amgen's board has endorsed a shareholder resolution calling for oversight and disclosure. Shareholders will vote on the plan at its May annual meeting. Companies that earlier agreed to disclosure and oversight are Morgan Stanley, Johnson & Johnson, Schering-Plough, PepsiCo, Coca-Cola, and Eli Lilly.

ENTREPRENEURS

EBAY'S RHINE GOLD

Thousands of German startups are using the auction site to sell goods

BY JACK EWING

IN THE U.S., GROUND ZERO OF modern capitalism, it is almost an article of faith: Europeans have grown risk-averse and lack entrepreneurial zeal. But don't tell that to the thousands of folks who use eBay Inc. to do an end run around decades of state-imposed regulations and old ways of thinking. One of them is German businessman Norbert Otto, who recalls the exact moment he realized selling ski gear over eBay had become far more than a hobby for him.

When Otto printed out his checking account statement at a local bank's automated teller machine, the statement had so many pages that the branch manager scolded Otto for tying up the ATM for so long. Soon after, Otto opened a commercial account for Sport Otto, his online business, which last year sold $1.8 million worth of skates, skis, snowboards, and other sporting goods exclusively over eBay.

Not bad for an operation that began three years ago as a way for Otto's son to earn extra cash. Today, Sport Otto has 25 part-time employees, a large truck to haul merchandise from Dutch ports, and operations that occupy much of Rabenkirchen, a hamlet of just 60 inhabitants two hours north of Hamburg. In this region close to Denmark, where old-timers speak a dialect incomprehensible to outsiders and unemployment is 12%, Sport Otto is one of the few local employers creating new jobs. "We're very thankful that this online platform exists," says Otto, 58, a sports instructor by profession who manages the business with his 20-year-old son, Jan. "In this region, it's the only chance we have."

The Ottos' small-but-thriving operation provides a window into one of Europe's fastest growing entrepreneurial sectors: the eBay store. According to a survey by ACNielsen International Research, the Ottos are among 64,000 Germans who earn at least 25% of their income from eBay, selling all manner of collectibles, furniture, electronics, and more. Germans snatched up $6 billion in merchandise on eBay in 2004, the most recent year for which such data are available.

Germany's eBay market is second only to the U.S. A decade of slow growth and stagnant wages has turned Europe's largest economy into a nation of bargain hunters, with 20 million registered eBay users. That's close to 25% of the population, a greater share than in any other country in which eBay operates. With eBay gaining momentum, its success in Germany could portend a similar boom in France, Italy, and elsewhere in Europe.

In red tape-bound Germany, starting an eBay business is a relative snap for anyone with broadband and inventory and shipping software, which is readily available for a few thousand dollars. And logistics companies such as German post office Deutsche Post offer services tailored to small e-commerce operations. Compare that with the difficulties of finding startup financing in a country where banks are reluctant to lend and relatively few people own houses that can serve as collateral. Even those who scrape together funds are constrained by myriad regulations. Shops, for instance, must close on Sundays and by 8 p.m. on weekdays.

GIANT CUSTOMER

SOME EXPERIENCED businesspeople see eBay as a growth opportunity in an otherwise slack economy. In 2003, Sven Asböck and Frank Hoffmann, who had worked for a mail-order company that went bankrupt, launched DTG Dynamic-Trade in Neumünster, an hour north of Hamburg. The business snatches up all sorts of surplus merchandise, then sells the stuff on eBay. Sales have doubled every year, to $6 million in 2005, and the company employs 22 full-time workers. "We sell everything you can imagine," says Asböck. No kidding: Current offerings include bedroom sets, toasters, and telescopic rifle sights.

The business of supporting German e-merchants has also grown into a thriving industry. More package deliveries are generated by eBay for Deutsche Post and its DHL unit than the biggest catalog retailers. One customer is Bielefeld-based SE.LL Marketing, which helps customers such as toy train maker Brio unload ex-

CHART BY LAUREL DAUNIS-ALLEN/BW

TEAM OTTO In a slack economy, eBay is a growth engine

cess merchandise on eBay. SE.LL rarely even sees the goods it auctions off, having outsourced the warehousing, packing, and shipping to DHL. "We want to focus on services. Fulfillment is not our core business," says SE.LL co-founder Christof Sander, 29, a former manager at German media company Bertelsmann.

In Rabenkirchen, eBay—combined with the easy availability of logistics services and software—has created a hotbed of e-commerce. For two decades Otto coached basketball, track, and other sports at municipal sports clubs and ran a ski shop on the side. But then the financially strapped local government cut his hours in half, and a recession devastated his shop's sales. In 2002, when son Jan, then 17, asked for money for driving lessons, Norbert told him he would have to earn it by selling off some of the ski shop's excess inventory. The skis sold quickly on eBay—at twice their wholesale price.

Soon Jan found himself behind the wheel of a battered blue cargo van, ferrying Chinese-made parkas and plastic sleds from the port of Rotterdam. Sport Otto began hiring staff, using part-timers to avoid paying health and pension contributions that can nearly equal an employee's take-home pay. The fledgling company also took over a cluster of small buildings in Rabenkirchen that had been vacant ever since the former tenant, a construction company, shut down.

BUYING A BENZ

AT FIRST GLANCE, the Ottos don't appear to run an especially tight ship. Swim goggles, baseball bats, and mosquito nets are arranged haphazardly on wooden shelves. Yet every item is bar-coded and scanned. From a desk equipped with two flat screens and littered with wholesale sporting goods catalogs, Jan knows when to redeploy snowboarding trousers from the barn to the packing shed. As customers bid, software tallies the average price and profit on each sale.

The business hasn't made the Ottos rich. Their one luxury is a Mercedes-Benz SUV. Jan lives in the same building used to pack orders, while Norbert occupies a modest apartment above Sport Otto's offices. Both start work at 7 a.m. and often don't finish until late in the evening. They dream of building a modern, computer-driven warehouse and buying products directly from Asian suppliers. For now, Norbert says, "we're investing everything back into the business." Spoken like a true entrepreneur.

–With Robert D. Hof in San Mateo, Calif.

(TOP TO BOTTOM) PHOTOGRAPHS BY GERRIT MEIER; LI LIANG/IMAGINECHINA.COM

CHINA

A Behemoth Kept at Bay

When Gary Wang wanted to buy a microphone for his iPod, he didn't bother with eBay EachNet, the Chinese arm of eBay Inc. Instead, he went to rival site TaoBao, quickly found what he wanted, and paid for the gadget with TaoBao's electronic payment system. He got the machine by courier the same day. "TaoBao is naturally the first place I go" when shopping online, says the 32-year-old Wang, an eBay user during his studies in the U.S. and now CEO of Toodou, a podcasting company in Shanghai.

That kind of enthusiasm has made TaoBao China's No.1 auction site, leaving eBay in the dust. TaoBao last year was home to 72% of China's $1.7 billion in online auctions, measured by the value of goods sold, compared with eBay's 27%, according to the China Internet Development Research Center. That spells trouble for eBay's international ambitions, especially in the world's No.2 Internet market, with 110 million Netizens and Web auction transactions that grew 235% last year.

TaoBao stole the lead by offering its services for free. And TaoBao's founder, Jack Ma, has been better at creating tools users like, including an electronic payment system and an instant messaging service for traders. "Jack Ma believes in building community first" and will worry about profits later, says Morgan Stanley analyst Richard Ji.

But eBay is determined not to repeat its experience in Japan, where it beat a humbling retreat in 2002. So in January it scrapped transaction fees and now charges sellers as little as 1¢ per item for listings. Then in February, eBay added a feature allowing traders to talk via Internet phone links. Important steps, and vital if eBay wants to stay in the game in China.

THE UNDERDOG The auction site lags far behind homegrown TaoBao

LEGAL EAGLE
If Yoko Mukai passes the bar, she'll enter a good job market

TORIN BOYD/POLARIS

JAPAN

LAWYERS WANTED. NO, REALLY

Once litigation-averse, Japan is rushing to fill a shortage of attorneys

BY IAN ROWLEY AND KENJI HALL

REMEMBER THIS OLD chestnut? If you were to lay all of America's lawyers end-to-end on the equator...it would be best to leave them there. Well, it now appears that Japan might have room for them instead. After decades of enjoying one of the world's smallest concentrations of attorneys, the country is embarking on a program to mint thousands of new ones every year.

For much of the postwar era, Japan didn't feel it needed many lawyers. That worked in a consensus-driven society bent on economic growth. Court battles in Japan were always a last resort and considered very bad form. Today, with patent disputes and cross-border mergers on the rise, the nation is discovering that legal sharpies actually come in handy when settling disagreements. But with just 22,000 licensed attorneys, compared with more than a million in the U.S., "it's extremely difficult to get talented lawyers [in Japan]," says Stephen Bohrer, an American who heads cross-border transactions at Nishimura & Partners, a big Tokyo law firm.

Japan's legal community finally seems to be getting serious about easing the shortage. In 2004 the government for the first time allowed universities to begin offering graduate programs in law. Since then 74 new law schools have opened their doors, with the first graduating classes—some 3,000 students—to hit the streets this spring. Prior to the shift, Japan's sole graduate-level legal program was a two-year course of study sponsored by the Supreme Court—but it was only offered to those who managed to pass the bar exam first. And only 1,000 to 1,500, or about 3% of those who sit for the test, were allowed to pass annually. That meant most candidates took the bar exam at least five times before they passed—or gave up.

Tokyo is doing its best to make the new schools attractive. This year the bar results will be weighted so that about a third of grads pass, leaving just 500 spots for the 40,000 or so exam takers who didn't attend one of the new programs. By 2010 the government plans to double the number of test takers allowed to pass the exam, to about 3,000, with most of the increase going to grads of the new schools. "Law school has expanded my possibilities," says 30-year-old Yoko Mukai, who signed up for a $15,000, two-year course at the University of Tokyo School of Law after failing the bar several times in the past.

MERGER MAVENS

WHAT WILL JAPAN do with all its new lawyers? Given that the economy is growing at its fastest clip in years, demand for savvy merger attorneys is surging. And Japanese companies are turning to the legal system to settle disputes that once might have been worked out in back rooms. In 2004, for example, Sumitomo Trust & Banking and Mitsubishi Tokyo Financial Group faced off in court after UFJ Holdings pulled out of a planned deal with Sumitomo and merged with MTFG instead. "In the past [such a court battle] would never have happened," says Masatomo Suzuki, a partner in Tokyo with Cleveland-based law firm Jones Day.

With so many new schools starting all at once, growing pains are inevitable. One concern is finding enough qualified professors. And some fret that it might not be fair to give law school grads a leg up on the bar exam. "Everyone is watching closely to see what kind of people they'll churn out," says Robin Doenicke, a partner at Zensho Consulting Group, a legal search firm in Tokyo.

Despite the changes, it's unlikely Japan will ever fully embrace the kind of legal conflict common in the U.S. Litigation is messy and flies in the face of Japan's cultural preference for harmony. But a more sophisticated, and contentious, legal system may be just what the country needs in order to keep its economic overhaul on track. And that means tolerating unseemly courtroom brawls that once might have shocked.

THE STAT

People per Lawyer

JAPAN
5,800

U.S.
270

Data: Japan Federation of Bar Associations, American Bar Assn.

STAY AWHILE Relaxing at Wainwright Bank

Coffee, Tea, or Mortgage?

Banks are cozying up to customers while using high-tech tools to identify prospects

BY MARA DER HOVANESIAN

BARCLAYS BANK PLC WAS long the dominant credit-card player in the British market, until American rivals showed up a few years ago with cutthroat pricing and direct-mail sales tactics. Barclays had been getting more than 80% of its new customers the old-fashioned way—from application forms stacked in piles at its local branches. It needed to raise its game, but how? The storied lender fired up its database of 10 million bank account customers, augmented it with demographic and behavioral data and credit bureau information, and came up with a list of customers who were inclined to sign up for more services. Then it started selling them stuff.

The strategy worked. Barclays went from attracting around 500,000 to 700,000 credit-card accounts a year to more than 1.7 million by 2005. It also began tracking credit-card purchases and capturing what customers are looking for on its Web site to fine-tune promotions and spur sales in other parts of the bank. "The future will be driven by customers who are signaling [what they want] through the Internet and other areas," says Keith Coulter, managing director at Barclays U.K.

Ah, the Internet. That's where savvy shoppers call up the latest and best rates on any number of financial products and services and sign up for them in a matter of minutes. Add to that the emergence of peer-to-peer banking in the form of PayPal Inc. and Prosper.com—which cut out banks entirely—and the possibility of Wal-Mart Stores Inc. entering the business, and you have the perfect conditions for what industry people call churn, and what the rest of us call defections.

That's why banks are in full-scale makeover mode. Washington Mutual Inc., a pioneer in adopting sales strategies perfected by retailers, routinely hires people from Starbucks and other places to drive sales. But it's doing far more than just calling branches "stores" and recasting tellers as sales associates. WaMu Chief Operating Officer Stephen J. Rotella calls it a "cultural awakening."

> Banks are adopting strategies long known to retailers

The most forward-thinking banks, among them Wachovia Corp. and Bank of America Corp., are enlisting architects to redesign their sleepy storefronts, behaviorists to profile customers, and high-tech consultants to rev up their 21st century marketing machines with high-tech gadgetry and systems. Susan Duchesneau, client relationship manager in the financial services unit at SAS, a business intelligence and analytics firm in Cary, N.C., says banks "will know how to predict the future and change their customers' behavior."

In the past year, Bank of America has invested heavily in creating a single repository of consumer data to get a view of what customers are likely to do and when they are likely to do it. "We are increasingly capable of predicting both," says Cathy Kenworthy, who heads consumer marketing at Bank of America. "But compared with the retailers, we've got a long way to go."

A long way indeed. Banks attract less than a third of the $3,500 that the average American household spends each year on financial services. To capture more market share, they must sell products across the entire financial spectrum, from brokerage services to home-equity lines, certificates of deposit to credit cards. And once they succeed in scoring new business, they must hold onto it.

HOLISTIC VIEW

INCREASINGLY, THEY'RE betting that technology will get them there. They're turning a massive volume of transactions, from credit-card purchases to online in-

PLAYBOOK: BEST-PRACTICE IDEAS

The Toaster Is Toast

The latest tactics banks use to grab your attention

GIVE THEM GOODIES

Umpqua Bank of Roseburg, Ore., hands out Umpqua chocolate and has a digital music kiosk so customers can rip and burn tunes onto CDs

HOME AWAY FROM HOME

A plasma TV and lounge, free coffee and doughnuts, and a cybercafe lure customers and non-customers to **Wainwright Bank & Trust in Boston**

SHAWN G. HENRY

quiries and call-center complaints, into bits of intelligence used to piece together holistic pictures of customers's wants and needs. "Business intelligence [helps] pinpoint who might be interested in particular products," says Mark N. Greene, vice-president for strategy at IBM's Financial Services group.

Mostly, banks mine for behavioral clues, such as when a customer is about to switch banks or may be in the market for more services. If, say, a couple has recently paid for flowers, an expensive cake, and a tropical vacation, chances are they are newlyweds—and might soon want a mortgage. What's more, Barclays isn't the only one zeroing in on its best prospects. Last year, Wachovia created profiles of 1.2 million of its most profitable customers, and assigned "financial specialists" to call them to see if there's anything they need. The effort contributed to a 9% increase in the average customer balance last year.

Banks are also trying to make their customers "stickier"—more likely to hang around a branch. It's no easy task. Industry studies show that pedestrians walk faster past a bank than past other establishments. Some banks are redesigning branch offices to be more engaging, with play areas for kids and digital music kiosks for their parents. Tiny Wainwright Bank & Trust Co. in Boston has turned bank design on its head. It invites people—customers or not—to surf the Web at its cybercafe, cozy up on the couch and watch TV, or sit by the fireplace and enjoy free goodies from Dunkin' Donuts.

Following the credit-card industry's lead, some banks are offering membership rewards for the first time. Citibank's ThankYou Network, launched in April, 2005, offers loyalty points redeemable for goods and services. The program has attracted 9.3 million accounts so far. "The objective is to create an experience that is very unbank-like," says Paul Kadin, marketing director at Citibank North America, whose promotion budget now includes "appreciation stations" with simulated surfing, golf, basketball, and other leisure experiences.

Banks are also monitoring spending patterns and targeting people accordingly. For instance, "if they figure out people shop at Starbucks seven times a week, they could offer free lattes," says Trevor Rubel, vice-president for products at Intelligent Results Inc., a predictive modeling outfit in Bellevue, Wash. "Or if someone is shopping at Home Depot several times a month, a bank can offer a home-equity product. It all comes to getting back to a banking relationship that you know and [that] knows you."

STRATEGIC WEAPON

TECHNOLOGY IS allowing banks to pitch products far outside the confines of branches. BlackBerry and cell-phone alerts tell customers about current promotions. And call centers are turning into marketing centers. Cleveland's KeyCorp identified life-stage markets, such as Young Transactor, Family Asset Builder, and Mature Thriver based on surveys about attitudes, aspirations, and demographics. Incoming calls from electronically tagged customers are routed to trained operators, who are prompted with cues on how to steer the conversation. "Call centers were an operational utility, a necessary evil," says Trina Evans, director of KeyCorp's centers, which have seen a 150% increase in sales since 2003 without an increase in staff. "Now we are a channel to drive business and a strategic weapon for the company."

In the near future, banks will embed chips in ATM cards that alert managers when preferred customers have walked in the branch door. Voice recognition and semantic engines on voice call systems will be rewired to indicate that a caller may be a promising sales prospect. Microsoft Corp. says it hopes to position its Xbox 360 video-game console as an engaging financial tool. "If a bank produced a game that allowed you to simulate what impact your current decisions will have on the future, you and your family could have some serious fun," says Bill Hartnett, general manager of strategy for Microsoft's Financial Services Group.

Human contact is still the marketing vehicle of choice, however. "We have all the traffic we need and then some," says Bank of America's Kenworthy. "Our marketing challenge is to make our associates more effective. That's the whole enchilada."

GREEN APPEAL

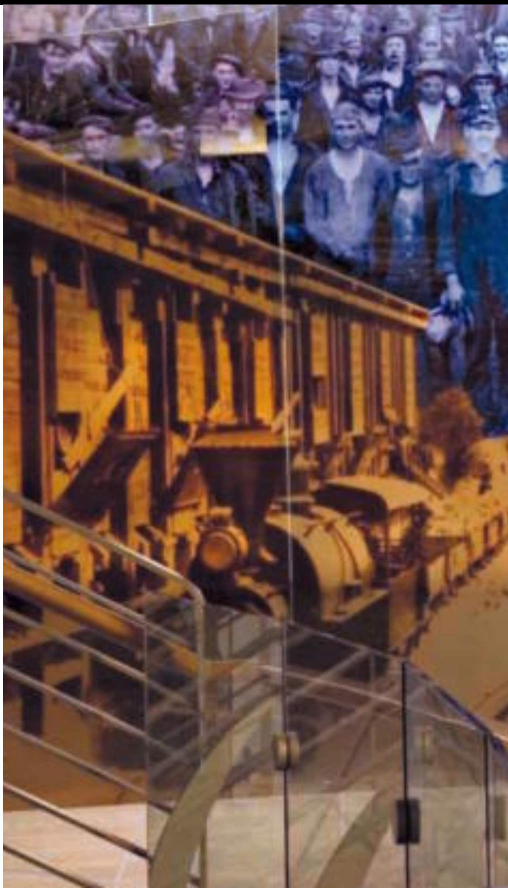
Pittsburgh-based PNC Bank's branches appeal to the ecologically minded with energy-efficient fixtures and countertops made of recycled paper and sustainable wood

FREE TICKETS

Bank of America of Charlotte, N.C., offers free tickets to 50-plus museums in the Northeast to customers during May, National Museum Month

COMMUNITY OF INTERESTS

First National Bank of Hermitage, Pa., has a Lifestyle 50 club that organizes trips for fiftysomethings to exotic destinations



Time to 'Make a Buck in the Muck'

Mine operator Phelps Dodge aims to strike while the copper is hot

BY CHRISTOPHER PALMERI

AMID THE PRICKLY PEAR cacti and greasewood shrubs of Safford, Ariz., something else is blooming: jobs. Over the past three years, the town's largest employer, mining giant Phelps Dodge Corp., has added 300 positions at its nearby facilities. Many more are coming as the company hopes to begin construction this summer on the first major new copper mine in the U.S. in over 30 years.

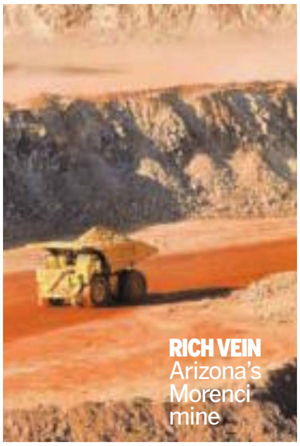
It represents a rich vein of cash for Safford, a hamlet of 9,600 hardy souls in the desert 165 miles southeast of Phoenix. Housing starts are up and new restaurants have opened, bringing new customers to establishments such as Nikki's Hard Rock Beauty Shop. "Our Wal-Mart got super-sized," says Sheldon Miller, director of the local chamber of commerce. "It's like jump-starting the economy."

The global boom in commodity prices is breathing new life into communities such as Safford, and giving an even bigger boost to Phelps Dodge, the largest copper miner in the U.S. Copper prices have surged from 78¢ to $2.34 per pound in the past three years, as strong demand from China and India at times exceeded the industry's ability to produce the metal. Last year, Phelps Dodge earned $1.5 billion on sales of $8.2 billion, after posting a loss of $338 million as recently as 2002. The company's stock price has shot up sixfold since then, to a recent 74 per share.

For Chief Executive Officer J. Steven Whisler, the new prosperity is bringing its own challenges. A Phelps Dodge employee for three decades, the 51-year-old Colorado Springs native has seen copper prices ebb and flow and knows the importance of planning for the bad times. He has quadrupled capital spending to $700 million a year, split the stock, paid down over $1.7 billion in debt, and earmarked $935 million to cover retirement, health care, and environmental clean-up costs. That means that the company's pension plan is now fully funded. "Almost every week you pick up a newspaper and an American icon is struggling with its pension liabilities," Whisler says. "That creates stress with our employees."

Even after all of Whisler's shoring up of the balance sheet, he still had a cash pot of $1.9 billion, and just $677 million in debt, at the end of 2005. He has begun returning a big chunk of cash to shareholders: Since December the company has paid out $900 million, or $4.50 per share, in special dividends. It plans to distribute at least another $600 million by the end of 2006.

For some shareholders, though, those efforts aren't enough. Atticus Capital LLC, a New York City-based activist hedge fund that controls 10% of the company's shares (half of that in the form of



RICH VEIN Arizona's Morenci mine

Turning **Copper** into Gold

Copper prices have tripled in the past three years, making Phelps Dodge Chief Executive J. Steven Whisler a very popular man. Here's how he's trying to please his various constituents.

EMPLOYEES Creating hundreds of jobs with $1.6 billion in capital projects, including the first major new copper mine in the U.S. in over 30 years. Also put $535 million into trusts to shore up retiree health-care and pension accounts.

ENVIRONMENTALISTS Putting $800 million into cleanups at older mine sites, winning kudos from activists such as Nancy Freeman, who's getting new wells and water testing for her hometown of Green Valley, Ariz.

SHAREHOLDERS Paying out $1.5 billion by the end of this year in special dividends or share buybacks. Hedge fund Atticus Capital, however, wants billions more, something Whisler calls "a reckless bet that could threaten our company's future."

DANCOOGAN.COM

CEO WHISLER "You have to plan...on the down cycle to survive the tough times"

options), has been pushing the company to embark on a multibillion-dollar stock-repurchase program, arguing that shares are undervalued. In a letter on Feb. 15, Atticus executives Timothy R. Barakett and David Slager told Whisler they had hired outside advisers to consider options, including selling the company out from under him. "A significant buyback of stock is not only the right thing to do for your shareholders; it is your surest guarantee of independence," the letter states. An Atticus spokesman declined comment.

CYCLICAL SAGA

WHISLER FIRED BACK in a press release, calling Atticus' demands "a reckless bet that could threaten our company's future." Interviewed three weeks later in Phelps Dodge's copper-topped headquarters building in downtown Phoenix, Whisler was less combative but still resolved not to bend in order to please Atticus. "We've seen a few cycles and we'll probably see a few more," he said. "In this business, you have to plan and focus on the down cycle to survive the tough times."

The company has had more than its share of tough times. Founded in 1834 as a New York-based trading house, Phelps Dodge is among the last independent copper producers, as once-storied names such as Anaconda and Kennecott have been snapped up by foreign rivals. *BusinessWeek* included Phelps Dodge in a 1984 cover story called "The Death of Mining" that featured an ingot with handles on it made to look like a coffin. It was an era Whisler remembers well.

Then a young lawyer at the company's head office, he spent six months in 1983 filling in for striking workers at the massive Morenci mine, about 50 miles northeast of Safford. Whisler drove a dump truck, changed tires, and pulled copper sheets from the smelter. Ultimately, the mine workers voted the union out. "We spent a long time trying to educate employees that copper prices were low, we were losing money, and had to do some different things," Whisler says.

Those different things include deploying new technology. In the 1980s, Phelps Dodge began to replace many of the smoke-belching smelters long used to refine copper with a leaching process that uses chemicals to extract minerals from ore. Whisler is investing $210 million in a new leaching facility at Morenci. By first pulverizing rock to the consistency of sand, the process will allow Phelps Dodge to obtain copper from ore it otherwise couldn't have, extending the life of the 125-year-old mine. The process came out of the company's 130-person technology unit, based in Safford. "We're just trying to make a buck in the muck," says the unit's general manager, Rick Gilbert.

Whisler is also directing capital to plant expansion. He's in the middle of an $850 million addition to a mine in Peru that will triple production there, to 600 million pounds per year by the middle of 2007. By 2008's second half, Whisler hopes to have the $550 million Safford mine up and running.

Getting approval for a new mine took 12 years of persistence

Getting approvals from state and federal authorities for the new mine took 12 years of persistence and paperwork. The project's manager, Steven Holmes, followed in the footsteps of his now-deceased father, who tried to develop an underground mine in the hills above Safford in the mid-1970s.

The current mine deal involved a controversial land swap with the Bureau of Land Management that environmentalists and a local Apache tribe protested as fraught with ecological risk and a bad deal for the government. In combination with the Peruvian project, the Safford mine should help lift the company's annual copper production by 20%, to 3 billion pounds by 2010.

And therein lies a debate over copper prices and Phelps Dodge's future. Copper bulls argue that continuing demand from construction markets around the world, coupled with the difficulties producers have had adding new supply, should keep prices high or rising for years to come. In 2003, China overtook the U.S. as the world's largest copper consumer.

But copper demand isn't as strong as prices suggest. Last year worldwide usage actually fell 1.5%, according to the International Copper Study Group, a research organization sponsored by copper-producing countries. Robust growth in China, India, and Russia did not offset declining demand in the U.S., Japan, and Europe. On the New York Mercantile Exchange, copper trades at $2 per pound for delivery in February of 2008, high by historical standards but below today's price.

Whisler is thus in the awkward position of cheerleading for his chief product while also trying to temper expectations. He has spoken about a "second copper age," one in which more of the world's 4 billion people lacking plumbing and electrical connections gain access to such copper-dependent services. At the same time, he's cautious. "There's a fair amount of financial money in commodities today," he says. "Is that creating some froth? Yes. How much, I don't think anybody knows."

Can Whisler manage to please both Safford and New York? It's a delicate balancing act for a CEO, even in a boom. ■

Innovation: The View from the Top

IBM's honcho on what CEOs can do to lay the groundwork for real breakthroughs

IBM CONDUCTS A SURVEY OF CEOs and government leaders every two years to find out what's high on their agendas. This year's topic: innovation. Some results were surprising. Business-model innovation scored high, especially at top-performing companies. And execs now see collaboration with other companies—even rivals—as indispensable. Senior Writer Steve Hamm interviewed IBM Chairman Samuel J. Palmisano about the findings. Here's an edited version of their conversation.

Innovation is a hot button for chief executives. What's driving that?

CEOs and business leaders around the world see increased competitiveness, and they see challenges in their business models going forward. They see many things commoditizing. They see that all roads lead to innovation. With the Internet and the proliferation of semiconductors, you'll end up with trillions of things connected—not just individuals but cars, roads, homes, appliances, health-care data, and pacemakers. All of these things are available today that weren't available in the past.

In a way, everybody needs the challenge or the threat to get them going. The threat is that all these competitors are coming online that have global capabilities. They're all enabled by these technologies. The opportunity is to take advantage of the fact that we have low-cost transistors, RFID [radio frequency identification] tags, and supercomputing that is inexpensive and pervasive. All of a sudden, this infinite computing capacity is available, and it's economically affordable to solve many of the world's more complex problems. So my colleagues, other CEOs, look at this thing and say, "You know, geez, the opportunities are everywhere. So how do I take advantage of it?"

PALMISANO "Everybody needs...the threat to get them going"

JEFF GEISSLER/BLOOMBERG NEWS

Your survey found that business-model innovation has become a focus for CEOs.

People realize that you need to do innovative products. You need to have your products differentiated. But with product innovation, it's a certainty that your competition is shortly going to copy what you've done. There was just an announcement that Samsung has a pretty cool way to listen to music as an alternative to the iPod. There will always be the next hot car and the next great high-definition television. But with all of those things, your competition's going to react to what you've just done. It might take them a year or two, but it's inevitable. They will react.

With business-model innovation, though, if you can come up with a unique way of doing things, it's much tougher to react to. The holy grail of strategic thinking is, how do you come up with a business model that differentiates you and that creates value for your customers, and, by doing that, puts you in a unique position in your industry?

Why is business-model innovation so much harder to achieve than product innovation?

It's because organizations have inherent resistance to change. Look at [how long it has taken] IBM. Years ago we talked about remixing our product portfolio. We talked about moving to the high-value innovator spaces in technology and services because there's more profit-margin opportunity. Now, the profit of our portfolio is mixed a third, a third, a third—services, software, and systems and technology.

The next step to drive productivity is we're going to globalize IBM. We're flattening our structure and having collaboration hubs established around the world, and rebalancing all those resources. That's 330,000 people.

There's a lot of inherent resistance to this shift and this change. With many companies, what makes it hard to do is not necessarily setting the strategy but executing it. That's where it requires strong leadership from the CEOs as well as collaboration with groups outside of your own organization. You need to collaborate because the collaboration is so important to learning.

Is collaboration with business partners a key part of business-model innovation?

Our point of view is simple: In today's environment, with all the global opportunities that exist and these new technologies, the best way to make them unique for your own enterprise is to foster collaboration. You can do that in multiple dimensions. You can collaborate within your own organization. We can be multicultural and diverse in IBM because we happen to be in 173 countries around the world. So, by definition, there's a lot we can do amongst ourselves to collaborate with different views of opportunity or technology within our diverse population.

In addition, you need to collaborate between companies and governments and educational institutions. I think that the breakthrough that we got done in the Cell processor, which is based on our Power

"AUSTRALIA HAS BEEN AN INTEGRAL PART OF KELLOGG'S GLOBAL OPERATIONS SINCE 1924 AND PROVIDES THE RIGHT BUSINESS CLIMATE TO DELIVER STRONG, DEPENDABLE GROWTH.

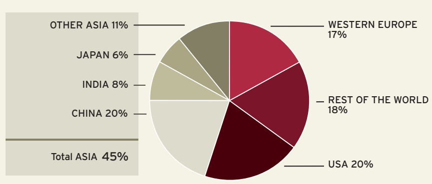
AUSTRALIA IS CHARACTERISED BY A HIGHLY-SKILLED, MULTICULTURAL WORKFORCE, A VIBRANT ECONOMY AND A COMMITMENT TO SUSTAINABLE INDUSTRY GROWTH AND DEVELOPMENT."

A.D. DAVID MACKAY, PRESIDENT AND CHIEF OPERATING OFFICER, KELLOGG COMPANY

Australia | the place to grow your business in the world's fastest growing region

The Asia-Pacific is fast becoming the engine room of world economic growth. In the next ten years, it is forecast that Asia's economies will account for 45%[1] of world GDP (GDP based on purchasing power parity), significantly more than the United States and Europe combined.

SHARE OF WORLD GDP[1] IN 2015



With its strong business and cultural links with Asia, and with a time zone that straddles the Asian, European and US business days, Australia is ideally placed to provide the skills, resources and high quality services to meet Asia's development needs. Australia's top four merchandise trading partners are Japan, China, Korea and the United States[2].

While Australia is well known for its commodity exports, services account for almost 80% of economic activity[2]. Over the five years to end 2004, Australia's services exports to China almost quadrupled, while services exports to India and Korea increased by 131 and 86 per cent respectively[2].

No country in the Asia-Pacific region can match Australia's range of multilingual skills, and its education system is ranked in the world's top four in meeting the needs of a competitive economy[3]. Our workforce is also ranked first in the Asia-Pacific for overall productivity per person employed[3].

Australia's regulatory environment is business friendly. Of the 30 OECD countries, Australia is ranked as having the fewest restrictions on product markets and the least restrictive impact of regulation on economic behaviour.

So, with Australia still ranked the world's most resilient economy, your investment decision could not be simpler. The future is here – in Australia

Well known for its great-tasting, high-quality foods since 1906, **Kellogg Company** is the world's leading producer of cereal and a leading producer of convenience foods.

Kellogg Company enjoys projected annual sales of more than US$10 billion with products manufactured in 17 countries and marketed in more than 180 countries around the world.

The Australian operation was the first Kellogg facility to be established outside of North America with Australian production commencing in 1924. Realising the market potential, Kellogg increased its investment in Australia, building a new plant in Sydney in 1928. This facility's port-side location provides Kellogg with easy trade access to the booming Asia-Pacific region.

Kellogg Australia continues to invest in its Sydney plant and has acquired another manufacturing facility. This expansion has been undertaken to meet the needs of the growing domestic cereal market, snack food industry, as well as catering for the demands of export success.

AUSTRALIA | AT A GLANCE

- Most resilient economy in the world for the fourth year in succession (IMD WCY 2005)
- Lowest risk of political instability in the Asia-Pacific (IMD WCY 2005)
- Experienced a 90% increase in the stock of foreign direct investment over the last five years to a record US$211b in December 2005 (ABS 2006)
- 15 years of continuous expansion with forecast growth of 3.2% in 2006 compared to the OECD average of 2.9% (OECD 2006)
- One of the lowest cost business destinations in the developed world (KPMG 2004)
- Fastest place in the world to start a business (World Bank 2005)
- Ranked second in the Asia-Pacific for patent and copyright enforcement (IMD WCY 2005)

[1] Consensus Economics; IMF: economics @ ANZ **[2]** Australian Bureau of Statistics 2005 **[3]** IMD World Competitiveness Yearbook 2005

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Australian Government
Invest Australia

architecture, would not have happened if we hadn't designed chips for Sony, Toshiba, Microsoft, and Nintendo. Now, clearly, some of these folks are easy to collaborate with because they aren't in our space—Sony or Nintendo. But the other two are clearly competitors of IBM—Toshiba and Microsoft. Yet at the end of the day, it was through these collaborations that we were able to get through this incredible breakthrough. Now we're applying that breakthrough to all sorts of places, whether it's high-definition television, consumer electronics in the home, high-definition radar systems, or medical imaging.

We also started collaborating with communities of experts. It started with Linux and the open-source community, where we all come together and share in some of these areas of technology and standards.

Another thing that you found in your survey is that the CEOs feel they have to personally lead the innovation campaign.

With product innovation, if you stand up on your soapbox and you cheer a little bit, that will certainly help. But the reason I think that the CEOs have to lead this is because, fundamentally, the biggest breakthroughs are a result of changing the business model and the processes and the culture. When you say the new strategy is going to be to change the business model, every CEO understands that's their job. When you talk about driving culture or management systems to change your culture, my colleagues all understand that's their job. So CEOs realize that they have to get these new types of innovation done through their own leadership.

We all do it in different ways. Go back even 10 years ago. Was it natural for IBM to go collaborate around the future of innovation or the future of our technologies? Was it natural for us to open up to the world the things we solved technically as we were inventing things to get feedback on where that was going? Was it natural for IBM to join into the open-source community to talk about standards around lots of technologies? These weren't natural things to occur. The CEO has to give permission to the organization to have it happen. If the CEO doesn't give people permission to go change behavior and to collaborate, then it's not going to happen. Everybody is looking for the signal. They want to know whether things are really changing fundamentally. ■

MICHELLE CHANG

A Big Push for the Very Small Screen

Putting broadcast TV on cell phones could make Qualcomm a media power

BY RONALD GROVER

Paul E. Jacobs is definitely not made from the TV executive mold. The 43-year-old CEO of Qualcomm Inc. has a PhD in electrical engineering and made his mark at the cell-phone chipmaker by writing software code to compress speech. But these days Jacobs is sure talking like a TV guy, chatting about 15-second commercials and consumers' viewing tastes with the gusto of a media mogul. "The cell phone is the TV of the future," he says. "And the future isn't that far off."

Real media moguls have no reason to worry—yet. San Diego-based Qualcomm and its \$5.7 billion-a-year collection of patents and licenses won't be taking on CBS anytime soon. But as every tech company from Apple Computer Inc. to Google Inc. maneuvers to make money by showcasing video, Jacobs is in a race to make the cell phone your TV on the go. Later in the year, Qualcomm plans to offer the cell-phone industry's first broadcast TV service. Called MediaFLO, it is expected to include 20 channels of near-TV-quality programs, 10 music channels, and the cell-phone equivalent of a TiVo in your palm, with the ability to store programming in the memory of your phone to be played back later. "It's the ultimate in giving consumers TV when and where [they] want it, and that has become crucial," says Joseph Rizzo, U.S. tech-sector chief at PricewaterhouseCoopers. MediaFLO plans to sell the service to cell-phone providers for a cut of subscriptions, similar to the way TV programmers negotiate distribution on cable and satellite. (Its only deal so far is with Verizon Wireless.)

NEXT-GENERATION NETWORKS

THE PAYOFF COULD BE huge. Within four years, as many as 26 million cell-phone users could be spending $3 billion a year on video subscription services, figures technology researcher IDC. With a potential market that vast, it's no surprise Qualcomm is facing growing competition. It's already in a race with phone services that offer their own versions of video on the go. What's more, a consortium that includes phonemaker Nokia, chip giant Intel, Microsoft, and Texas Instruments plans to offer a rival service, Modeo, later this year based on technology being tested in several European markets.

Making TV programming available on cell phones isn't a new notion, of course. But interest so far has been scant, in part because rather than actually broadcasting, current efforts involve downloading shows and sports from servers, forcing consumers to wait for pictures that can be fuzzy and intermittent. The leading service, MobiTV, has 500,000 subscribers who pay $9.99 a month to watch clips and programs from 20-odd channels, including Fox Sports, Discovery, and MSNBC. Qualcomm and the next generation of TV networks intend to make the picture better, deploying the same broadcast towers and discarded analog spectrums used by the broadcasters. The result: a TV-like experience, with sharper pictures and live video, all on a two-inch screen.

For Qualcomm, the MediaFLO network is a bold departure from its start in silicon and software. Three years ago, as TV companies were being pushed by the federal government to trade their analog spectrum for new digital signals, Qualcomm paid about $87 million for the nationwide rights to the slice of the UHF spectrum that had been reserved for channel 55. With plans to spend up to $800 million, Qualcomm devised compression technology to jam channels into that spectrum. It is also providing 800 minutes of short programs stored in the memory of cell phones that can be replayed later. "We're very geeky around here, so we wanted to make this the very best we could," says Peggy L. Johnson, president of Qualcomm Internet Services.

But the competition is pushing ahead with technology, too. Modeo will use the existing broadcast towers owned by Crown Castle International, which controls more than 10,000 U.S. sites. Taking over spectrum once used by weather-balloon operators, Modeo has tested its service in Pittsburgh and plans an initial rollout in the top 30 U.S. markets, says Modeo President Michael Schueppert. Qualcomm says only that it will launch initially in half of Verizon's markets. Verizon declined to comment.

MediaFLO, a separate unit of Qualcomm, is becoming a sort of mini media company. It has hired TV producers from New York and Los Angeles to create original programming and has started talking to advertisers about "aggregating eyeballs." Gina Lombardi, president of MediaFLO USA Inc., says the company is ironing out distribution deals with programmers. These are believed to include NBC, MTV, and ESPN. Neither she nor the rumored partners would comment further.

There are huge hurdles to entering a business as entrenched as entertainment. TV networks, worried about how their local affiliates would react to the competition, have yet to sign on. And there is no agreement yet that would outline how to share ad revenues with the phone services, says Lombardi. That is making some phone outfits nervous. "It is a proprietary system, and that gives us pause," says Paul Reddick, Sprint's vice-president for business development.

Then there's the larger question of whether folks will even want to watch a palm-size TV. A spate of recent studies shows that consumers want their phones mostly to make calls (box). Jacobs blames the lack of interest on less-than-great experiences with handheld TV. So he knows the pressure is on to deliver. "If we don't do this right," Jacobs frets, "there won't be TV on cell phones for two generations."

TV in Your Pocket

Video and broadcast TV on cell phones are about to explode. A few market projections:

26 MILLION
Number of subscribers to mobile-video services by 2009

$3 BILLION
Revenues generated by mobile-video subscriptions by 2009

$1.26 BILLION
Spending on cell-phone ads in 2009

Data: IDC, Ovum

ADVERTISING

Call It a Sell Phone

Cell-phone users may balk at receiving video and advertising on their handsets, but advertisers are ready to spend.

Even if 71% of people surveyed last month by market researcher RBC Capital Markets Corp. say they don't want video and ads on their cell phones, advertisers are undeterred. Nearly 90% of major consumer brand marketers in a separate survey say they plan to market their wares via cell phones anyway, according to Airwide Solutions Inc., which advises mobile carriers. Revenue from mobile advertising is expected to hit about $1.3 billion by 2009, up from $50 million in 2005, projects telecommunications research firm Ovum.

Consumers reject the idea of video and ads on phones, say media experts, because they assume it will replicate the Net, where they already feel assaulted by pop-ups and adware. A promising model, though, suggests Rishad Tobaccowala, chief innovation officer at ad outfit Publicis Groupe, is using the cell phone as an "opt-in" ad device. Carriers, he says, would be smart to "incentivize consumers to accept ads relevant to them." One obvious carrot: offer credits to decrease a user's cell-phone bill.

It's not that people hate advertising. They just hate ads that are irrelevant to them. Make it worthwhile, and the cell phone might just become as useful a tool to consumers as TiVo.

–David Kiley

KWATINETZ At first, "Our mistake was doing what everyone else was doing"

West Coast VCs, East Coast Rules

Azure's Wall Street refugees rely on in-depth research—and it's paying off

BY PETER BURROWS

EVEN WITHIN THE CHUMMY world of Silicon Valley venture capitalists, many people haven't heard of Azure Capital Partners. To the extent they have, it's usually because of the San Francisco firm's ties to one of Silicon Valley's infamous characters. Azure's four founders all rose to prominence while working for Frank Quattrone, the former Credit Suisse First Boston rainmaker whose conviction for obstruction of justice was overturned on Mar. 20. (None of the founders was implicated in the investigation.)

Now Azure looks poised to make a name for itself for more positive reasons. After a couple of hits in recent years, it has at least four companies in its stable of investments that could be headed for big paydays in the next year. They include software developer Zend Technologies Ltd., which has been in talks to be acquired by software giant Oracle Corp., and Calix Networks Inc., which could be headed for an initial public offering. Fast-growing Calix, with more than $100 million in revenues, makes gear for telecom companies that want to offer TV and other services. "This will be a scorching IPO," says analyst Sam Wilson of JMP Securities LLC.

Azure isn't your typical venture firm. Rather than depending on partners' gut instincts, it relies heavily on the hard-core research its partners learned on Wall Street. Their approach is to conduct in-depth studies, often taking a year or more, to investigate investment possibilities. That has led Azure to place many of its bets on little-known companies in out-of-favor markets. "They are the quants of the VC world," says Carl Russo, chief executive at Calix. "They're either creating a very different model for a venture firm, or there will be a huge waste of money. Azure won't be run-of-the-mill."

It wasn't always that way. Azure was founded in April, 2000, by First Boston investment bankers Paul Ferris and Cameron Lester, as well as research analysts Michael Kwatinetz and Paul Weinstein. They easily raised $530 million and poured much of it into 20 startups, including some high-profile outfits with sky-high valuations. When the Net collapse came, they got pounded. "Our mistake was doing what everyone else was doing," says Kwatinetz.

The partners quickly changed tactics. They made their own research central to their investment strategy, focused on early-stage deals, and put in money only if they could get at least a 25% stake and a seat on the board. They also slowed down, making only four to six deals a year, vs. the 20-deal pace of the first year.

The approach led them to invest early in several promising tech areas. In 2001 they began doing research into open-source software, including interviews with 50 companies in the sector. The result was three investments in 2002, when few investors saw the potential in giving software away for free. The sector is red-hot today. Zend is likely to fetch $200 million if it's acquired by Oracle or another company. "By doing proactive primary research, it builds your confidence to make counterintuitive bets," Weinstein says.

What are the promising sectors now? Azure is betting on the ecosystem of companies that work with Microsoft Corp., shunned in recent years because of the giant's slow growth. Azure did some research and decided to take a stake in SourceCode Technology Holdings Inc., with less than $1 million in revenues. Now the company is on track to pass $50 million in sales this year, making it a strong IPO candidate.

Azure saw the potential in open source early on

The Azure method isn't about to supplant the traditional approach of VC leaders such as Kleiner Perkins Caufield & Byers. But for now the Wall Street refugees at Azure are convinced there is room for their brand of investing. "Back in the 1990s, it was all about time to market, and getting eyeballs," says Ferris. "Now, it's more about finding an economic basis for success—and that's only going to get more important." ▮

—With Justin Hibbard

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THE BUSINESSWEEK 50

Full rankings of all S&P 500 companies at BusinessWeek.com/BW50

BusinessWeek online

Making the Grade

Perennial Highflier: How UnitedHealth Group, a five-time BW50 company and No. 4 on our list this year, has managed to generate earnings gains topping 20% year after year. **www.businessweek.com/BW50**

The Story Behind the Story: For a podcast interview with Atlanta Bureau Chief Dean Foust by Executive Editor John A. Byrne, go to **www.businessweek.com/search/podcasting.htm**

The BEST Perfor

2006 With oil prices high, energy's strong showing in this year's rankings is no surprise. But a closer look finds a host of companies that have scored big by building intense customer loyalty.

BY DEAN FOUST

THE LAST PLACE YOU MIGHT EXPECT to find creativity would be the corner drugstore. But just take a look at CVS Corp. First, it focused on the pharmacy, creating a sophisticated system that allows customers to phone in, and then pick up, prescriptions at preset times. And after an exhaustive survey of shoppers, the chain, based in Woonsocket, R.I., embarked on a sweeping makeover of the rest of its 5,400 stores, focusing on its core female shoppers. Shelves that previously stood six to seven feet high were lowered to five feet, putting every item within view of the average woman (who, CVS found, is 5 feet 4 inches tall). Stores were repainted in vivid designer colors.

Not least, CVS made a major upgrade of its beauty sections. It hired several hundred beauty advisers, who help shoppers select just the right shade of foundation and then recommend other cosmetics. And the company added exclusive brands such as hair-care products by Beverly Hills stylist Christophe as well as Lumene, a Finnish skin-care and cosmetics brand that is the top-selling beauty line in Europe. The new ranges "have created energy and momentum for us," says Helena Foulkes, CVS's senior vice-president for marketing and advertising. "Our beauty business is outperforming our overall store." The innovations have paid off for CVS. Same-store sales rose 6.5% last year, helping fuel an overall 33% increase in earnings. Investors are raving as well, with CVS shares up 132% over the past three years—a performance that helped earn CVS the No. 39 slot in this year's BusinessWeek 50, our 10th annual effort to identify the best-performing companies in Standard & Poor's 500-stock index.

Some powerful economic and demographic forces favored certain sectors this year. With oil at $60 a barrel, energy-related companies are at the fore. Among them are a number of service providers, including Baker Hughes (No. 21), National Oilwell Varco (No. 27), and Weatherford International (No. 36). That's further evidence for investors that the biggest winners aren't always the companies digging for gold but sometimes the companies selling the picks and shovels. And the list was populated, once again, with a number of health-care companies, including Amgen (No. 9) and Aetna (No. 10), a reflection of the aging of baby boomers.

Pull out energy and health care, however, and you'll find a lot of successful companies on this year's BW50 that, like CVS,

mers

earned their stripes the hard way, by thriving in industries where stiff competition and cutthroat pricing have wiped out lesser companies. These companies have used innovation—be it through technology, or clever design and marketing—to win the hearts and wallets of consumers. And with more and more businesses seeing their competitive edge whittled away by the Internet and globalization, experts say it's imperative for companies always to look for new ways to build, and then maintain, intense customer loyalty.

Competitive Advantage

THE BEST EXAMPLE MAY BE this year's No. 1 company, Apple Computer Inc., which has used catchy TV ads as well as cutting-edge technology to stay ahead of competitors selling MP3 devices, most recently with the video capabilities of its newer iPods (page 68). Ditto for 24th-ranked Starbucks Corp., which is staying a step ahead of other coffee shops by creating new drinks such as current fave Marble Mocha Macchiato as well as producing music compilations aimed at baby boomers, all of which give its customers new reasons to keep coming back.

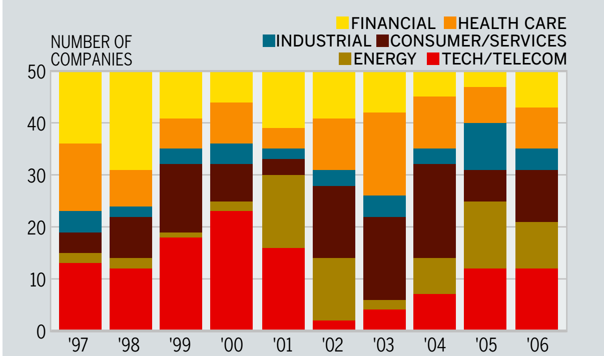
Staples Inc. (No. 44) turned a perpetual source of customers'

1	Apple Computer
2	WellPoint
3	Caremark Rx
4	UnitedHealth Group
5	Schlumberger
6	Occidental Petroleum
7	Halliburton
8	Qualcomm
9	Amgen
10	Aetna
11	Lowe's
12	Burlington Northern Santa Fe
13	Motorola
14	Yahoo!
15	Goldman Sachs Group
16	Lehman Brothers Holdings
17	Gilead Sciences
18	Jabil Circuit
19	Best Buy
20	EMC
21	Baker Hughes
22	Texas Instruments
23	Cisco Systems
24	Starbucks
25	Intel
26	D.R. Horton
27	National Oilwell Varco
28	JPMorgan Chase
29	Merrill Lynch
30	Valero Energy
31	ConocoPhillips
32	Marathon Oil
33	Prudential Financial
34	Microsoft
35	Freeport-McMoRan Copper & Gold
36	Weatherford International
37	eBay
38	Coventry Health Care
39	CVS
40	FedEx
41	Franklin Resources
42	Lennar
43	Coach
44	Staples
45	NVIDIA
46	Norfolk Southern
47	Caterpillar
48	McKesson
49	Hartford Financial Services Grp.
50	Home Depot

Data: Standard & Poor's Compustat

annoyance—the rebate process that many have grown to distrust—into a competitive advantage. By allowing shoppers simply to file for a rebate at its Web site without photocopying receipts or cutting UPC codes off boxes, Staples has earned the trust and loyalty of millions. Staples says its research showed that 80% of customers found its online rebate process "extremely easy" and—most important—are more likely to seek out Staples for their future needs. "We think the marketing of rebates is a significant positive in terms of brand loyalty and sales," says James F. Sherlock, director of sales and merchandising for Staples. So far, eight million customers have claimed their rebates electronically, and Staples is working to enhance the program further. By early next year it hopes to give customers a choice of a rebate check, direct deposit into their bank account, or the ability to convert the funds into an immediate purchase at Staples.

EVOLUTION The 50 through the years



Data: Standard & Poor's

Several companies have made their mark by providing better service. Adrian Slywotzky, a vice-president at Mercer Management Consulting, notes that Lowe's (No. 11) and Best Buy (No. 19) have both put a premium on offering more service than their better-known rivals, Home Depot and Wal-Mart Stores, respectively. Lowe's, for instance, has designed its stores to appeal to women, with wider aisles that make it easier for moms to navigate a stroller or shopping cart and better lighting. Lowe's also uses a higher proportion of full-time workers, who tend to be more knowledgeable, than Home Depot. Best Buy has managed to steal away from Wal-Mart popular brands, such as Samsung Group, that prefer their goods to be displayed in Best Buy's bright and lively stores. "This proves that smaller players who create a different value proposition that emphasizes service can compete with the big boys," says Slywotzky.

Marketing savvy may make for profitable businesses, but, alas, it doesn't always produce big returns for investors. While 32 of the 50 companies that made last year's roster generated positive

CHART BY RAY VELLA/BW

THE BEST AND WORST OF THE S&P 500 COMPANIES

EARNINGS Best earnings growth and biggest losses in the S&P 500

TOP TEN (ONE-YEAR)	PERCENT CHANGE	TOP TEN (THREE-YEAR)	PERCENT CHANGE	BOTTOM TEN (ONE-YEAR LOSS)	MILLIONS OF DOLLARS
TXU	2091%	Phelps Dodge	835.5%	General Motors	–$8,445.0
CA	1970	Transocean	523.6	CBS	–8,321.8
Allegheny Technologies	1727	Avaya	496.6	Unisys	–1,731.9
Rowan	693	Robert Half Intl.	457.6	Eastman Kodak	–1,455.0
Biogen Idec	541	Apple Computer	318.7	XL Capital	–1,252.0
Halliburton	512	Monster Worldwide	315.1	Sanmina-SCI	–1,010.5
Agilent Technologies	511	Valero Energy	234.5	Dynegy	–803.0
Genzyme	410	Devon Energy	230.3	Qwest Communications	–757.0
Newell Rubbermaid	405	Monsanto	221.9	El Paso	–693.0
Freeport-McMoRan C & G	392	Symbol Technologies	212.6	Tenet Healthcare	–621.0

TOTAL RETURNS The best and worst in shareholder returns among the S&P 500

TOP TEN (ONE-YEAR)	PERCENT CHANGE	BOTTOM TEN (ONE-YEAR)	PERCENT CHANGE	TOP TEN (THREE-YEAR)	PERCENT CHANGE	BOTTOM TEN (THREE-YEAR)	PERCENT CHANGE
Express Scripts	131.8%	Gateway	–49.8%	Allegheny Technologies	1673.4%	Tenet Healthcare	–56.6%
Advanced Micro Devices	121.6	Lexmark International	–41.2	Apple Computer	812.6	New York Times	–36.1
Corning	112.8	General Motors	–39.2	Advanced Micro Devices	604.4	General Motors	–29.2
Broadcom	109.8	Symbol Technologies	–34.3	TXU	603.4	Tribune	–28.8
Allegheny Technologies	107.3	Ford	–34.2	E*Trade Financial	509.0	Unisys	–27.9
Tellabs	106.9	RadioShack	–33.1	Allegheny Energy	497.0	Ciena	–25.8
Ciena	103.0	Apollo Group	–32.9	Williams	479.4	Lexmark International	–24.5
E*Trade Financial	92.8	Avon Products	–31.1	Valero Energy	463.8	Maytag	–22.3
Allegheny Energy	88.9	Sanmina-SCI	–29.9	Monster Worldwide	456.6	Merck	–21.5
Office Depot	85.4	Tenet Healthcare	–27.7	Circuit City Stores	453.9	Fifth Third Bancorp	–20.9

Data: Standard & Poor's Compustat, Thomson First Call returns over the ensuing 12 months, the group as a whole failed to beat two of the major indexes. The BW50 stocks earned an 8.2% return in the year through Mar. 14, 2006. That's better than the 5.5% total return for the Dow Jones industrial average, but below the 9.4% gain of the S&P 500 and the 12.7% earned by the NASDAQ Composite index.

That's no big surprise. The BW50 has a growth and momentum bias. It tends to shine during years when the market is rising quickly—and performs less well in grinding markets. And last year's class was held back by the tech sector, with Electronic Arts, Dell Computer, and Symantec all suffering losses of 20% or greater. But as the saying goes, it's not a stock market, but a market of stocks, and there are plenty of ways to mine the BW50 for investment ideas (page 78).

Tech isn't as dominant this year, and given the diversity of this year's list, we've selected a cross section of companies to profile: Apple, which built on the popularity of the iPod to become this year's star performer; FedEx, which has ridden the manufacturing boom in China better than any delivery company; two standout homebuilders, Lennar and D.R. Horton; Goldman Sachs, which continues to spin profits out of its proprietary trading; and Schlumberger, whose heavy investments in R&D and technology made it a standout in the energy-services field. What they all have in common is that they have developed products and services that are distinct from the rest of the herd. In addition, we've included brief snapshots of each of the BW50 companies. And we round out this year's coverage with statistical tables that provide performance rankings for the BW50. The full ratings for the S&P 500 appear on BusinessWeek Online. Read on.

–With William C. Symonds in Boston, Brian Grow in Atlanta, and Fred Katzenberg in New York

METHODOLOGY How we measured the top 50

ONE OF THE BUSINESSWEEK 50'S MAIN GOALS is to capture the dynamic nature of strong growth. That's reflected in how we identify the best of the Standard & Poor's 500-stock index. We use 10 performance metrics, starting with sales and earnings growth. We tally both for the most recent 12-month and three-year periods, to reward companies that prosper over time. This year, for the first time, we include long-term earnings prospects. We factor in net profit margins. And finally we account for the market's view, by measuring total shareholder returns for one- and three-year periods.

We weight the results for sales volume, because it's harder for large companies to post impressive revenue- and profit-growth figures. And we factor in the debt-to-capital ratio, to recognize clean balance sheets. That also makes it harder for corporations to qualify with growth that's primarily the result of debt-laden acquisitions.

SALES GROWTH The best and worst in sales performance among the S&P 500

TOP TEN (ONE-YEAR)	PERCENT CHANGE	BOTTOM TEN (ONE-YEAR)	PERCENT CHANGE	TOP TEN (THREE-YEAR)	PERCENT CHANGE	BOTTOM TEN (THREE-YEAR)	PERCENT CHANGE
WellPoint	117%	OfficeMax	–31%	Biogen Idec	92.6%	Dynegy	–28.6%
National Oilwell Varco	100	El Paso	–27	Chesapeake Energy	82.0	CBS	–17.6
Sears Holdings	93	Teradyne	–24	Yahoo!	80.6	El Paso	–16.6
North Fork Bancorp.	91	Duke Energy	–19	Caremark Rx	78.3	J.C. Penney	–14.9
XTO Energy	80	American Electric Power	–15	XTO Energy	63.3	Cooper Tire & Rubber	–11.2
Freeport-McMoRan C&G	76	Applied Materials	–14	Gilead Sciences	62.1	Clear Channel Communs.	–9.7
Chesapeake Energy	72	Solectron	–12	eBay	54.9	ConAgra Foods	–9.6
Apple Computer	66	Forest Laboratories	–12	Constellation Energy Group	50.7	CMS Energy	–9.3
EOG Resources	59	Electronic Arts	–10	WellPoint	47.5	Citizens Communications	–7.2
Rowan	57	Sanmina-SCI	–9	EOG Resources	46.8	MeadWestvaco	–6.8

NET MARGIN Best/Worst, S&P 500

TOP TEN (2005)	PERCENT	BOTTOM TEN (2005)	PERCENT
Ambac Financial Group	45.3%	Ciena	–85.0%
ProLogis	42.7	CBS	–57.2
Public Storage	41.2	Dynegy	–34.7
MGIC Investment	41.1	JDS Uniphase	–32.3
Linear Technology	40.3	Unisys	–30.1
Gilead Sciences	40.1	El Paso	–17.3
QUALCOMM	37.4	XL Capital	–11.2
Yahoo	36.1	Eastman Kodak	–10.2
Burlington Resources	35.7	Sanmina-SCI	–8.9
Apache	35.2	Tenet Healthcare	–6.5

LONG-TERM EARNINGS GROWTH Best/Worst, S&P 500

TOP TEN (2005)	EST. GROWTH RATE	BOTTOM TEN (2005)	EST. GROWTH RATE
Nabors Industries	59.5%	Citizens Communications	1.0%
Newmont Mining	50.0	United States Steel	2.0
Transocean	50.0	Qwest Communications	2.0
Noble	43.0	CenturyTel	2.5
Rowan	33.0	Merck	2.7
Yahoo!	25.7	Verizon Communications	3.0
Jabil Circuit	25.0	American Electric Power	3.0
National Oilwell Varco	25.0	Equity Residential	3.0
eBay	25.0	Consolidated Edison	3.5
Weatherford Intl.	25.0	Progress Energy	3.5

Data: Standard & Poor's Compustat, Thomson First Call

THE BUSINESSWEEK 50

STRATEGIES FOR SUCCESS
APPLE COMPUTER

iPods, Sure. But Don't Go Dissing Macs

BOYS' LIFE Shopping for Apple computers in New York's SoHo

BY PETER BURROWS

#1 IT'S REMARKABLE THAT APPLE Computer Inc., heading the BusinessWeek 50 list of the best corporate performers, was on the brink not so long ago. "Oh, the company was going bankrupt, all right," recalls ex-board member Edgar S. Woolard Jr. But in mid-1997, Woolard called Steven P. Jobs and asked him to retake the helm of the company Jobs had co-founded in 1976. In short order, Jobs tightened up operations, re-energized Apple's talented troops, and in 2001 oversaw the debut of a magical little device called the iPod.

Those cute gizmos, in their various digital-music-and-video-playing incarnations, have made Apple more powerful than ever, a Wall Street darling that has the early lead in the race to define the world's digital media future. The question of Apple's social and cultural impact was perhaps settled once Jobs was the subject of a *Saturday Night Live* parody (for cranking out iPods so small they're invisible). But the question still dogging investors, who have bid up Apple shares more than 100% since January, 2005, to around $64, is: Can the company keep it up?

The answer will depend not only on successive generations of the iPod but also, to a large degree, on Apple's Macintosh PCs. While the iPod gets most of the headlines, the Mac still brought in 39% of Apple's sales in 2005. And while most analysts think that iPod sales will continue to skyrocket for the next couple of years, they also believe that the music player market will come back to earth at some point. "The Mac will be increasingly important [to Apple's growth] in the last years of the decade," says Needham & Co. analyst Charles Wolf.

The reason is straightforward: On the whole, PCs are much bigger than digital music. Right now, Apple dominates the digital music player market, which is expected to hit $12 billion in 2009, with a share of more than 70%. But Apple has just 5% of the $75 billion home PC market. Each additional point of PC market share that Apple gains would equal roughly $750 million in sales. That's a big chunk for a $16 billion company. Shaw Wu, an analyst at American Technology Research, thinks Mac sales could grow 25% in 2007, vs. 10% for the broader industry. Beginning in 2007, says Wu, "I think the Mac business will out-

grow the iPod business."

Of course, not everyone agrees Apple can make that happen. Indeed, Apple shares have dropped 25% since mid-January on fears that the iPod wasn't lifting Mac sales, and that the "iPod halo effect" hasn't materialized. In fact, as Apple is converting from Macs that use IBM's PowerPC processors to ones with chips made by Intel Corp., its market share gains have stalled. Also contributing to the concerns are some well-publicized hacker attacks on the Mac, which have sullied its pristine reputation as a virus-free alternative to Windows. "I really don't think there has been much of a halo effect," says Roger L. Kay, president of technology consultant Endpoint Technologies Associates Inc. "Most of what they've done is reconvert the faithful."

POTENT CACHET Despite a price that's twice that of its PC rivals, the MacBook Pro has a waiting list

CATRINA GENOVESE

Nevertheless, there are plenty of reasons to expect a Macintosh renaissance. Currently, Apple is struggling to meet demand for its new MacBook Pro laptop despite a $1,900 price tag that is nearly twice that of garden-variety rivals. Apple-watchers expect the company to launch lower-priced MacBooks in coming months to compete for the lion's share of the market. By early next year, Adobe Systems Inc. will have converted its popular graphics and Web publishing software to run at top speed on the new Intel-based Macs, a critical event for Mac power users. "They should regain share in the back half of the year," says Smith Barney Citigroup analyst Richard Gardner.

Opening New Windows

APPLE HAS SOME WILD CARDS it can play to goose the Mac's market share, as well. While Apple won't comment, Needham's Wolf believes that the Intel-based Macs will be able to run Windows programs right along with Mac titles by yearend. That could entice hordes of disgruntled PC owners to give the Mac a shot, secure in the knowledge that they can continue using familiar programs. This prospect seems to resonate among younger buyers, where Apple's resurgence has been most pronounced. Earlier this year, Wolf surveyed 255 college students, and the number of Windows-compatible PC owners who said they would "definitely" buy a Mac if it had this capability jumped from 1.8% to 13.5%.

In the longer term, Apple could still try an oft-debated strategy: licensing its Mac software to other PC makers. Dell Inc. has already expressed an interest in stamping out Mac clones, much as it does with Windows-based PCs today. With more companies hawking Macs, Apple's market share could rise into double digits. "Multiple PC makers have expressed an interest. It's not just Dell," says Kay. Such a scenario could eat into Apple's own hardware sales. But it would boost margins by bringing in a royalty stream that could approach $1 billion per year, guesses Kay.

For the moment, Apple is plenty tied up in its transition to Intel and in creating the next headline-grabbing digital entertainment device. Each week the company is adding content to its online iTunes music and video store, everything from *The Daily Show* episodes to Walt Disney Co.'s *High School Musical,* a full-length movie. As a result, analysts expect more products aimed at the living room. Many also expect the company to unveil an Apple branded cell-phone-cum-iPod by yearend. All those pots on the fire could well help Apple continue to remake our entertainment diets. But if Apple manages to maintain the kind of stellar performance it delivered in 2005, the Mac will be a major reason why. ■

WELL BEING Tech can help the chances of finding big reserves

PIERRE BESSARD/REA

STRATEGIES: SCHLUMBERGER

Free-Flowing Technology

FOCUSED EXPERTISE Schlumberger keeps its lead in the oil patch with far and away the biggest outlays on R&D

BY MARK MORRISON

#5

FOR A COMPANY IN SUCH an old, dirty business as providing oil-field services, Schlumberger Ltd. has made its mark in a decidedly newfangled way. The industry leader has maintained its position for most of its 80 years by being far and away the most technologically advanced player in the game. Maybe it's encoded in the company's DNA: The business started in a Paris office in 1920 based on Conrad Schlumberger's revolutionary idea of using electrical measurements to map subsurface rock bodies.

Today, its menu of services for Big Oil is broader than that of such peers as Halliburton Co. or Baker Hughes Inc. Schlumberger can do everything from sizing up the geology of a site to assisting directional drilling to extract oil, from managing information about reserves and production for super-majors such as Shell Oil Co. to cementing the holes on a completed well. With oil and gas prices at record levels and exploration budgets bulging, Schlumberger's revenues and profits are surging. Demand for its high-margin services has propelled the New York company into the No. 5 spot on the BusinessWeek 50 this year.

Credit is due in large part to Chief Executive Andrew Gould, who upon taking over in early 2003 righted Schlumberger's course after an ill-fated, multibillion-dollar foray in information-technology consulting. Investors have certainly welcomed Gould's sensible retrenchment: The stock price has tripled since his arrival.

Gould, a 30-year company vet who works in Paris, has a simple plan: Exploit Schlumberger's advantages in scale, breadth, and industry-leading technologies. Last year, the company's R&D budget was $506 million—substantially more than any of its competitors, according to brokerage A.G. Edwards Inc. "Schlumberger has the clear leadership position and is very committed to maintaining that," says analyst Poe Fratt. In November the company cut the ribbon on a 53,000-square-foot addition to its Global Drilling Technology Center in Gloucestershire, England, where 270 engineers vet prototype drilling systems before they're deployed to fields around the globe. Schlumberger can drill horizontal wells so far and with such accuracy, Gould recently boasted, "we can hit a target the size of a tennis court from 10 miles away."

With easy-to-find oil scarce, Big Oil companies are looking to expensive and risky exploration projects deeper in the sea, and Schlumberger technology can improve the chances that wells will find substantial oil or gas reserves. That's a big reason revenues jumped 25% in 2005, to $14.3 billion. Late last year, for example, Norsk Hydro ASA, a Norwegian oil-and-gas producer, employed a Schlumberger sonic scanner that uses acoustics to help provide data on oil fields that previous technology wasn't able to yield. Also working for ConocoPhillips in Alaska's North Slope, Schlumberger's PeriScope system helped steer a 6,800-foot horizontal well in a reservoir only eight feet thick.

Many exploration and production companies are also returning to older fields where the high price of oil justifies the use of Schlumberger's well-stimulation and information-management processes. Shell, for one, just signed Schlumberger to a three-year contract to squeeze the last bits of oil left in long-forsaken fields all over Europe. The technology, which improves Shell's ability to read seismic data, makes it possible for Shell to make better decisions about stimulating old wells in places such as Norway, Holland, and Scotland.

To be sure, if oil prices fall from their historical highs, Schlumberger's technology will look less affordable to the energy companies. But Gould has said it'll take "several years" to replace today's tight supplies, many of which have been under exploration since the last up-cycle in the 1970s. Gould's biggest problem nowadays is to find enough qualified engineers and other skilled workers to handle the increased workload. It's inevitable that another downturn will visit the energy sector, but with Gould at the helm, expect Schlumberger to keep doing what it knows best. ■

STRATEGIES: GOLDMAN SACHS

White-Hot, and Streaking Ahead

BY JOSEPH WEBER

#15 GOLDMAN SACHS GROUP INC. HAS BEEN dazzling Wall Street with its take-no-prisoners advance lately. Its investment-banking, trading, and asset-management businesses are all white-hot. Their combined efforts led to a 24% gain in net income, to $5.6 billion in 2005, on a 45% rise in revenues, to $43.4 billion. As the 137-year-old firm blasts past peers, it seems nearly unstoppable.

Firing on all cylinders propelled Goldman to the No. 15 spot on the BusinessWeek 50, a huge leap from its 116th-place perch in our larger Standard & Poor's 500-stock index tally a year ago. Its stock jumped 23% in 2005, to about $128, and has since topped $150. Most analysts remain effusive. "The growth will accelerate this year," says CIBC World Markets' Meredith Whitney, who expects shares to reach $190. "You have a tremendous environment for [making] and for harvesting investments."

Not So Transparent

THE MOST POWERFUL engine at Goldman is one that roars mostly behind the scenes. Its trading and principal investments business, where commodities, fixed-income, and equities traders use proprietary strategies to play the markets, churned out $16.3 billion, or 66% of its revenues net of such expenses as interest. The business has made some savvy investments, taking stakes in U.S. power plants and other energy concerns while demand is hot. Globally, too, Goldman made smart bets: A $1.3 billion stake in Sumitomo Mitsui Financial Group Inc. bought in 2003 is worth more than $4 billion.

Having such a fat slice of its profits come from a business that stays largely mum about how it achieves its gains makes some analysts nervous. Goldman, according to CreditSights Ltd. analyst David H. Hendler, "is a high-performance race car, but we don't know exactly how the engine works." One oft-repeated line on Wall Street: The best way to invest in a hedge fund is to buy Goldman stock.

Goldman's risk profile is going up in part because it's investing more alongside its clients. This year, for example, it paired with clients Allianz and American Express Co. to provide the lion's share of $3.8 billion plowed into the Industrial & Commercial Bank of China. The firm will help the giant Chinese bank upgrade technology and processes and then expects to gain after it goes public in a mammoth initial public offering.

Just how much riskier is Goldman? Its "value at risk," (VAR), a measure of how much money it could lose on any particular trading day, jumped 15%, to $92 million, in the first quarter. Standard & Poor's analyst Robert Hansen argues that as a share of revenues, the amount at risk has declined as the revenues have grown. He's not worried, since net revenue this year should hit $29 billion, up 14%. CreditSights analyst Hendler frets, however, that "what goes up can come down." If market losses add up, he warns, revenues will fall as well. Says Goldman Chief Financial Officer David A. Viniar: "We take risks commensurate with opportunities that we see." The VAR number is the highest it has been, but not the highest it will be, he adds. "As the business grows, we see more opportunities in more places."

NYSE Goldman was in on its Archipelago deal

DANIEL BARRY/BLOOMBERG NEWS

If market bets do turn against it, Goldman has other, albeit smaller, profit engines. It ranked No. 1 last year in mergers, playing advisory roles in 6 of the 10 biggest deals in the world. It helped Procter & Gamble Co. swallow Gillette in a $57.2 billion move; abroad, it midwifed acquisitions such as Gas Natural SDG's $51.2 billion takeover of another Spanish utility, Endesa. In a controversial move, it also advised both sides in the merger between the New York Stock Exchange and Archipelago Holdings. Investment banking revenues hit their highest level in four years, at $3.7 billion. And its asset-management arm weighed in with $4.8 billion in gains.

As Goldman expands, its risks will expand as well. And one of its major areas of expertise is, of course, managing risk. Now, Goldman's greatest challenge may simply be topping its own performance. ■

MATCHMAKER
In 2005, Goldman served as an adviser on 6 of the year's 10 biggest deals

THE BUSINESSWEEK 50

STRATEGIES: HORTON AND LENNAR

More than One Way To Build a Home

BY PETER COY

#26

#42

WALL STREET DISDAINS THEM EQUALLY, but there are real differences between the two homebuilders in this year's BusinessWeek 50. D.R. Horton Inc. (No. 26) of Fort Worth is intensely focused on growth, vowing to double the number of homes it builds by 2010. Lennar Corp. (No. 42) of Miami intends to grow, too, but it's building a cash hoard that would allow it to buy land and smaller builders at fire-sale prices if the opportunity arises. Horton will be a superstar if its growth strategy pans out, while Lennar could come out ahead if there's a downturn.

It's easy to understand why investors stash Horton and Lennar into the same mental filing cabinet. They're both big builders that specialize in starter and first-step-up homes in the Sunbelt, with selling prices averaging about $300,000. By coincidence, even their revenues last fiscal year were twinned: around $14 billion for each, with Lennar edging out Horton. Fearing a housing slump, the market gives them roughly equal price-earnings ratios: around seven times last year's earnings. Only one sector of the Standard & Poor's 500-stock index has a lower trailing p-e: auto makers.

Growth Ethic

DESPITE THEIR SIMILARITIES, the differences between Horton and Lennar are telling. Horton, already No. 1 in homes sold, is aiming for close to 15% annual unit growth. The ethic is bred in the bone at Horton, which has had rising revenues and profits every quarter since it was founded by Chairman Donald Ray Horton in 1978. Donald J. Tomnitz, Horton's CEO, says he's expecting lots of demand from baby boomers, immigrants, and "echo boomers." But even if that demand doesn't materialize, the company aims to grow by grabbing business with aggressive incentives or, as a last resort, price cuts, says analyst Ivy L. Zelman of Credit Suisse Group. Says Zelman: "Horton is being accused by other builders of spiraling down the market." Horton responds that growth won't come at the cost of profitability.

In addition to being growth-hungry, Horton is decentralized. Each of its 77 markets in 26 states is run by a profit-center manager, who decides what to build and where. And crucially for a softer market, it's also probably the lowest-cost producer of entry-level houses, thanks in part to putting the screws to its suppliers, says analyst James F. Wilson of JMP Securities LLC.

Lennar has a more button-down, centralized style. Although it's forecasting 13% unit growth this year, it stresses return on capital over steady growth. In a unique strategy to prevent its homebuilding units from overbuying land to feed construction growth, it has put land acquisition into a separate division that's rewarded for keeping costs low. It reduces capital needs by bringing in joint-venture partners, as it is doing in a huge project planned for the former El Toro Marine Corps Air Station in Irvine, Calif. And its balance sheet is among the cleanest in the industry, with nearly $1 billion in cash and non-financial-services debt at 33% of capital. That's plenty of money for vulture acquisitions in a softening market. A final difference comes in quality: Lennar, along with last year's BW50 member Pulte Homes Inc., scores highly in the annual J.D. Power & Associates New-Home Builder Customer Satisfaction Study. Horton has fared poorly, although Tomnitz says its market success proves customers are happy.

Differences in strategy don't seem to matter much to many investors, who have tarred all builders as risky propositions. That frustrates both of the BW50 homebuilders. Horton executives argue that their track record of steady growth will be unbroken.

BROWSING A Horton model home in Camarillo, Calif.

AXEL KOESTER

BOOMERS VS. BUST Horton is betting on continued demand, while Lennar is well-positioned for a softer market

"Some people accuse us of being cocky, which, if you know us, we're not. We're very conservative people," says Tomnitz. As for Lennar, its executives concede that the market is softening but see opportunities. Says Chief Financial Officer Bruce E. Gross: "If there's a slowdown, there is a unique opportunity to consolidate the industry." Adds Zelman: "The jury's out on which will prove to be the right formula." Take your pick. ■

ON THE MOVE FedEx plans a $150 million superhub in Guangzhou

ZHANG WEI/IMAGINECHINA.COM

STRATEGIES: FEDEX

Taking Off Like 'A Rocket Ship'

BY DEAN FOUST

#40

AS SOON AS MOTION COMPUTING INC. in Austin, Tex., receives an order for one of its $2,200 tablet PCs, workers at a supplier's factory in Kunshan, China, begin assembling the product. When they've finished, they individually box each order and hand them to a driver from FedEx Corp., who trucks it 50 miles to Shanghai, where it's loaded on a jet bound for Anchorage before a series of flights and truck rides finally puts the product into the customer's hands. Elapsed time: as little as five days. Motion's inventory costs? Nada. Zip. Zilch. "We have no inventory tied up in the process anywhere," marvels Scott Eckert, Motion's chief executive. "Frankly, our business is enabled by FedEx."

There are thousands of other Motion Computings that, without FedEx, would be crippled by warehouse and inventory costs. That value proposition has made the Memphis shipping giant an indispensable partner for companies whose products are made in China. In the past two years, the volume of goods that FedEx has shipped over its vast international network has soared 40%, with much of the growth from Asia. FedEx earnings leapt 21% last year, and its stock price has more than doubled since 2003, landing FedEx the No. 40 spot on the BusinessWeek 50. "FedEx has been a rocket ship," says Daniel Ortwerth, analyst at St. Louis brokerage Edward Jones.

That FedEx has become the preferred carrier out of China is no accident. As far back as the 1980s, FedEx founder and CEO Frederick W. Smith predicted that Asia would become an economic powerhouse. In 1989 he shelled out $895 million to buy Tiger International Inc., a struggling cargo hauler that nonetheless had assets Smith coveted: flying rights into most major Asian airports and a management team with a deep knowledge of the Pacific Rim. Wall Street roundly panned the move—many Asian economies were unstable at the time—but it was prescient, giving FedEx a 10-year jump on rivals. "Analysts didn't like it," chuckles Michael Ducker, executive vice-president for international in FedEx' express unit. "But like Wayne Gretzky used to say, we saw the puck and skated toward it."

These days, FedEx operates 120 flights weekly to and from Asia, including 26 out of China alone. As a result, FedEx now controls 39% of the China-to-U.S. air express market, vs. 32% for United Parcel Service Inc. and 27% for DHL International, according to Satish Jindel, president of SJ Consulting Group Inc. in Pittsburgh.

Now Smith is doubling his bets on China. FedEx plans to close its Asian hub in the Philippines by 2008 in favor of a new $150 million superhub in Guangzhou, a city in the heart of one of China's fastest-growing manufacturing districts. Also in 2008, FedEx will take delivery of the first of up to 20 of Airbus' A380 cargo haulers, birds so massive that they hold twice the load of the Boeing MD-11. The A380 can fly nonstop from Asia to FedEx' U.S. hubs. Here again, Smith was ahead of the pack: By being the first American customer, he not only beat UPS to the punch but got to contribute to the configuration of the A380, too. "They played a pivotal role in the design," says Allan McArtor, chairman of Airbus North America Holdings Inc. and a former FedEx executive.

FedEx' ambitions in China may extend beyond exports. In January, it spent $400 million to buy out its 50-50 delivery partner in China, Datian Group. That gives FedEx full control over Datian's truck fleet and its 89 distribution hubs. Some analysts, such as Morgan Stanley's James Valentine, believe that the purchase is a step toward FedEx domestic service between China's largest cities, at least for large business customers. Some wonder, though, if China is ready for that, given the shabby state of its highways. "[FedEx] could run up against infrastructure problems," warns Ortwerth. Smith isn't worried. He's been right about China before. ■

WHAT GREAT WALL? FedEx is the preferred carrier out of China, with flying rights into most Asian airports

THE BUSINESSWEEK 50

INVESTING BY DAVID HENRY

TOP Prospects

ARE THE STOCKS OF THE BusinessWeek 50 as interesting as the companies? In many cases, yes—at least for courageous investors. BW50 company stocks tend to be unusually volatile and richly priced.

Shares of NVIDIA Corp., the factoryless maker of high-performance computer graphics chips, for example, are among the most volatile in the Standard & Poor's 500-stock index. And the price-earnings ratio of the BW50 is 18.6, two points more than the index. Shares of Yahoo! Inc., another BW50 member, recently traded at a massive 60 times expected 2006 earnings, even though the stock had tumbled 20% in the preceding two months.

High valuations and volatility are no surprise among the ranks of the BW50. Many of the companies are well known, widely held, and carry a median market capitalization of $33 billion, nearly three times the median S&P 500 company. Their potential growth attracts a lot of attention. Stock analysts surveyed by Thomson First Call expect earnings per share of the median BW50 company to grow annually the next five years by 15%, vs. 11% for the S&P 500.

THRILL OF THE CHASE The distinguishing characteristics of the BW50 stocks are their volatility and high valuations

Dividends Yielding Clues

STILL, THE BW50 is worth mining for investing ideas. Consider Prudential Financial Inc., the insurance and investment giant. Its stock is moderately volatile and sells at a below-market p-e of 14. Analysts figure earnings will grow 13% annually over the next three to five years. Pru pays a dividend yield of 1% and has enough resources to continue buying back shares even after reducing its share count by a sizable 6% last year.

For investors who abhor stock gyrations, rail carrier Burlington Northern Santa Fe Corp. is worth a closer look. The stock is less volatile than the market as a whole, and the company is raking in cash as it packs its lines with railcars loaded because of the growing economy. It is handing a good chunk of that cash back to investors through dividends and share buybacks. And while Texas Instruments Inc.'s high volatility might put off nervous investors, its earnings per share are expected to grow an exceptional 20% annually over the next three to five years. Better yet, the stock has been selling for a relatively modest 20 times earnings recently.

To find potential winners, we screened the shares of the BW50 in several ways using data from research divisions of Standard & Poor's. First, we pruned the list to 36 by including only those rated four- and five-star buys by S&P's Equity Research Services. Based on S&P's data and analysis, these shares

TIM BOWER

are expected to make money and beat the total return of the market over the next year.

We also sifted the stocks according to their riskiness. Since there's no real way to know the odds that a stock will lose money, we used the next best thing to gauge risk: betas, a standard Wall Street tool. Betas measure how much a stock price changes compared with the market as a whole. If you're looking for stocks that don't jump around more than the market, you want a stock with a beta of 1 or less.

Only 12 of the BW50 stocks met that test, most of those just barely. The betas we used were based on weekly price changes for the past two years as compiled by Capital IQ, an S&P research service for institutional investors, investment bankers, and private equity funds. (Wall Street often uses five-year periods to measure beta, but we shortened the period after finding that the five-year measure classified stocks of energy producers as exceptionally low risk, apparently because they barely budged until the price of oil spiked in 2004.) For moderate risk, we found nine stocks with betas from 1 to 1.2. Then we flagged as higher risks 12 stocks with betas of 1.6 and greater.

PORTFOLIO PICKS
From the BusinessWeek 50

LOWER RISK

COMPANY SYMBOL	PRICE	BETA	SHAREHOLDER PAYOUT %*
Microsoft (MSFT)	26.87	0.90	5.90
Burlington Northern (BNI)	78.64	0.90	2.41
JPMorgan Chase (JPM)	41.14	0.97	5.26

MODERATE RISK

COMPANY SYMBOL	PRICE	BETA	PEG**
Weatherford Intl. (WFT)	43.12	1.09	0.79
Goldman Sachs (GS)	141.29	1.09	0.88
Merrill Lynch (MER)	77.21	1.15	1.06
Halliburton (HAL)	68.00	1.18	1.08
Prudential Financial (PRU)	77.04	1.19	1.07

HIGHER RISK

COMPANY SYMBOL	PRICE	BETA	GROWTH RATE ***
Coach (COH)	35.72	1.70	20.00
Texas Instruments (TXN)	29.85	1.84	20.00
Yahoo! (YHOO)	32.06	1.90	25.65
NVIDIA (NVDA)	47.13	3.14	20.00

* Current dividend yield plus percentage reduction in shares outstanding past four quarters ** Ratio of price-earnings ratio to projected growth rate *** Growth rate in earnings per share projected by stock analysts
Data as of Feb. 28 **Data:** Standard & Poor's Compustat, Capital IQ, Equity Research Services

Sharing the Wealth

AND THEN WE REFINED each list even further. We hunted for stocks with low prices compared with expected earnings. Alas, few companies in the BW50 have the safety margin of a low p-e ratio. So we looked to dividend yields—one of the more reliable components of future returns on stocks—as tallied by S&P's Compustat. Only six BW50 companies yield more than the 1.9% of the S&P 500. A number, however, have been returning a lot of money to shareholders by buying back stock. To winnow out buybacks made by companies just to sop up the shares they issue for employee stock options, we gave companies credit for the percentage by which they actually reduced their numbers of shares outstanding. And then we added that to their dividend yield and came up with what we call shareholder payout. We found 17 of the BW50 with payouts of more than 2%.

We discovered three stocks with low volatility and high payouts worth a further look, including Burlington Northern. Another company, Microsoft Corp., reduced its shares outstanding by 4.5% last year and is yielding 1.4%. Analysts expect earnings to grow 12% annually. The third, banking giant JPMorgan Chase & Co., is yielding 3.3% and trading at a relatively low 12 times expected 2006 earnings.

Investors willing to accept greater stock gyrations have more opportunities. Among the stocks with moderate risk to consider, several now offer the prospect of growth at a reasonable price. Five, including Prudential Financial and Goldman Sachs & Co., traded as of Feb. 28 at price-earnings ratios of less than 1.1 times their expected earnings growth—the so-called p-e to growth, or PEG, ratio. Oilfield service company Weatherford International Ltd. has among the highest earnings-per-share growth forecasts of any of the BW50 at 25%. Another oilfield company, Halliburton Co., is expected to increase earnings 16% annually as demand for energy stays strong around the world.

The most volatile stocks include some with exceptionally high expected growth rates. They may not all be worth the extra risk of owning them, but four have projected earnings per share growth of 20% or more. Chipmaker Texas Instruments has the most going for it. Its price-earnings ratio of 20 is below its historical average and no more than the stock's growth rate. Buybacks cut the company's share count by 7% last year. NVIDIA, too, has a p-e roughly equal to its 20% growth rate. But the stock has run up 115% from April through February, vs. a 20% gain at Texas Instruments in the same period.

The contrast between NVIDIA and Texas Instrument shares shows that quantitative filters can only guide investors so far. Buyers have to look around to flush out the rest of the story. With so many stocks to choose from and so little time, the BW50 is a good place to start.

The Ranking

They're not all in energy and health care. How companies of every stripe soared even in a climate of thin margins and cutthroat competition

APPLE COMPUTER INC.

» ALL THOSE LITTLE white earbuds are a bona fide cultural phenomenon—and serious business for Apple. Booming sales of its iPod music players have propelled the Cupertino (Calif.) icon to the top of our list of the best corporate performers. Apple shows few signs of slowing down. Of the 42 million iPods sold since the line was introduced five years ago, 32 million were sold in 2005, including 14 million in a killer Christmas quarter. Apple's profits leapt 216% in 2005 on a 66% jump in sales. Investors are still bullish, not only for what Steve Jobs has done, but also for what lies ahead. Jobs, soon to be the biggest shareholder in Walt Disney Co. thanks to its recent purchase of his Pixar Animation Studios, has inked landmark deals with TV studios and other Old Media powers. If Apple can extend its portable music dominance into the living room, its remarkable recovery might have far to run.

INDUSTRY
Technology Hardware & Equipment
SALES
$16.2 billion
NET INCOME
$1.6 billion

STEVEN P. JOBS, 51
CEO since 1997

LARRY C. GLASSCOCK, 57
CEO since 1999

WELLPOINT INC.

INDUSTRY
Managed Health Care
SALES
$45.1 billion
NET INCOME
$2.5 billion

2

» WELLPOINT IS proof that there is life after a megamerger. Born in late 2004 of the union of two regional giants based in California and Indiana, Wellpoint is the nation's biggest health insurer, with 34 million members. Last year it snapped up New York-based WellChoice, along with a small Wisconsin health plan. Wellpoint shareholders seem to think bigger is better, bidding up the stock 38% last year. Based in Indianapolis, the company is preparing to sign up as many as 2 million new members under the Medicare drug program in 2006. It is also reaching out to the uninsured with low-priced coverage.

EDWIN M. "MAC" CRAWFORD, 57
CEO since 1998

CAREMARK RX INC.

INDUSTRY
Health-Care Services
SALES
$33.0 billion
NET INCOME
$932 million

3

» IN A PILL-POPPING nation, designing prescription plans and processing pharmacy claims is one lucrative business. Few know better than pharmacy benefits manager Caremark Rx, which helps companies, insurers, and government agencies put together drug coverage for employees. The Nashville company saw strong growth in its business filling prescriptions through the mail. Profits leapt 55%, to $932 million, on sales of $33 billion, up 28%. And Caremark, along with rivals, is poised to cash in again. The Medicare drug benefit is expected to boost spending on drugs by as much as $15 billion.

DR. WILLIAM W. MCGUIRE, 57
CEO since 1991

UNITEDHEALTH GROUP INC.

INDUSTRY
Managed Health Care
SALES
$45.4 billion
NET INCOME
$3.3 billion

4

» UNITEDHEALTH Group already serves an astonishing 65 million Americans with its health plans and other services. Now a push into serving the elderly could make it the biggest provider in Medicare's new prescription program in 2006. Its formula for success over the past 15 years: maintain a diverse mix of businesses, and make smart acquisitions. Even if gains from employer-sponsored plans slow, UnitedHealth's push into faster-growing niches such as discount health-care cards may boost profits. Earnings for the Minnetonka (Minn.) company are expected to jump about $1 billion, to $4 billion, in 2006.

ANDREW GOULD, 59
CEO since 2003

SCHLUMBERGER LTD.

INDUSTRY
Energy Services
SALES
$14.3 billion
NET INCOME
$2.2 billion

5

» WITH THE PRICE OF oil near historic highs, energy companies are willing to invest big money to find new fields and rework old ones. No outfit benefits more than Schlumberger, the leading oil services provider. The New York-based company was global long before the concept was in vogue, and now has 58,000 employees of 140-plus nationalities working in more than 80 countries. That footprint, and state-of-the-art technology, is key as new oil is found in increasingly deep water and remote areas. It may not be glamorous work, but shares have tripled since 2002, and demand for Schlumberger's expertise is steady.

RAY R. IRANI, 71
CEO since 1990

6

OCCIDENTAL PETROLEUM CORP.

» BACK IN THE LATE 1990s, when oil prices were low, Occidental's CEO placed two big bets, spending just over $7 billion to snap up aging oil fields in Texas and California. Today, with near-record prices for crude, those wells have turned Oxy into the world's most profitable oil company. Last year the Los Angeles outfit managed an impressive $20-per-barrel profit, tops in the industry, according to Deutsche Bank Securities Inc. Lebanese-born Irani is still on the hunt. Last year he pounced on Tulsa's Vintage Petroleum for $3.8 billion and built up the biggest acreage position in Libya, newly open to American companies after years of sanctions. That nation was the site of Oxy's largest discoveries back in the day when industry legend Armand Hammer ruled the roost. Irani figures that new projects and acquisitions could boost production to nearly 1 million barrels a day by 2010, a sizable jump from the current 590,000. No doubt old man Hammer would be proud of the way his hand-picked successor is managing things.

INDUSTRY
Energy
SALES
$15.2 billion
NET INCOME
$5.3 billion

(L. TO R) PHOTOGRAPHS BY (JOBS) JOHN G. MABANGLO/EPA/CORBIS; (GLASSCOCK) DANIEL ACKER/BLOOMBERG NEWS; (GOULD) EVA-LOTTA JANSSON/BLOOMBERG NEWS

THE BUSINESSWEEK 50

DAVID J. LESAR, 52
CEO since 2000

7

HALLIBURTON CO.

INDUSTRY Energy Services
SALES $21 billion
NET INCOME $2.4 billion

» JUST A COUPLE of years ago, Dave Lesar had the corner office job no one in his right mind would want. As CEO of Halliburton, the huge oil-services construction-contractor firm, Lesar faced an energy slump depressing his core oil-and-gas services business, billions in unsettled asbestos liabilities, and political hot potatoes ranging from previous CEO Dick Cheney's compensation to controversial no-bid contracts in Iraq. Deal with them he did. The former Arthur Andersen accountant certainly benefited from sky-high energy prices, which have lifted all ships in the sector. Still, Lesar was able to put Halliburton's asbestos issue to rest by paying more than $4 billion into a trust intended to compensate more than 400,000 claims. He has also begun the process of separating Halliburton from its chronically controversial Kellogg Brown & Root construction unit. The first step is a probable IPO for 20% of KBR's shares, expected later this year. Halliburton stock, which traded in the single digits in early 2002, recently hit $70. And the outlook is bright, as long as global economic growth doesn't peter out.

PAUL E. JACOBS, 43
CEO since 2005

8

QUALCOMM INC.

INDUSTRY Communications Equipment
SALES $6 billion
NET INCOME $2.3 billion

» RAISING ITS earnings expectations has become a regular event at Qualcomm. The San Diego-based cell-phone chipmaker has hiked its projections three times in the last year on the strength of its hot-selling CDMA digital wireless technology. The industry leader in the U.S., Qualcomm's revenues have grown nearly fivefold since 2002. Now it's making big inroads into Europe, China, and India, where its wireless technology trailed behind the more widely deployed GSM. Also, it's gearing up for the U.S. launch later this year of MediaFLO, a TV-over-the-phone service that it hopes will drive chip sales.

KEVIN SHARER, 58
CEO since 2000

9

AMGEN INC.

INDUSTRY Pharmaceuticals & Biotech
SALES $12.4 billion
NET INCOME $3.7 billion

» AMGEN MAY BE ONE of the grandpas of the biotech industry, but it's looking as sprightly as ever. Profits jumped 55% last year on strong sales of its flagship drugs to treat anemia and to prevent chemotherapy-induced infections. Unlike many of its Big Pharma cousins, the California company is adept at balancing its investments in marketing and research, allowing it to boost sales of existing drugs while developing promising new treatments, such as those for colon cancer and osteoporosis. Will Amgen's constitution stay strong? Analysts predict a 15% annual rate of growth in earnings over the next five years.

RONALD A. WILLIAMS, 56
CEO since 2006

10

AETNA INC.

INDUSTRY Managed Health Care
SALES $22.5 billion
NET INCOME $1.6 billion

» THOUGH NEW TO the top job, Williams has been a key player in the much lauded turnaround at Aetna. The industry veteran worked alongside former CEO Jack Rowe to tighten up operations, winnow membership rolls, improve program offerings, and return the Hartford health insurer to profitability. The result: total returns of 385% to shareholders over the past three years. Now Williams is looking to build on Aetna's innovations in areas like consumer-driven health care and disease management programs. In a fast-consolidating industry, though, the first big move by Aetna's new boss may be a significant acquisition or merger.

ROBERT A. NIBLOCK, 43
CEO since 2005

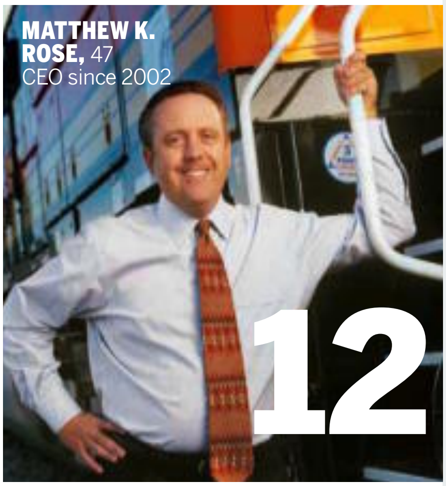
11

LOWE'S COS.

INDUSTRY Specialty retail
SALES $43.2 billion
NET INCOME $2.8 billion

» AH, THE SWEET smell of untapped markets. While archrival Home Depot Inc. is pulling back on the pace of new store openings as it approaches saturation in the U.S. market, No. 2 home improvement retailer Lowe's is still in full growth mode. The Mooresville (N.C.) company opened its first store in New Hampshire in 2005 and added a total of 150 stores overall. Its bright, airy, and female-friendly stores and an established reputation for customer service are luring shoppers from Home Depot. And Lowe's stock continues to be a darling of Wall Street: It's up more than 210% over the past five years.

(L TO R) PHOTOGRAPHS BY (LESAR) MICHAEL HART; (SHARER) AMGEN, INC./BLOOMBERG NEWS; (NIBLOCK) NELL REDMOND/BLOOMBERG NEWS



MATTHEW K. ROSE, 47
CEO since 2002

12

BURLINGTON NORTHERN SANTA FE CORP.

INDUSTRY
Railroads
SALES
$13 billion
NET INCOME
$1.5 billion

» **THERE'S ONE** good thing about being a railroad even as manufacturing, one of the industry's historic customer bases, moves offshore: Imported products have to get to consumers, too. Burlington Northern Santa Fe is one of two railroads making its debut on the BW50 list. Volume is one reason. Burlington, whose 32,000 miles of track lace the western two-thirds of the U.S., boasted record shipments in 2005, with double-digit growth in consumer goods, farm products, lumber, and other commodities. Leverage is another reason. Like every other transportation outfit, the Fort Worth-based company has been hit by all-time-high energy costs. But CEO Rose was able to pass along all the extra expense to customers through a surcharge. As a result, profits nearly doubled, to $1.5 billion. It doesn't look like Burlington is about to lose the head of steam it has built up: Industry analysts recently revised upward their profit forecasts for 2006 and 2007. The railroad is also bumping up its capital spending to meet higher demand.

EDWARD J. ZANDER, 59
CEO since 2004

13

MOTOROLA INC.

INDUSTRY
Communications Equipment
SALES
$36.8 billion
NET INCOME
$4.6 billion

» **THERE'S NO** secret to the spark behind Motorola's sizzling success: It's all about "RAZR and more RAZRs," says CEO Zander. Fueled by the RAZR, the company shipped 146 million phones in 2005, up 40% over 2004. The growth has helped Motorola boost global market share from 15.4% at the end of '04 to 19%, edging closer to industry leader Nokia Corp. To keep RAZR sales brisk, Motorola has introduced its phone in a variety of colors—black, gunmetal gray, magenta, and blue. At the same time, several new phones are hitting the market, including the SLVR and Q, svelte cousins of the RAZR. Zander hopes they'll have the same sharp edge.

TERRY S. SEMEL, 63
CEO since 2001

14

YAHOO! INC.

INDUSTRY
Internet Software & Services
SALES
$5.3 billion
NET INCOME
$1.9 billion

» **YAHOO! BOASTS** diverse Internet businesses, from search and banner ads to subscription services like fantasy sports leagues. There were more than 400 million visitors in the fourth quarter of '05, up 25% from a year earlier. The number of pages viewed rose 23%. But although Yahoo's top line grew 47% in '05, that was less than half the pace of Google Inc.'s growth. Yahoo is losing search market share to Google while trying to hatch a media strategy. Its stock price has been flat since late '04, even as Google's shares leapt 300%. All reasons why maintaining its position as Internet world-beater may not be so easy.

HENRY M. PAULSON JR., 60
CEO since 1999

15

GOLDMAN SACHS GROUP INC.

INDUSTRY
Diversified Financials
SALES
$43.4 billion
NET INCOME
$5.6 billion

» **GOLDMAN SACHS** Group has a killer combination of businesses. It has a tour de force in its trading and investment business, which churned out $6.2 billion in pretax income in 2005. And Goldman's investment banking advisory division, which pumped out $413 million, is one of the strongest in the world. With dealmaking expected to stay robust and Goldman's traders thriving in commodities, fixed income, and equities alike, analysts are bullish on the company. But as Goldman and its clients invest more often together, its risk profile may rise. So far, though, shareholders don't seem to mind.

RICHARD S. FULD JR., 59
CEO since 1993

16

LEHMAN BROTHERS HOLDINGS INC.

INDUSTRY
Diversified Financials
SALES
$32.4 billion
NET INCOME
$3.3 billion

» **LEHMAN BROTHERS** is no longer just a bond issuance and trading shop. After expanding its asset management business and poaching talent from competitors, the New York investment bank enjoys the revenue mix and client roster of Wall Street's elite. While Lehman's bond business has thrived, CEO Fuld has also steered the bank to a No. 3 ranking in global mergers and acquisitions. Lehman's profits have more than tripled since 2002. Its stock price is up 132% over the same period. And for the third straight year, the firm's U.S. equity research staff earned top honors in *Institutional Investor* magazine's annual survey.

(L TO R) PHOTOGRAPHS BY (ROSE) WYATT McSPADDEN; (ZANDER) LUCAS SCHIFRES/BLOOMBERG NEWS; (SEMEL) ROBERT GALBRAITH/BLOOMBERG NEWS; (FULD) FABRICE TROMBERT

JOHN C. MARTIN, 54
CEO since 1996

17

GILEAD SCIENCES INC.

INDUSTRY Pharmaceuticals & Biotech
SALES $2 billion
NET INCOME $814 million

» ONCE, TAMIFLU was simply the icing on the cake for Gilead Sciences, a fast-growing biotech that's a leader in developing HIV drugs. But fears of an avian flu pandemic have led governments to begin stockpiling the antiflu drug, which Gilead invented and later licensed to Roche Holdings Ltd. Largely owing to Tamiflu, Gilead's royalty revenues skyrocketed 166%, to $219 million, in 2005. The Foster City (Calif.) company is also trying to cement its No.1 position in its core HIV drug business. Strong sales there helped push overall revenues up 53%, to $2 billion. Profits jumped 81%, to $814 million. In the second quarter, Gilead plans to seek approval from the U.S. Food & Drug Administration for the first-ever regimen to treat HIV that would pack three drugs into one pill. That project, which Gilead is developing with Bristol-Myers Squibb Co., could hit the market by the end of the year. Analysts are so optimistic that Gilead can maintain its leadership in the antiviral market that they're predicting the company's earnings will grow 19% a year for the next five years.

TIMOTHY L. MAIN, 48
CEO since 2000

JABIL CIRCUIT INC.

INDUSTRY Technology Hardware
SALES $8.1 billion
NET INCOME $253 million

18

» JABIL HAS BEEN A big beneficiary of the outsourcing boom. From its humble start in the mid-1960s assembling circuit boards for electronics companies around Detroit, Jabil has grown into a leading contract manufacturer, employing roughly 50,000 workers in 19 countries. Since the tech bust in 2001, the St. Petersburg company has been on a major push to diversify beyond consumer electronics through acquisitions. Last year it bought the manufacturing operations of Varian, a maker of electronics for the aerospace and medical industries. The strategy is paying off: Profits soared 40% in 2005, to $253 million.

BRADBURY H. ANDERSON, 55
CEO since 2002

BEST BUY CO.

INDUSTRY Specialty Retailing
SALES $29.4 billion
NET INCOME $1 billion

19

» THE NATION'S No. 1 consumer-electronics chain has ridden exploding consumer demand for digital TVs, camcorders, and cameras to a spot on the BusinessWeek 50 list. Investors have certainly enjoyed the run: Shareholder return over that three-year period was 184.1%. This year won't be a slam dunk: Resurgent No. 2 Circuit City Stores, as well as Wal-Mart Stores, are aggressively gunning for Best Buy's business. To stay ahead, the Minneapolis company is stocking more upscale products and moving into new high-margin businesses such as Geek Squad, its in-home computer troubleshooting service.

JOSEPH M. TUCCI, 58
CEO since 2001

EMC CORP.

INDUSTRY Technology Hardware
SALES $9.7 billion
NET INCOME $1.1 billion

20

» CREDIT TUCCI WITH one of the most remarkable turnarounds in tech history. The new EMC is no longer just about storage hardware. Thanks to $4 billion worth of acquisitions over the past three years, the Hopkinton (Mass.) company's portfolio now includes document management, computer virtualization, and tech systems management. The shift toward software, with its higher margins, is driving profit growth: This year, Pacific Crest Securities expects EMC to boost net income by 30%, to $1.8 billion. Tucci, who has a $7.4 billion war chest, is set to continue his diversification drive.

CHAD C. DEATON, 53
CEO since 2004

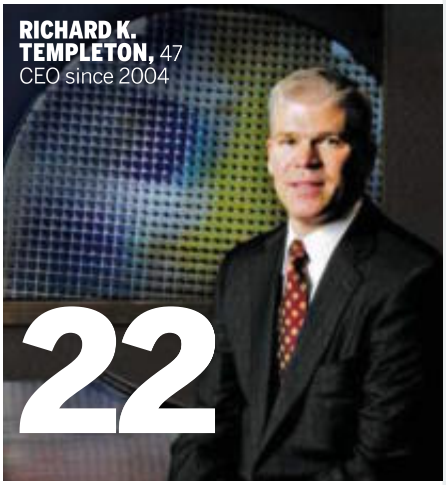
BAKER HUGHES INC.

INDUSTRY Energy Equipment & Services
SALES $7.2 billion
NET INCOME $874 million

21

» ECCENTRIC billionaire Howard Hughes is long gone, but the Houston company that issued his first dividend check is still drilling away. Earnings leapt 66% last year at Baker Hughes, which is a leading supplier of drill bits, well-logging tools, and other equipment for finding and producing oil and gas. Results have been buoyed by a ramp-up in capital spending by oil companies. With eight technology centers around the globe and over 2,200 engineers, Baker Hughes continues to search for ways to keep profits pumping even if oil prices slide. New products generated about a quarter of last year's sales.

(L TO R) PHOTOGRAPHS BY (MARTIN) MARK RICHARDS; (TUCCI) ZACK STECKLER/BLOOMBERG NEWS



RICHARD K. TEMPLETON, 47
CEO since 2004

22

TEXAS INSTRUMENTS

»IT'S HARD NOT to love Texas Instruments these days. Nokia Corp. and other cell-phone makers, experiencing explosive growth in both established and developing markets, are buying its digital and analog chipsets in ever-increasing numbers. TI's profits jumped 25% in 2005, and gross margins rose to 17.4%, compared with 14.8% a year ago. There's even more room for the company to grow now, thanks to CEO Templeton's plans to branch out into consumer electronics, with TI chips going into new gizmos such as the Slingbox streaming media server and giant TVs with digital-light-processing, or DLP, chips. Plus, the sale of the company's Sensors & Control segment to Bain Capital should plop some $3 billion into TI's coffers this year, which could go toward an acquisition or be used to continue its share buybacks. But after a long stretch of red-hot sales, analysts predict that TI's revenue growth will slow to a leisurely 3.1% in 2006, or $13.8 billion, before surging again in 2007. With demand running ahead of Wall Street's expectations, though, those predictions may be conservative.

INDUSTRY
Semiconductors
SALES
$13.4 billion
NET INCOME
$2.3 billion

JOHN T. CHAMBERS, 56
CEO since 1995

CISCO SYSTEMS INC.

INDUSTRY
Technology Hardware & Equipment
SALES
$25.9 billion
NET INCOME
$5.6 billion

23

»CISCO HAS LONG been one of the most admired tech companies. The San Jose (Calif.) outfit has posted solid, if not spectacular, sales growth in recent years as it maintained its dominance in corporate networking gear and moved into related emerging areas such as wireless home routers, Net-based phones, and security software. But Cisco really started getting love from investors after it broke its strategy mold by acquiring 55-year-old set-top box maker Scientific-Atlanta Inc. in November. The deal could crimp margins in the short term, but it may give Cisco a leading role in wiring the digital homes of the future.

JIM L. DONALD, 51
CEO since 2005

STARBUCKS CORP.

INDUSTRY
Hotels, Restaurants, & Leisure
SALES
$6.7 billion
NET INCOME
$524 million

24

»ONGOING DEMAND for coffee-based drinks and scrupulous cost containment kept Starbucks growing in fiscal 2005. The Seattle company has made moves into music sales and film production, but what's paying the bills is a continued laser-like focus on speeding up transactions, growing abroad, and finding niche markets in the U.S., such as drive-throughs and rural locations. Despite the threat of saturation in North American markets, the thirst for Starbucks apparently remains unquenchable: The company has realized 14 consecutive years of comparable-store sales growth of 5% or more.

PAUL S. OTELLINI, 55
CEO since 2005

INTEL CORP.

INDUSTRY
Semiconductors
SALES
$38.8 billion
NET INCOME
$8.7 billion

25

»INVESTORS spanked Intel hard a year ago when factory snafus and other execution missteps tripped up the chipmaking titan. Intel roared back in 2005's second half, thanks to near-complete dominance of the notebook PC segment. Intel's revenues rose 13% for the year and net income jumped 15%. But rival Advanced Micro Devices continues to steal share in the lucrative server-chip segment. Analysts predict that Intel's earnings will tumble 26% this year as AMD continues to win business one chip at a time. Intel execs say a more competitive slate rolling out in the second half of 2006 will turn the tide.

DONALD J. TOMNITZ, 57
CEO since 1998

D.R. HORTON INC.

INDUSTRY
Homebuilding
SALES
$14.2 billion
NET INCOME
$1.5 billion

26

»REVENUE AND profit have risen every quarter since D.R. Horton's founding in 1978. And execs at the Fort Worth company are confident of hitting their target of 100,000 homes sold in 2010, double their industry-leading sales of 2005. "The skeptics are dead wrong," says CEO Tomnitz. "The next five years will be a lot easier than the last 28." If housing continues to soften, Horton's emphasis on efficiency and on wringing concessions from suppliers should help it undercut other builders. It also has its strongest balance sheet ever. One risk: 28% of last year's unsold land and homes was in bubbly California.

(L TO R) PHOTOGRAPHS BY (CHAMBERS) SEOKYONG LEE/BLOOMBERG NEWS; (OTELLINI) NEAL ULEVICH/BLOOMBERG NEWS

MERRILL A. "PETE" MILLER JR., 55
CEO since 2001

NATIONAL OILWELL VARCO INC.

INDUSTRY
Energy
SALES
$4.6 billion
NET INCOME
$287 million

27

» PICK APART A drilling rig, and you'll find dozens of products made by National Oilwell Varco, including specialized motors, pumps, and cranes. The surge in exploration and production spending is leading to gushing profits for this Houston company, which was formed from the merger of the oil field products businesses of steelmakers USX Corp. and Armco Inc. in 1987. Net income more than doubled in 2005, to $287 million. National Oilwell has been quite savvy about exploiting new opportunities for growth, including last year's $2 billion acquisition of rival Varco International.

JAMES DIMON, 50
CEO since 2006

JPMORGAN CHASE & CO.

INDUSTRY
Diversified Financials
SALES
$79.9 billion
NET INCOME
$8.5 billion

28

» A HEALTHY increase in investment banking fees has plumped up the bottom line at JPMorgan Chase. But this New York bank's story is still about potential. Can Dimon, who became CEO on Jan. 1, six months ahead of schedule, complete the integration of Bank One and set a new course for growth? In the near term he'll have to deal with losses in the credit-card business and volatile trading revenues. For now, Wall Street has faith that Dimon's business acumen and strict attention to cutting costs will propel growth. Some observers expect a big deal by the end of the year: That would do the trick.

E. STANLEY O'NEAL, 54
CEO since 2002

MERRILL LYNCH & CO.

INDUSTRY
Diversified Financials
SALES
$47.8 billion
NET INCOME
$5.1 billion

29

» MERRILL LYNCH has got its mojo back. Once slowed by bloated costs, the firm is building a presence in everything from wealth management advice to energy trading and private equity. Merrill's global markets and investment banking net revenues rose 25% in 2005. Under O'Neal, Merrill's net profits have tripled, to $5 billion, and its stock price has risen 47% since 2002. It will book an aftertax gain of about $1 billion in exchange for combining its asset management business with BlackRock Inc. O'Neal isn't signaling his next move, but Street talk is that he may try to buy a regional retail broker or bank.

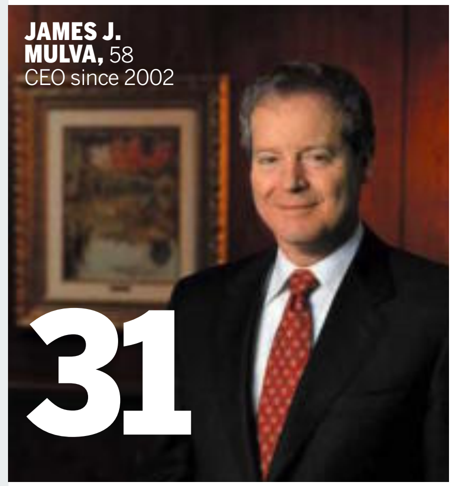
WILLIAM R. KLESSE, 59
CEO since 2006

VALERO ENERGY CORP.

INDUSTRY
Energy
SALES
$81.4 billion
NET INCOME
$3.6 billion

30

» AS GROWTH IN demand—together with the dual punch of Hurricanes Katrina and Rita—strained U.S. refining capacity again in 2005, the perennial poor cousins of the energy sector enjoyed record margins. No company was in better shape to capture the upside than Valero, the largest independent. It was a fitting climax to a remarkable 25-year run as CEO by William E. Greehey, who remains chairman. Greehey made his mark as a master consolidator. And he smartly invested billions to outfit his plants to refine heavy sour crude, which is cheaper than light sweet, giving Valero an enviable edge over refining rivals.



JAMES J. MULVA, 58
CEO since 2002

31

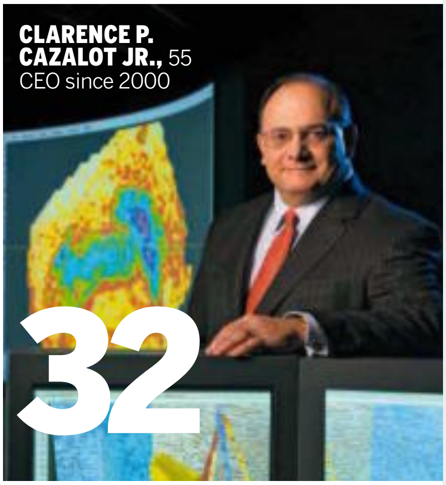
CONOCOPHILLIPS

INDUSTRY
Energy
SALES
$162.4 billion
NET INCOME
$13.6 billion

» LIKE ITS RIVALS in the oil patch, ConocoPhillips is gushing with profits. But the nation's No. 3 oil major continues to separate itself from the pack with super-aggressive investments, such as the $36 billion acquisition of natural gas leader Burlington Resources Inc., due to be completed in March. By the end of 2006, CEO Mulva also plans to spend as much as $3 billion to raise Conoco's stake in Russia's OAO Lukoil to 20%. The company is also pushing ahead with major projects in politically risky places such as Venezuela and Libya, where it recently won approval to restart operations. Conoco is pouring big money into downstream operations as well. It has bought a refinery in Germany and announced a $5 billion, multiyear program to add capacity for processing heavy crude in the U.S. So far, Mulva's bets have paid big rewards for investors: Total returns have risen 41% annually since 2002, about double those generated by Exxon Mobil Corp. and Chevron Corp. As long as global energy demand keeps growing at its current torrid pace, Conoco's shareholders are likely to get many more happy returns.

(O'NEAL) DIANE BONDAREFF/BLOOMBERG NEWS

THE BUSINESSWEEK 50



CLARENCE P. CAZALOT JR., 55
CEO since 2000

32

MARATHON OIL CORP.

»ALTHOUGH IT ranks a distant No. 4 among U.S.-based oil majors, Marathon is winning respect in a global industry where size is supposed to matter. The onetime USX subsidiary had an impressive eight discoveries out of 11 wildcat wells last year. The Houston-based company also scored a big coup in 2005 when it was allowed back into Libya, one of the world's most prolific areas, after being shut out for 19 years. CEO Cazalot, a former Texaco executive, also has ramped up downstream investments. He spent about $4 billion to buy out joint venture partner Ashland Inc.'s share in a refining, marketing, and transportation operation. And after completing a big expansion of Marathon's Detroit refinery, he recently announced a $2.2 billion upgrade of a Louisiana facility. Downstream businesses kicked in more than half of Marathon's operating income last year. Refining margins have already softened from last year's hurricane-induced spikes but are expected to remain at historically high levels until major new U.S. capacity comes onstream in a few years.

INDUSTRY
Energy
SALES
$58.6 billion
NET INCOME
$3.1 billion

ARTHUR F. RYAN, 63
CEO since 1995

PRUDENTIAL FINANCIAL INC.

INDUSTRY
Insurance
SALES
$31.7 billion
NET INCOME
$3.6 billion

33

»INSURANCE companies aren't generally known for red-hot growth. But Newark (N.J.)-based Prudential Financial saw its profits rise 49% last year. Its stock, meanwhile, soared 33%, more than twice as much as its peers. Growth at the No. 3 U.S. provider of broker-sold variable annuities has been generated in part by a shopping spree. The latest deal, on Mar. 9, is Prudential's $560 million acquisition of Allstate Corp.'s variable annuity business. And CEO Ryan still has some $3 billion in capital with which he can buy back stock or make strategic acquisitions in an industry that is ripe for consolidation.

STEVEN A. BALLMER, 50
CEO since 2000

MICROSOFT CORP.

INDUSTRY
Software
SALES
$41.4 billion
NET INCOME
$13.1 billion

34

»IT'S EASY TO LOOK at Microsoft and see the warts. Annual sales growth has slowed to single digits, and upstarts are moving ahead in new, vibrant markets such as search. But give Microsoft its due: The company continues to crank out huge profits via its twin monopolies, the Windows operating system and the Office productivity suite. And long-running efforts, such as its server software business and Xbox game console, are contributing to financial results in meaningful ways. With its next version of Windows due out early next year, Microsoft seems poised for a new round of earnings growth. Wall Street is expecting 12% a year.

RICHARD C. ADKERSON, 59
CEO since 2003

FREEPORT-McMORAN COPPER & GOLD INC.

INDUSTRY
Metals & Mining
SALES
$4.2 billion
NET INCOME
$995 million

35

»FREEPORT'S profits more than quadrupled, and shares soared in 2005, on sky-high copper and gold prices and strong production at its unrivaled Grasberg mine in Indonesia. Except for Hurricane Katrina, which devastated Freeport's home city of New Orleans, it was "a year we'd like to live over again," CEO Adkerson said recently. But this year, ever-tense relations with locals have erupted in a new spate of protests at Grasberg. Four guards were killed in March, and operations were halted for four days. Still, Adkerson is upbeat: Copper demand remains strong, and Freeport has quieted discord in Indonesia before.

BERNARD J. DUROC-DANNER, 52, CEO since 1990

WEATHERFORD INTL. LTD.

INDUSTRY
Energy Equipment & Services
SALES
$4.3 billion
NET INCOME
$466 million

36

»FOUNDED IN 1987, Weatherford has expanded rapidly through acquisitions and now does business in 100 countries. Its most recent deal: the $2.3 billion purchase last year of Precision Drilling Corp.'s energy services and contract drilling operations. It's a strategy that has produced compound annual stock returns of 27% for nearly 20 years running. The Houston company is now a leading provider of equipment and tools that allow oil companies to drill and collect data from wells in remote parts of the world. Last year it helped Chevron Corp. set an industry record by drilling the Gulf of Mexico's deepest well, boring down almost 6½ miles.

(LEFT) PHOTOGRAPH BY (CAZALOT) ROCKY KNETEN

THE BUSINESSWEEK 50

37

MARGARET C. WHITMAN, 49
CEO since 1998

EBAY INC.

»DESPITE NEW COMPETITION from the likes of Google Inc. and its GoogleBase classified ad service, eBay is still humming. Sales last year jumped 39%, to $4.6 billion, thanks in part to the rapid expansion of online payment unit PayPal Inc., which eBay bought in 2002. The San Jose (Calif.) online marketplace is counting on more savvy acquisitions to make up for slow growth in its core U.S. auction market, spending $3.6 billion in a yearlong shopping spree. The biggest prize eBay won was $2.6 billion-plus Internet phone phenom Skype Technologies, which it hopes will grease communication between buyers and sellers. The challenge for Whitman & Co. this year will be to manage this batch of acquisitions. At the same time, eBay is unleashing a flurry of new initiatives aimed at drawing a wider variety of merchants and retailers to sell or advertise on eBay. EBay Express, for instance, will let merchants more easily sell new items at fixed prices. Doing all of that won't be easy. The resulting uncertainty may be why investors have knocked eBay's stock down 15% since the beginning of the year.

INDUSTRY
Internet Services
SALES
$4.6 billion
NET INCOME
$1.1 billion

DALE B. WOLF, 50
CEO since 2005

38

COVENTRY HEALTH CARE INC.

INDUSTRY
Managed Health Care
SALES
$6.6 billion
NET INCOME
$502 million

»MANAGED-CARE company Coventry is thriving in a business otherwise dominated by a handful of big players. An emphasis on cost control has yielded 12% operating margins, among the best in the industry. Last year, the Bethesda (Md.) insurer spent $1.8 billion to buy First Health Group Corp., giving it a national provider network of 4,500 hospitals and 450,000 doctors and clinics, as well as an entrée into managing workers' comp claims. Coventry has about 500,000 clients in Medicare drug plans, but it only dipped a toe into consumer-directed health care. "Everything in moderation," emphasizes Wolf.

THOMAS M. RYAN, 53
CEO since 1994

39

CVS CORP.

INDUSTRY:
Drug Retail
SALES:
$37 Billion
NET INCOME:
$1.2 billion

»CVS, THE NATION'S largest retail pharmacist, has the wind at its back. Sales of prescription drugs account for 70% of its business, all growing thanks to an aging population of baby boomers and rising use of generics. Net income soared 33% in 2005, on a 21% increase in sales. The Woonsocket (R.I.) company also has been smart about driving sales in the front of the store. It has used its loyalty-card program, the country's biggest, to bolster sales of beauty aids and other products. CVS got a big boost with the purchase of some 1,100 stores from Eckerd Corp. in 2004. This summer, it expects to add 700 Albertson's outlets.

FREDERICK W. SMITH, 61
CEO since 1971

40

FEDEX CORP.

INDUSTRY
Air Freight & Logistics
SALES
$30.9 billion
NET INCOME
$1.6 billion

»THE RISE OF FAX and e-mail should have spelled doom for FedEx, which made its name in the '70s and '80s delivering critical documents for customers. It didn't. Realizing that the trend toward just-in-time manufacturing created new opportunities for carriers that could "absolutely, positively" guarantee delivery down to the hour, FedEx persuaded Corporate America to view its jets and trucks as mobile warehouses. The sales pitch worked, and now FedEx is thriving as never before. Sales have topped $30 billion, while profits increased 21% last year. Since 2004, shares have risen more than 50%.

GREGORY E. JOHNSON, 44
CEO since 2004

41

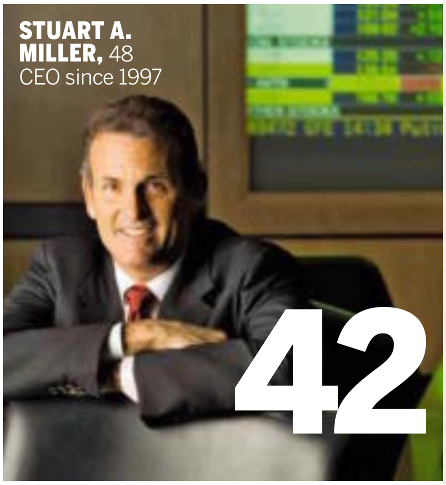
FRANKLIN RESOURCES INC.

INDUSTRY
Diversified Financials
SALES
$4.5 billion
NET INCOME
$1.1 billion

»FRANKLIN Resources, the largest of the publicly traded U.S. mutual fund companies, has been on a tear. Its stock is up an annualized 43% over the past three years, and profits are robust. The San Mateo (Calif.) company's popular Templeton international mutual funds have attracted increased investor interest as foreign equities have outpaced domestic issues. This year management plans to repatriate nearly $2 billion in foreign earnings. Franklin won't say what it will do with the windfall, but by law it can, among other things, move toward acquisitions or research and development.

(L TO R) PHOTOGRAPHS BY (WHITMAN) ANDY FREEBERG; (SMITH) JON HANCOCK/BLOOMBERG NEWS

THE BUSINESSWEEK 50



STUART A. MILLER, 48
CEO since 1997

42

LENNAR CORP.

INDUSTRY
Homebuilding
SALES
$13.9 billion
NET INCOME
$1.3 billion

» **RIP-ROARING GROWTH** in California and Florida, where homebuilder Lennar did nearly half of its business last year, helped propel the Miami company to five-year compound annual growth of 42% in profits and 24% in revenue. But now those saltwater markets are softening, and the company plans to pound the hammer more slowly. It's looking for 13% growth in unit sales this year. Analysts say Lennar can tolerate a weaker housing market better than some rivals because of its disciplined land-buying program, its conservative 33% ratio of nonfinancial services debt to capital, around $1 billion in cash, and an opportunistic culture. With LNR Property Corp., a commercial real estate developer it spun off in 1997, Lennar builds communities that include housing, offices, and retail. It specializes in developing former military bases. Lennar might gain market share in a housing downturn because it snaps up land and smaller builders at market bottoms. For now, it's trying to rev up sales. In suddenly cooling Palm Beach, Fla., after cutting broker commissions to 2% in 2004, it set out to entice brokers by raising commissions last year to as high as 5% for multiple sales.

LEW FRANKFORT, 60, CEO since 1995

43

COACH INC.

INDUSTRY
Consumer Discretionary
SALES
$1.9 billion
NET INCOME
$455 million

» **BETWEEN THE** cheap handbags and ones that cost as much as a car, there's Coach. The New York accessories maven has deftly cultivated the "accessible luxury" segment, selling fashionable, well-made items to consumers who want quality without a ridiculous price tag. Coach has avoided the bargain bin dilution that has plagued brands from Calvin Klein Inc. to Tommy Hilfiger Corp. It doesn't slash prices on the Web or at full-price stores. Coach's factory outlets are generally about an hour's drive from its retail stores. That keeps fashionistas apart from suburban moms who may not care if a cherry-red wristlet is so last year.

RONALD L. SARGENT, 50
CEO since 2002

44

STAPLES INC.

INDUSTRY
Specialty Retailing
SALES
$16.1 billion
NET INCOME
$834 million

» **SARGENT MANAGED** to expand profits by 18% last year—not bad for a business that might seem mature. He also boosted margins by selling Staples' brand office supplies in his own outlets as well as in a growing number of grocery stores. In 2005, Sargent added close to 100 new stores to his network of 1,780 in North America and Europe. But for the Framingham (Mass.) company, the biggest sales growth these days comes from delivering office supplies to businesses, most of which order online. Sales through staples.com jumped 27%, to $3.8 billion, last year. That's quite a pile of pencils and paper clips.

JEN-HSUN HUANG, 43
CEO since 1993

45

NVIDIA CORP.

INDUSTRY
Information Technology
SALES
$2.4 billion
NET INCOME
$303 million

» **FOR A TIME, NVIDIA** could do no wrong. Its graphics chips were the preferred choice of PC gamers and hip companies like Apple Computer Inc. Investors have been fond of the company, too, thanks to a total return over three years of 273.5%. But while profits soared 202% on an 18% rise in sales last year, rivals have been muscling into the graphics chip market. So CEO Huang has moved to diversify, winning a potentially lucrative slot in Sony Corp.'s upcoming PlayStation 3, due in November, and branching out into high-end cellular phones and medical devices. The big challenge: making those low-margin businesses profitable.

CHARLES W. MOORMAN, 54
CEO since 2005

46

NORFOLK SOUTHERN CORP.

INDUSTRY
Railroads
SALES
$8.5 billion
NET INCOME
$1.3 billion

» **THIS IS ONE** railroad company that's really chugging along. Powered by a global economy shipping goods to all corners of the country and zooming oil prices that made rail-shipped coal a hot commodity, the Norfolk (Va.) company turned in steaming financials in 2005. Profits shot up 39%, to $1.3 billion, on a 16% increase in sales of $8.5 billion. But the company, which runs 21,300 miles of track, mostly in the eastern U.S., isn't just riding high on a shipping boom. Best-of-breed technology keeps trains running on time, and helped Norfolk achieve an industry-leading profit margin of 15.1% last year.

(L TO R) PHOTOGRAPHS BY (MILLER) JEFFERY SALTER/REDUX; (FRANKFORT) COACH INC. VIA BLOOMBERG NEWS; (SARGENT) STAPLES INC./BLOOMBERG NEWS; (HUANG) DAVID HARTUNG/BLOOMBERG NEWS



JOHN H. HAMMERGREN, 46
CEO since 2001

McKESSON CORP.

INDUSTRY
Health-Care Distributors
SALES
$85.9 billion
NET INCOME
$776 million

RAMANI AYER, 58
CEO since 1997

HARTFORD FINANCIAL SERVICES GROUP INC.

INDUSTRY
Insurance
SALES
$27.1 billion
NET INCOME
$2.3 billion

ROBERT L. NARDELLI, 57
CEO since 2000

THE HOME DEPOT INC.

INDUSTRY
Specialty Retail
SALES
$81.5 billion
NET INCOME
$5.8 billion

JAMES W. OWENS, 60
CEO since 2004

47

CATERPILLAR INC.

» THESE DAYS, MOST old-line manufacturers are cutting American jobs as they struggle against low-cost foreign rivals. Not Caterpillar. The Peoria maker of heavy-duty machinery and engines, and the only capital-goods outfit on this year's BusinessWeek 50 list, boosted its headcount by 8,200 people, or 10.5%, in 2005, with the bulk of its new hires in the U.S. Cat needs the added help to keep up with demand fueled by the boom in construction, energy, and raw materials. Indeed, the waiting list for some of Cat's biggest equipment is years long. Little wonder, then, that its profits jumped 40% in 2005, or that its one-year total return to shareholders ranked No. 27 among all companies in the Standard & Poor's 500-stock index. Owens, a 34-year company vet, anticipates another strong year in 2006, with income rising at least 15% and sales increasing 10%, to $40 billion. Owens also has begun to gird Caterpillar against the next cyclical downturn in the industrial cycle with a big push into service businesses such as remanufacturing and logistics. Owens' ambitious goal is to make Cat a $50 billion company by decade's end. At the rate Caterpillar is growing, he may get there early.

INDUSTRY
Machinery
SALES
$36.3 billion
NET INCOME
$2.9 billion

48

» McKESSON, THE world's biggest drug distributor, came up with a cure for a splitting legal headache last year. A $960 million settlement ended a suit stemming from a massive 1999 earnings restatement that contributed to the San Francisco company's ending in the red in fiscal 2001. Now, McKesson's focus is squarely back on distributing medicines to pharmacies and hospitals. That's sweet relief, as growth in generic drug sales has bolstered margins in this notoriously low-margin business. Also helping get McKesson back in the black: sales of its new, higher-margin health-care management software.

49

» TO DRIVE FRESH growth, Ayer is pushing rapidly into wealth management and retirement planning. Sales of 401(k) plans, one of Hartford's fastest-growing products, jumped 31%, to a record $3.2 billion in 2005. Hartford is also making inroads internationally. One especially hot performer is its Japan annuity business, which last year saw assets surge 53% over the prior year. Continued growth in the Maryland-based firm's bread-and-butter life insurance and variable annuities sales, as well as a foray into new international markets, helped push assets under management up 11% last year, to $323 billion.

50

» THIS AIN'T YOUR daddy's Home Depot anymore. The housing boom along with an efficiency push at its 2,047 stores have helped the Atlanta home improvement giant turn in stellar financial results. Sales shot up from $46 billion in 2000 to $81.5 billion last year, and profits have more than doubled. Now, Nardelli is looking beyond the big-box store, to the $410 billion market to supply professional contractors. He has spent billions, rolling up more than 35 companies, to build out the Home Depot Supply unit. But the stock price, at about $43, hasn't followed suit: It has barely budged since Nardelli took over in December, 2000.

(L TO R) PHOTOGRAPHS BY (OWENS) MICHAEL L. ABRAMSON; (NARDELLI) DANIEL ACKER/BLOOMBERG NEWS

THE BUSINESSWEEK 50

Inside The Ranking

The S&P 500 represents a huge universe, accounting for some 74% of the market capitalization of all U.S. stocks. The numbers we used to rank them in our proprietary formula are shown in these tables, along with a wealth of additional financial information. For full rankings of the S&P 500 companies go to **www.BusinessWeek.com/BW50.**

GLOSSARY & FOOTNOTES

Companies on this list are from the Standard & Poor's 500. Each company is ranked by ten criteria: one-year total return; three-year total return; one-year sales growth; three-year average annual sales growth; one-year profit growth; three-year average annual profit growth; net profit margins; and estimated long-term earnings growth, with additional weight given to a company's sales and debt-to-capital ratio. A company's composite rank is calculated using the sum of all of its ranks.

MARKET VALUE
Share price on Feb. 28, 2006, multiplied by the latest available common shares outstanding.

TOTAL RETURN (1 YEAR)
Annual dividend per share, reinvested, plus Feb. 28, 2006, share price, as a percent of Feb. 28, 2005, share price.

TOTAL RETURN (3 YEAR)
Annual dividend per share, reinvested, plus Feb. 28, 2006, share price, as a percent of Feb. 28, 2003, share price.

SALES
Latest available sales through the most recent 12 months ended Jan. 31, 2006. Includes all sales and other operating revenues. For banks, this includes revenues for all banking operations.

SALES THREE-YEAR AVERAGE CHANGE
Calculated using the least-squares method. Data for 2005 and 2004 are as reported by company in 2005.

PROFITS
Latest available profits through the most recent 12 months ended Jan. 31, 2006. Net income from continuing operations before extraordinary items.

PROFITS THREE-YEAR AVERAGE CHANGE
Calculated using the least-squares method. Data for 2005 and 2004 are as reported by company in 2005. If results for one of the earliest three years are negative or not available, the average is for two years.

NET MARGINS
Net income from continuing operations before extraordinary items as a percent of sales.

RETURN ON INVESTED CAPITAL
Net income available for shareholders as a percent of debt and equity funds.

LONG-TERM EARNINGS GROWTH
The median estimate by analysts of the annual growth rate of earnings compiled by Thomson First Call. For most companies, this is for the next 3-5 years.

RECENT SHARE PRICE
Price for a single share of a company's most widely traded issue of common stock as of the close of trading Feb. 28, 2006.

HIGH/LOW PRICE
Trading range for the company's common stock, Feb. 27, 2005, to Feb. 28, 2006.

P-E RATIO
Price-earnings ratio based on latest 12 months' earnings and Feb. 28, 2006, stock price.

DIVIDEND YIELD
Annual dividend rate as a percent of the Feb. 28 stock price.

ESTIMATED EARNINGS PER SHARE
Diluted earnings per share, excluding extraordinary profit or loss, divided by number of common and common equivalent shares.

EARNINGS PER SHARE ESTIMATES
Analysts' consensus estimates for 2005 compiled as of Feb. 28, 2006, by Thomson First Call.

(a) Data as of September, 2005.
(b) Data as of October, 2005.
(c) Total return from Oct. 3, 2005.
(d) Total return from Jan. 3, 2006.
(e) Two-year growth rate.
(x) Sales include excise taxes.
(y) Sales include other income.
(z) Sales include excise taxes and other income.
NA=not available. NC=not calculable. NM=not meaningful. NR=not ranked. INC=incomplete.
† Because *BusinessWeek* is owned by The McGraw-Hill Companies, the S&P 500 Scoreboard does not include a forecast of the company's earnings.

Note: Compustat data provided by Standard & Poor's, from sources such as statistical services, registration statements, and company reports that S&P believes to be reliable but are not guaranteed by S&P or *BusinessWeek* as to correctness or completeness. This material is not an offer to buy or sell any security.

Additional data: Thomson First Call.

THE BUSINESSWEEK 50 THE TOP PERFORMERS OF THE S&P 500

RANK		COMPANY	MARKET VALUE			SALES			PROFITABILITY		
2006 RANK	2005 RANK		FEB. 28, 2006 $ MIL.	TOTAL RETURN (1 YEAR)	TOTAL RETURN (3 YEAR)	12-MONTH 2005 $ MIL.	CHANGE FROM 2004 %	3-YEAR AVERAGE CHANGE %	12-MONTH 2005 $ MIL.	CHANGE FROM 2004 %	3-YEAR AVERAGE CHANGE %
1	14	**Apple Computer** AAPL	57916.3	52.7	812.6	16190.0	66	40.9	1605.0	216	318.7
2	35	**WellPoint** WLP	50714.0	25.8	157.6	45136.0	117	47.5	2463.8	157	60.3
3	22	**Caremark Rx** CMX	22117.9	30.0	184.9	32991.3	28	78.3	932.4	55	11.4
4	5	**UnitedHealth Group** UNH	79076.3	27.8	181.3	45365.0 [y]	22	22.6	3300.0	28	35.3
5	166	**Schlumberger** SLB	67712.2	53.9	186.4	14309.2	25	4.1	2199.0	117	135.0
6	6	**Occidental Petroleum** OXY	36809.9	32.4	227.6	15208.0	34	26.9	5272.0	102	65.3
7	129	**Halliburton** HAL	34884.0	56.5	252.6	20994.0 [y]	3	19.6	2357.0	512	163.7
8	13	**Qualcomm** QCOM	77814.0	32.0	179.1	6024.0	19	21.5	2250.0	23	64.6
9	106	**Amgen** AMGN	92387.5	22.5	38.1	12430.0	18	30.6	3674.0	55	27.5
10	63	**Aetna** AET	28891.5	39.8	385.0	22491.9 [y]	13	4.8	1634.5	35	57.4
11	64	**Lowe's** LOW	53453.1	16.4	75.0	43243.0	19	17.8	2771.0	27	22.8
12	200	**Burlington Northern Santa Fe** BNI	29220.3	58.5	230.3	12987.0	19	13.4	1531.0	94	23.6
13	143	**Motorola** MOT	53303.1	37.8	194.0	36843.0	18	11.0	4599.0	110	126.9
14	8	**Yahoo!** YHOO	45851.0	-0.7	207.5	5257.7	47	80.6	1896.2	126	168.8
15	116	**Goldman Sachs Group** GS	61767.9	31.0	109.3	43391.0	45	24.1	5626.0	24	39.8
16	151	**Lehman Brothers Holdings** LEH	39616.2	61.2	169.6	32420.0	53	24.4	3260.0	38	48.5
17	47	**Gilead Sciences** GILD	28627.1	80.2	266.3	2028.4	53	62.1	813.9	81	127.8 [e]
18	153	**Jabil Circuit** JBL	7759.3	47.2	127.9	8095.4	23	29.3	252.8	40	97.5
19	83	**Best Buy** BBY	26387.4	50.7	184.1	29382.0	10	12.3	1018.0	16	20.1
20	229	**EMC** EMC	33425.7	10.7	89.7	9664.0	17	22.2	1133.2	30	51.1
21	163	**Baker Hughes** BHI	23225.3	45.0	126.7	7185.5	18	13.8	874.4	66	66.4
22	139	**Texas Instruments** TXN	47658.2	13.2	80.3	13392.0	6	18.0	2324.0	25	39.3
23	46	**Cisco Systems** CSCO	124516.5	16.2	44.8	25946.0	10	11.4	5581.0	4	21.8
24	33	**Starbucks** SBUX	27861.3	40.2	209.8	6713.8	20	24.8	523.9	24	33.8
25	55	**Intel** INTC	121931.4	-12.9	22.5	38826.0	13	13.2	8664.0	15	39.8
26	—	**D. R. Horton** DHI	10649.8	5.0	284.1	14246.7	28	24.5	1539.6	49	51.0
27	—	**National Oilwell Varco** NOV	10615.2	34.3	170.6	4644.5	100	41.8	286.9	149	57.0
28	242	**JPMorgan Chase** JPM	143442.8	16.8	102.9	79902.0	40	23.1	8483.0	90	56.5
29	188	**Merrill Lynch** MER	70693.6	33.6	135.1	47783.0	46	19.1	5116.0	15	25.6
30	4	**Valero Energy** VLO	33211.1	51.7	463.8	81362.0	51	42.5	3590.0	99	234.5
31	2	**ConocoPhillips** COP	83993.7	12.3	158.5	162405.0	37	45.9	13640.0	68	158.2
32	54	**Marathon Oil** MRO	25873.4	52.3	231.8	58596.0	30	28.7	3051.0	143	75.1
33	117	**Prudential Financial** PRU	38481.0	36.5	165.8	31708.0 [y]	13	5.8	3602.0	49	131.5
34	42	**Microsoft** MSFT	279018.1	8.1	29.5	41359.0	7	10.5	13057.0	31	18.0
35	350	**Freeport-McMoRan Copper & Gold** FCX	9318.2	28.0	230.1	4179.1	76	27.4	995.1	392	71.0
36	—	**Weatherford International** WFT	14990.0	44.7	115.4	4333.2	38	22.9	466.2	38	77.9
37	19	**eBay** EBAY	56251.6	-6.5	104.3	4552.4	39	54.9	1082.0	39	64.1
38	—	**Coventry Health Care** CVH	9685.6	41.7	373.5	6611.2	24	22.2	501.6	49	49.3
39	74	**CVS** CVS	23069.3	14.3	132.1	37006.2	21	15.2	1224.7	33	18.4
40	39	**FedEx** FDX	32588.3	10.1	110.7	30851.0	13	13.4	1575.0	21	33.5
41	71	**Franklin Resources** BEN	26506.2	51.3	229.6	4505.5 [y]	25	22.0	1135.6	47	38.8
42	—	**Lennar** LEN	9431.5	-0.6	149.7	13867.0	32	23.6	1344.4	42	34.1
43	17	**Coach** COH	13668.7	28.7	299.9	1933.9	27	32.7	454.6	46	58.3
44	61	**Staples** SPLS	17925.0	17.7	116.0	16078.9	11	11.5	834.4	18	25.2
45	345	**NVIDIA** NVDA	8067.5	62.6	273.5	2375.7	18	8.5	302.6	202	47.8
46	107	**Norfolk Southern** NSC	20978.0	44.5	179.7	8472.0	16	10.8	1281.0	39	47.4
47	23	**Caterpillar** CAT	49027.0	56.5	230.0	36339.0	20	22.8	2854.0	40	55.9
48	237	**McKesson** MCK	16563.8	45.7	107.3	85876.8	10	16.0	776.0	NM	14.8 [e]
49	82	**Hartford Financial Services** HIG	24891.3	16.4	140.6	27083.0	19	18.5	2274.0	8	33.4 [e]
50	89	**Home Depot** HD	89526.6	6.4	84.7	81511.0	12	11.9	5838.0	17	16.7

ESTIMATED LONG-TERM GROWTH %	NET MARGIN 2005	NET MARGIN 2004	RETURN ON INVESTED CAPITAL	INVESTMENT DATA RECENT SHARE PRICE $	12-MONTH HIGH/LOW $	P-E RATIO	DIVIDEND YIELD	EARNINGS PER SHARE 2004	ESTIMATED EARNINGS PER SHARE 2005	INDUSTRY GROUP
20.0	9.9	5.2	19.2	68	86/33	37	0.00	1.86	2.13	Technology Hardware & Equip.
15.0	5.5	4.6	7.9	77	80/58	19	0.00	3.94	4.57	Health-Care Equip. & Svcs.
20.0	2.8	2.3	10.9	50	54/37	24	0.00	2.05	2.30	Health-Care Equip. & Svcs.
17.0	7.3	7.0	15.3	58	65/44	23	0.05	2.48	2.90	Health-Care Equip. & Svcs.
17.5	15.4	8.8	18.8	115	132/65	32	0.87	3.62	4.95	Energy
10.0	34.7	22.9	28.9	92	98/64	7	1.57	12.89	10.69	Energy
15.0	11.2	1.9	25.3	68	82/40	15	0.88	4.54	3.99	Energy
20.0	37.4	36.1	18.8	47	49/32	36	0.76	1.32	1.49	Technology Hardware & Equip.
15.0	29.6	22.4	16.2	75	87/56	26	0.00	2.93	3.46	Pharmaceuticals & Biotech
15.5	7.3	6.1	14.5	51	52/34	19	0.04	2.70	2.75	Health-Care Equip. & Svcs.
17.0	6.4	6.0	15.5	68	70/51	20	0.35	3.46	4.02	Retailing
16.5	11.8	7.2	9.4	79	82/46	20	1.02	4.01	4.76	Transportation
10.0	12.5	7.0	22.5	21	25/14	12	0.75	1.82	1.30	Technology Hardware & Equip.
25.7	36.1	23.5	20.4	32	44/31	25	0.00	1.28	0.54	Software & Svcs.
13.4	13.0	15.3	4.3	141	146/95	13	0.99	11.21	11.86	Diversified Financials
12.0	10.1	11.1	4.0	146	150/86	13	0.66	10.87	11.35	Diversified Financials
19.0	40.1	33.9	24.8	62	64/34	36	0.00	1.72	2.07	Pharmaceuticals & Biotech
25.0	3.1	2.7	9.9	38	41/26	31	0.00	1.22	1.65	Technology Hardware & Equip.
16.5	3.5	3.3	18.8	54	56/32	27	0.59	2.02	2.64	Retailing
20.0	11.7	10.6	9.3	14	15/11	30	0.00	0.47	0.66	Technology Hardware & Equip.
17.5	12.2	8.6	15.1	68	78/42	27	0.77	2.56	3.57	Energy
20.0	17.4	14.8	18.9	30	35/23	21	0.40	1.39	1.47	Semiconductors
15.0	21.5	22.8	24.3	20	20/17	23	0.00	0.87	1.05	Technology Hardware & Equip.
22.0	7.8	7.6	23.4	36	37/22	55	0.00	0.65	0.70	Consumer Svcs.
15.0	22.3	22.0	22.6	21	29/20	15	1.94	1.40	1.23	Semiconductors
15.0	10.8	9.2	14.1	34	43/27	7	1.17	4.84	5.42	Consumer Durables & Apparel
25.0	6.2	5.0	5.7	61	78/39	34	0.00	1.81	3.04	Energy
10.0	10.6	7.8	3.7	41	42/33	17	3.31	2.38	3.37	Diversified Financials
12.1	10.7	13.6	3.4	77	78/52	15	1.30	5.16	5.99	Diversified Financials
4.4	4.4	3.4	17.7	54	64/29	9	0.45	6.10	7.54	Energy
6.0	8.4	6.8	21.1	61	71/48	6	2.36	9.63	9.75	Energy
7.0	5.2	2.8	20.6	71	78/43	8	1.87	8.49	9.69	Energy
13.0	11.4	8.6	11.6	77	79/55	12	1.01	6.46	5.63	Insurance
12.0	31.6	26.0	29.5	27	28/24	22	1.34	1.20	1.32	Software & Svcs.
15.0	23.8	8.5	30.5	51	65/32	11	2.47	4.67	3.39	Materials
25.0	10.8	10.8	7.7	43	46/24	29	0.00	1.47	2.26	Energy
25.0	23.8	23.8	10.8	40	48/31	51	0.00	0.78	1.02	Software & Svcs.
15.0	7.6	6.3	15.1	60	62/41	19	0.00	3.10	3.47	Health-Care Equip. & Svcs.
13.0	3.3	3.0	12.2	28	32/24	20	0.55	1.45	1.57	Food & Staples Retailing
15.0	5.1	4.8	12.5	107	109/77	21	0.30	5.12	6.52	Transportation
13.8	25.2	21.4	15.6	103	104/64	24	0.47	4.35	4.85	Diversified Financials
15.0	9.7	9.0	17.0	60	69/50	7	1.07	8.17	9.35	Consumer Durables & Apparel
20.0	23.5	20.4	33.4	36	37/25	30	0.00	1.18	1.24	Consumer Durables & Apparel
17.0	5.2	4.9	16.8	25	25/19	22	0.90	1.12	1.25	Retailing
20.0	12.7	5.0	20.8	47	51/21	29	0.00	1.65	2.36	Semiconductors
15.0	15.1	12.6	8.1	51	51/30	16	1.25	3.11	3.29	Transportation
10.0	7.9	6.7	11.8	73	74/41	18	1.37	4.04	4.95	Capital Goods
13.5	0.9	–0.3	11.3	54	55/35	22	0.44	2.50	2.62	Health-Care Equip. & Svcs.
12.0	8.4	9.3	11.3	82	89/65	11	1.94	7.44	8.50	Insurance
13.0	7.2	6.8	19.7	42	44/35	15	1.42	2.72	3.07	Retailing

Adidas' World Cup Shutout

U.S. fans of soccer's big event will see only Adidas ads on television. Nike's response: A MySpace-style site for soccer nuts

BY STANLEY HOLMES

IN NEW ADIDAS TV ADS, U.S. SOCcer star Pablo Mastroeni and Mexican soccer standout Jaime Lozano have three hours to recruit amateur players from the streets and beaches of Los Angeles. Their goal is to form one team of U.S. players and one team of Mexican-born players to square off in a sandlot soccer game. The ad, one in a series, is meant to capture the high-octane international rivalries that will erupt starting on June 9, the kick-off of FIFA World Cup Soccer. But all that competitive tension is nothing compared with how the company behind the ads, Adidas Group, feels about soccer when it comes to its nemesis, Nike Inc.

In the latest escalation of this decades-old rivalry, Adidas is pumping big bucks into soccer, the only category in which it leads Nike, to try to close the overall gap between the two companies. Over the next few months, Adidas is spending about $200 million to market all things soccer. Shoes, boots, national team jerseys, soccer balls, and more are featured in the ad campaign, dubbed "+10," which revolves around the idea that one player plus 10 others equals a team.

The World Cup's global TV and Web audience is bigger than the Olympics' or the Super Bowl's—28 billion in-home viewers worldwide. Adidas is an official sponsor and paid for the rights to shut Nike out of TV advertising in the U.S. for all 64 games. It's vital for Adidas "to dominate the World Cup," says CEO Herbert Hainer.

LEADING IN JAPAN

HAINER HAS SOME momentum, but he's under pressure to deliver more. After spending $3.8 billion to buy Reebok International last fall to boost Adidas' women's business, Hainer must prove the deal was more than a market share grab and integrate the companies smoothly. Meanwhile, Adidas, based in Herzogenaurach, Germany, has made gains in baseball and basketball in the U.S. and abroad. Its soccer business is growing in Europe at Nike's expense, and overall sales in Asia are rising faster than those of the U.S. sneaker giant. Adidas' global share of the branded footwear market is 34%, vs. Nike's 38%, according to NPD Group. But Adidas has surpassed Nike overall in Japan. Even its once-prosaic advertising, which paled in comparison with Nike's iconic spots, has given way to cinematic, edgy ads such as the World Cup campaign and spots featuring superstar David Beckham created by TBWA\Chiat\Day, the same agency that handles Apple Computer Inc.'s ads. Although it trails Nike in the U.S. by 14 share points, Adidas has an overall share outside the U.S. of 28%, not far from Nike's 31% (table).

Nike isn't about to concede any sport to Adidas. The Beaverton (Ore.) shoe giant is beefing up its lead in basketball and running, and since soccer is such an important gateway to brand loyalty with children worldwide, it's also pushing back on the soccer field. "Our goal is to be the No. 1 [soccer] brand in the world," says Nike President Charlie Denson.

Locked out of ad placements in the U.S. during the World Cup games, Nike is going guerrilla to get exposure. While Adidas blows its dollars on traditional ads, including locking up most of the outdoor signs in Germany, where the

ILLUSTRATION BY STEPHEN WEBSTER

matches are being played, Nike is taking the viral and digital route. The company teamed with Google Inc. to create the world's first social network for soccer fans, Joga.com. The site, which launched on Mar. 15, will roll out to 140 countries in 14 languages. Hoping to make Adidas wonder why it spent all that money on mere ads, Nike is making the site a replica of top social network site MySpace.com for soccer-mad fans to commune with each other over their favorite players and teams, download videos, create discussion groups, and the like. Nike expects millions of people to register. "It's this enormous focus on everything [soccer] that exists nowhere else that could make Joga.com so rich," says Stefan Olander, Nike's global digital director.

BECKHAM

New Attack

Adidas aims to cut Nike's overall lead by investing in soccer, the only sport in which Adidas has the edge.

	ADIDAS	NIKE
Share of total U.S. market	21%	36%
Market share outside the U.S.	28%	31%
Share of European soccer market	36%	32%
Share of U.S. soccer market	48%	32%

Data: NPD Group, *Sporting Goods Intelligence*

SHAPE-SHIFTING SHOES

THE CAMPAIGN AND Web site are named after the Brazilian phrase "*joga bonito*," or "play beautifully." Fans who join Joga.com or visit Nike's site can sift through layers of video clips, messages, and ads involving Nike's star players as well as watch videos about the magic of soccer—called *ginga* by Brazilians—in different nations. Fans can then download the clips to their iPods, computers, wireless phones, or portable PlayStations. Says Trevor Edwards, Nike's vice-president for global brand management: "Kids are talking online, connecting online, it's just a part of their world.... Gone are the days of one big ad, one big shoe."

If Nike has achieved maximum brand cachet through associations with top athletes such as Michael Jordan and Tiger Woods, Adidas is betting on buzz-generating designs and sponsorships of its own to win back share. Last year the company introduced a $250 computerized running shoe, Adidas 1, with a microchip that senses fit and performance and helps change the shoe's shape during a run. And it's looking to its World Cup ad blitz to position the recently launched +F50 Tunit soccer boots as the must-have footwear for soccer players, especially against Nike's Mercurial Vapor III boot, which has gained popularity as the lightest soccer shoe on the market. The Tunit allows wearers to customize the fit, including choosing among different weights for shoe chassis and cleats to match weather conditions and even the wearer's style of play.

Addressing local design trends is paying off, too. Adidas took the lead from Nike in Japan after sponsoring the Japan national team in the 2002 World Cup and by coming up with the adiZero, a lightweight, thin-soled sneaker that hit the spot with Asian consumers. Adidas was early to see the trend in Japan "to more lifestyle footwear and away from the technical, performance brands," says John Shanley, who follows Adidas for Susquehanna Financial Group.

Adidas is growing faster than Nike in other Asian markets, too, notably in China. It spent $80 million to be the exclusive sneaker sponsor of the 2008 Beijing Summer Olympics. "Nike could be rocked back on their heels...this all sets the stage for [expansion in] China," says Jeffrey Bliss, president of Javelin Group, an Alexandria (Va.) sports marketing firm. In fact, Adidas' gains in Asia pushed Nike to spend $44 million to sponsor the India national cricket team. That price tag may sound daft, but cricket is as much a gateway sport in India as soccer is in China.

All these frenzied moves and countermoves mean Adidas can't take its lead in soccer for granted. "I would never underestimate Nike's marketing muscle," says Sal Galatioto, president of Galatioto Sports Partners, a New York investment firm specializing in sports. "They always seem to have their finger on the pulse of what people want." Add to that pressure questions about whether Adidas can make the Reebok deal pay off, and the challenges of supplanting Nike in other markets remain huge. That's all the more reason Adidas needs its World Cup play to score early and often with fans.

DENIS DOYLE/GETTY IMAGES

A Turnaround Ace For New Orleans

Its schools were a mess before Katrina. Now they may be Bill Roberti's toughest job yet

CREEPING ROT
At Hardin Elementary, peeling desks, mud, and the stench of mold

PHOTOGRAPHS BY PHILIP GOULD

BY COLEMAN COWAN

JUST ONE LOOK AT BILL Roberti's mug tells you all you need to know. When it comes to business, he's brusque and focused, not much for small talk or a joke. Even as he folds his tree trunk of a body into the elementary school desk that has become his makeshift office space, he oozes steely resolve, honed through a dual career as a U.S. Army Reserve colonel and corporate turnaround artist. He doesn't waste words, and when he does speak, he booms. If the commanding 59-year-old is more indelicate than ever these days, it's because he's knee-deep in the most daunting challenge of his professional life: reconstituting the entire New Orleans public school system.

Roberti is a managing director at Alvarez & Marsal LLC, the New York turnaround consultant renowned for whipping Timex, Interstate Bakeries, and the post-Richard Scrushy HealthSouth into shape. In June, 2005, the firm was awarded a modest contract to help straighten out the crooked finances of the New Orleans system's 117 schools and its administration. After Hurricane Katrina the job has ballooned into something unimaginably more important. Even before Katrina flooded 80% of the city and emptied it of almost all of its residents, the New Orleans public school system was the worst of all major U.S. cities and faced intractable corruption, infighting, and racial tension. No one knows the odds against the schools better than Roberti, who did similar financial work at A&M for the St. Louis school system. Largely because of him and his staff, 10,165 students are back in the 20 public schools that are up and running.

The school board had faced a dicey, day-to-day cash crunch early this year. But as the city slowly repopulates, increased local tax revenues and federal funds have taken this year's budget off life support. The state also helped by deferring $68 million in unemployment insurance payments until January, 2007. For the first time since Katrina, Roberti was able to propose a balanced budget to the school board at its Mar. 21 meeting. But he is quick to point out that finances remain precarious. "One hiccup could still send us into a tailspin."

The original $16.7 million contract A&M got from State Superintendent of Education Cecil J. Picard has expanded to $18.6 million, encompassing physical rebuilding as well as the initial finan-

A&M'S ROBERTI Largely because of him and his staff, 10,165 students are back in class

Daunting Fix

» Alvarez & Marsal was hired to straighten out the New Orleans school system's finances. Now it's directing the rebuilding effort, too.

	PRE-KATRINA	POST-KATRINA*
SCHOOLS OPEN	117	20
STUDENTS (THOUSANDS)	63	10
BUDGET (MILLIONS)	$430	$235

*As of Mar. 20, 2006

Data: *BusinessWeek*, A&M Orleans Parish School Board Financial Report, State Superintendent of Education

cial work. Now the firm is reconstructing the financial and physical infrastructure of the entire 117-school system as well as sifting through the real estate and insurance mess created by the storm. Picard says the money for the contract comes out of the Orleans Parish School Board budget, whose deficit had gaped to $112 million earlier this year. So far, A&M has recovered $29.5 million from private insurers and obtained a $30 million community disaster loan from the federal government.

When the work began last summer, Roberti found a school system that was dysfunctional in a daunting number of ways. It was $450 million in debt, and state audits in 2004 and 2005 showed employees were siphoning millions in unauthorized paychecks. Phantom workers got payroll checks for years after they retired or were terminated. The accounting department employed no accountants. "Every aspect of the system was not working," says Roberti, a divorced father of two grown daughters. He's now living in a rented house with other A&M workers in the city's Algiers section.

What makes the job harder is the city's lingering devastation. It's been almost seven months since Katrina struck, yet conditions remain so putrid in some sections that Roberti and 35 A&M colleagues in New Orleans have each received eight vaccinations for diseases such as typhoid fever, diphtheria, and hepatitis. Some developed a hacking wheeze known locally as "Katrina cough," caused by airborne irritants remaining after the flood. At many city schools it's like Katrina happened yesterday. At Joseph Hardin Elementary in the Lower Ninth Ward, for example, overturned furniture, collapsed ceilings, and the stench of mold make it hard to venture more than a few feet into classrooms.

NEW RECRUITS

A CORNERSTONE OF Roberti's rebuilding plan has been the opening of charter schools. Of the 20 public schools open in New Orleans, 16 are charter schools; the other four are run directly by the New Orleans school board. After Katrina, A&M directed recruiting of the principals and teachers—many of whom had prior teaching experience, but none of whom, in the charter schools, were bound to the teachers' union contract. Some locals complain that Roberti is "selling off the school system." Such opposition isn't surprising; charter schools generate strong emotions just about wherever they're launched. But at Dwight D. Eisenhower Elementary School in Algiers, one of the new charter schools in New Orleans, principal Cynthia Bernard is amazed at the streamlined chain of command A&M put in place: "Without the bureaucracy, things get done quickly and easily now."

Not everyone was eager to hand financial control to outsiders. Former school board President Torin Sanders refused to sign A&M's $16.7 million contract after the board voted to approve it last June. A proposal to install Roberti as interim superintendent met with cries of racism; the school superintendent is African American, and the board vote went along racial lines. Local attorney Willie Zanders obtained a court order temporarily blocking passage of this year's $430 million school budget because it didn't include $160,000 in salary for his client—an ex-operations chief suspended in a dispute with the previous school superintendent. "That's the kind of nonsense that goes on," says Roberti.

The political back-and-forth is a reality in the fractured city, but Roberti and his team have managed to earn the respect of many locals through an undeniable drive to get the job done. A mere two days after the storm, with schools empty and the city still lawless, Roberti and two colleagues, Sajan P. George and Rajeev Jain, used Roberti's military ID to negotiate National Guard checkpoints to reenter the city. Their goal: retrieve payroll records on computer data tapes from a school administration building in Algiers. Arriving just before nightfall, they sought protection from a New Orleans Police Dept. tactical unit set up at a nearby elementary school "so they would know what we were doing and we wouldn't be shot at," Roberti explains. They slogged through foul water and retrieved the tapes, allowing them to dole out paychecks to workers scattered across the nation within two weeks of the storm. "It was important to give employees the money they were owed as soon as possible—they had no homes and needed all the help they could get," says Roberti.

Making nice with community groups isn't a task that normally falls to corporate consultants, but Roberti has no choice. At a Jan. 5 school board planning meeting, he laid out the system's dire financial straits. With detailed spreadsheets of cash flow and budget amendments, he showed that at that point revenues for the 2005-06 school year were down $271 million from pre-storm forecasts and that the schools would be facing a $65 million yearend deficit in June.

The board members, a mix of educators and concerned parents with little experience managing multimillion-dollar operations, had trouble keeping up. They interrupted him. Some found it hard to read a balance sheet. "We'll get to that in a minute, if you'll let me finish," Roberti told more than one board member.

As he tried to wrap up, a chaotic discussion about possible insolvency erupted. Brief grimaces betrayed moments of frustration, yet Roberti kept his cool, answering each question in clipped rebuttals. Eventually, his no-nonsense style sparked grudging admiration: "Your straightforward manner is refreshing, Bill," said board member Una Anderson. "Like a punch in the face, but refreshing." ∎

Seagate's Morale-athon

Inside the tech giant's $9,000-a-head team-building blowout in New Zealand

NATIVE DANCING War paint, skirts, and a Maori chant for "Seagate is powerful"

BY SARAH MAX

PLENTY OF COMPANIES *try to motivate the troops, but few go as far as Seagate Technology. In February the $9.8 billion maker of computer storage hardware flew 200 staffers to New Zealand for its sixth annual Eco Seagate—an intense week of team-building topped off by an all-day race in which Seagaters had to kayak, hike, bike, swim, and rappel down a cliff. The tab? $9,000 per person. Correspondent Sarah Max went along for the bonding.*

CEO WATKINS aims to break down barriers

SUNDAY "DON'T BE TOO COOL TO PARTICIPATE." It's cocktail hour, and nervous getting-to-know-you chatter floats around the Queenstown chalet, where we've arrived by gondola. Staffers from a dozen countries are talking and gazing out at a stupendous mountain view of The Remarkables. The employees been chosen from 1,200 who tried to get into Eco Seagate. (The company employs a total of 45,000.) There are no age limits: The oldest racer this year is 62.

In the first of many embarrassing exercises, four "tribes," each made up of 10 athletically, regionally, and operationally diverse teams, are asked to imitate the sound of the New Zealand birds for which their group has been named: Ruru, Kia, Tui, or Weka. "You're going to think some of this is pretty dumb," CEO Bill Watkins tells the crowd. "Just get involved. Don't be too cool to participate."

This event, or social experiment, is Watkins' pet project. He dreamed up Eco Seagate as a way to break down barriers, boost confidence, and, yes, make staffers better team players. "Some of you will learn about teamwork because you have a great team," he says. "Some of you will learn because your team is a disaster."

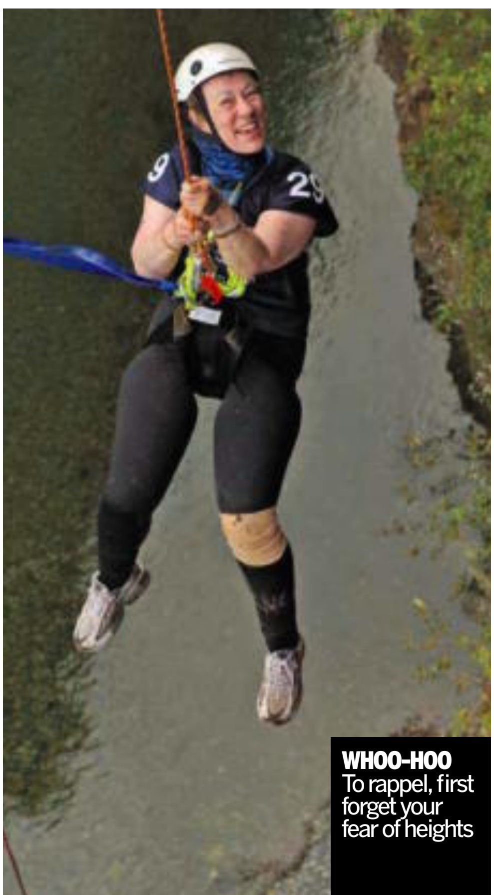
Watkins, whose company is the world's biggest maker of hard drives, knows about disastrous teams. When Seagate acquired his employer, Conner Peripherals, in 1996, hostility reigned as staffers jockeyed to guard their turf. "Corporate culture is the story of the company, " says Watkins. "Back then, Seagate had lots of great stories—about people getting fired. We needed to create a different culture—one that was open, honest, and encouraged people to work together."

KAYAKING was part of an all-day race for the four "tribes"

So how do you reprogram employees? You ask them to do something they've never done before, says Watkins, who took up adventure racing in the late 1990s and saw it as the perfect way to teach team-building. "You put them in an environment where they have to ask for help."

MONDAY BOOT CAMP IT AIN'T. "Oh, what a beautiful morning. Oh, what a beautiful day," croons Malcolm McLeod of Australia's Motivation Worldwide. "Now get out there and stretch." Dressed in referee garb, Malcolm and his gang of "stripies" have helped Eco Seagate run smoothly since the first one in 2000. Over the years the outing has evolved from just a race to a tightly organized event with a streamlined message. Each morning, Watkins or one of his top executives gives a presentation on a key attribute of a strong team, such as trust, healthy conflict, commitment, accountability. That lesson carries

MAKINGMOVIES (4); (BOTTOM RIGHT) ROSS LAND/GETTY IMAGES



WHOO-HOO To rappel, first forget your fear of heights

CYCLING beside the South Island's Lake Wakatipu

over to the afternoon, when tribes go off to learn orienteering, rappelling, mountain biking, or kayaking.

Today we're up at 5:45 for the "optional" pre-dawn stretch. But this isn't exactly boot camp. For Eco Seagate the company has taken over Rydges Lakeland Resort in Queenstown, a mountain village on the South Island. All participants have their own comfy rooms. The stretch takes place in a park across the street. Seagate CFO Charles Pope, 50, and his Shark Attack team are among the throng bending and groaning in the dark. "I don't like to schmooze for the sake of schmoozing," says Pope, who was initially opposed to the event because, for one thing, it costs a lot of money—about $1.8 million this year. That's a lot of hard drives. But it represents a fraction of the company's $40 million training-and-development budget.

In 2002, Pope caved in to Watkins' pleas to participate and came home a believer. Now, he says, Eco Seagate is one of the last things he'd cut from the budget. A lot of other companies might agree. While it's tough to find numbers for team-building events, partly because they're hard to define (a treasure hunt at a museum? a day at Disney World?), the business is growing fast, says Peter Grazier of TeamBuilding Inc. in Chadds Ford, Pa.

In the afternoon, the tribes head out for physical training. I'm "embedded" with the Rurus, who today will learn the most essential but least exciting skill of adventure racing—navigation—in the rolling hills overlooking Lake Wakatipu. The Five Elements team has done some team-building already: "We've been e-mailing almost every day since we got matched up," says Karri Barry, 37, a cash manager in Scotts Valley, Calif., where Seagate is headquartered. When the team gets maps and compasses today, they know that Choon Keong "C.K." Neo, 33, a quality manager in Singapore, will be the navigator, thanks to a stretch in his nation's military.

TUESDAY TESTING THE LIMITS. Watkins is pacing the stage of the hotel conference room, giving his morning pep talk. The speech: unscripted and emotional. The look: shaggy hair, cargo shorts, and trail-running shoes. Today he's wearing a backpack with the head of a large toy kiwi bird sticking out the top.

Yesterday each team was given one of these stuffed animals, its "sixth team member," and warned that one person must be in physical contact with it at all times. Many teams have strapped on the birds, dressed them, and even named them. Anyone caught without a bird will lose 15 green Eco tokens, which teams earn throughout the week and will use on race day to buy better maps, skip a checkpoint, or take a bridge over a frigid, fast-moving river.

At the rappel site, Pope's teammate

Tish Sanchez earns an extra token for volunteering to rappel off a bridge, her fear of heights be damned. The climbing instructors stay close. Still, Sanchez has to step out over the ledge and hang her life on a harness. "You can do it, Tish," says Pope encouragingly, standing on the bridge and looking down at his white-faced teammate. It's slow going at first, but halfway down, the usually reserved info tech manager starts yelling out: "Whoo-hoo!"

WEDNESDAY "SEAGATE IS POWERFUL. SEAGATE IS POWERFUL." Wearing war paint, headbands, and makeshift grass skirts, each tribe is performing its own uniquely choreographed *haka*—a Maori chant typically performed by native New Zealanders—in a competition worth 50 tokens to the winning tribe, as judged by a panel of Maoris. The chant—"*Moanaketi roopu kaha. Moanaketi roopu kaha*"—is said to mean: "Seagate is powerful. Seagate is powerful." But it could just convey: "What a bunch of nutcases."

"For me the race is anticlimactic," says COO David Wickersham, 49. "You learn so much about yourself in the first four days and, personally, I'm surprised by how people let their guard down." Tonight there's no question that people have shed their inhibitions. They've also shed some of their clothing: The men are shirtless, the women sport bathing suits and tank tops with skirts improvised from fabric of their team's color. There's a lot of chummy touching, though no canoodling that I can see.

But does all this expensive inhibition-ditching do anything for shareholders? Jeffrey Pfeffer, professor of organizational behavior at Stanford University's Graduate School of Business, says that while you can't measure the effect, companies with a "positive culture" probably outperform their peers. Of course, he adds, the underlying ethic has to live on after something like Eco Seagate. "If I send you off to an event and you go home and are treated like dog doo, it doesn't work."

THURSDAY "THE HARDEST YET" "How much water will there be on the course?"

"Will we have wet suits?"

"Did you say this could take us 10 hours?"

The night before the big test, Nathan Faavae, an adventure-racing superstar, is being bombarded with questions. He spent months studying maps and bushwhacking around Queenstown to design the course. "This will be the hardest Eco Seagate yet," says Faavae, who's a first-timer but tested the course with several veterans. He hands out bags filled with a map, jerseys, life jackets, and a radio.

FRIDAY TIME TO WALK THE WALK—AND SWIM THE SWIM. Here's the plan: The 40 teams are dropped on an island in the middle of Lake Wakatipu between 6 and 7 a.m. A conch sounds, and the teams race to their kayaks and paddle 1.5 miles to shore. Then, navigating with a compass, they trek over 4.3 miles of hilly terrain, mountain-bike 10.5 miles of rocks and ruts, then rappel 160 feet into a canyon for a hypothermic swim and hike.

Here's the reality: a ragged day of pain and suffering. After a slow start on the kayak, Five Elements runs past 20 teams on the hike, jumps on bikes, and pedals like mad to second place. "This pace is feeling a little leisurely," jokes Stuart Brown, 44, a program manager from Shakopee, Minn. Everyone laughs and speeds up. But an hour later they start to climb the big hill.

"Help me!" Engineer Kebiao Yuan, 41, is straddling his bike, so cramped he can't move. His teammates lift his leg over the bike, rub his knotted muscles, and squeeze a pack of sickeningly sweet energy gel into his mouth. Soon he's back on his machine, and Five Elements enters the final stretch of the bike leg. At the next transition point they ditch the bikes, run to the rim of a canyon, and rappel down. Then it's a 1.6-mile trek out, partly wading, partly swimming in 50F water. Too cold to feel anything at all, Five Elements crosses the finish line 5 hours and 51 minutes after the start—27 minutes after the first-place team, Fuel, and four hours before the stragglers.

At the finish line they find portable showers, dry clothes, and tables laden with grilled meats and salads. Miraculously, all 40 teams make it, carrying their silly kiwi birds.

I hang out near the beer, certain that exhausted Seagaters will have some critical things to say about Watkins' cockamamie event. Instead they gush about how they loved it. Then I recall CFO Pope's note of hard-headed realism. "I consider this an investment," he told me before the race, remarking that he'd soon e-mail all staffers in his organization and ask what they'd do differently as a result of Eco Seagate. "After all," he adds, "it isn't a vacation." ■

PLAYBOOK: BEST-PRACTICE IDEAS

Team-Building
What Works, What Doesn't

DO

MAKE PHYSICAL ACTIVITIES OPTIONAL "Employees should be allowed to opt out if something doesn't work for them," says Peter Grazier of TeamBuilding Inc. Find another way for these staffers to join in, and make safety a priority.

CHECK YOUR BLACKBERRY AT THE DOOR If people are peeling off to catch up with their e-mail, it's not effective, says Lynda Ford of consultancy Ford Group: "You can't send people away from the office and expect there to be no blips in productivity."

THINK ABOUT TIMING If you're announcing layoffs, slashing benefits, or cutting out the annual holiday party, an elaborate training event might hurt morale more than it helps, says Ford.

INCLUDE STAFFERS FROM ALL LEVELS AND DIVISIONS A company in crisis might want an event just for top dogs. If the goal is to strengthen the whole company, it's better to mix it up.

DON'T

LOSE SIGHT OF THE GOAL "Activities should be enjoyable but should all be aimed in one direction," says Foster Mobley of Foster Mobley Group, which has put on events for Deloitte, Citigroup, and Nokia.

LET THE BOSS RUN THE SHOW Leaders should not be the primary facilitators of training events, says Mobley, because they may be part of the company's problems. The executives "need to be in the event and playing alongside everyone else."

FORGET TO FOLLOW UP Ask employees what they got out of the event and what they're doing differently because of it, says Ford: "Don't view this as a one-time event but as part of a process."

BE A HYPOCRITE That is, stand up and talk to the group about what it means to be an effective team player, then go back to the office and act like a jerk.

EDITED BY CATHERINE ARNST

INNOVATIONS

Of methane and mega-tsunamis

›› Carbon dioxide from factories, cars, and other machines tends to grab all the headlines. Yet the earth's own emissions of methane, a more potent greenhouse gas than CO_2, may play a bigger role in global warming than once thought. Scientists at Alfred Wegener Institute for Polar & Marine Research in Germany have discovered deep-sea mud volcanoes that emit plumes of the gas, which bubble up all the way to the ocean's surface. Several thousand such volcanoes are estimated to exist throughout the world.

›› Additional regions of the earth may be capable of generating a mega-tsunami of the sort that killed more than 200,000 Asians at the end of 2004. Scientists at California Institute of Technology compared GPS coordinates, satellite images, and water-level indicators on coral reefs before and after the great tsunami-causing quake. Publishing in *Nature,* they found that it was caused by a 1,000-mile rupture between tectonic plates, much larger than computer models had described. The researchers now think geologically similar areas—such as the Caribbean and the sea between Taiwan and China—face a higher tsunami risk than previously thought.

–*Adam Aston*

(L TO R) SPENCER PLATT/GETTY IMAGES; AERO GRAPHICS, INC. /CORBIS

RESEARCH

AN AIR FORCE TROVE OF MEDICAL INFO MAY BE LOST

FOR 24 YEARS the Air Force has been collecting a huge trove of data on Vietnam veterans in an effort to determine the long-term effects of Agent Orange, a toxic defoliant sprayed on Vietnamese forests by the U.S. during the war. The Air Force Health Study now has some 87,000 biological specimens and volumes of long-term data on more than 2,200 soldiers, half of whom flew defoliant-spraying planes. But the study is set to end in September, and scientists are worried that its wealth of research will disappear if Congress doesn't appropriate funds to maintain it. In February, the Institute of Medicine issued a report recommending that the Air Force data be transferred to a new custodial organization so that scientists can continue to use it for medical research extending far beyond Agent Orange exposure. The cost, however, could run up to $500,000 a year.

SUPERBUGS

THE MIGHTY MORPHING MICROBES

DRUG-RESISTANT staph infections have skyrocketed in hospitals, where they can turn a routine procedure into a weeklong confinement. Now the microbes are expanding their sphere of influence. A recent study in the *Annals of Internal Medicine* found that treatment-resistant staph may be the primary cause of skin infections outside the hospital.

Researchers at Emory University found that 72% of the community-acquired skin infections tracked in Atlanta were due to methicillin-resistant *Staphylococcus aureus* (MRSA) bacteria. Consequently, the authors recommended a powerful antibiotic, vancomycin, be used for treatment rather than the standard penicillin-like antibiotics given for community-based staph infections. That's a major prescribing change, and it may not work for long. MRSA is usually treated effectively with vancomycin in hospitals, but resistant strains of staph have already emerged.

DATA STORAGE

THE BAR CODE LEARNS SOME SNAZZY NEW TRICKS

THE BAR CODE ISN'T just a useful tool for retailers and overnight shippers. It can also be a powerful medium for advertisers. Japanese startup Content Idea of Asia (CIA) says it has invented a printable bar code that stores bulky data files such as video clips in a space just the size of a postage stamp. These can be swiped with a cell phone and the contents then viewed on the phone's small screen. The code, dubbed paper memory, could add a high-tech gloss to conventional print ads.

Traditional zebra-stripe bar codes can't store much data. There are square bar codes that hold far more, in a two-dimensional matrix that's read up and down and side to side. CIA's PM Code adds color. In tests, the company's research chief, Kazuhiro Miwa, has shown that a paper memory code with eight color layers can store 600 kilobytes —enough for 20 seconds of low-resolution video. Snap a picture with the cell phone's camera, and the codes can activate the handset's Internet service to pull up an advertiser's home page, or view the embedded images. CIA hopes to sell its code in Japan later this year.

–*Kenji Hall*

Cooking Up A Vacation

Foodie travelers are causing a boom in hands-on culinary programs. **BY AMY CORTESE**

FISH DISH AT L'OASIS

CHRISTY CLARK FINISHED her four-hour shift in the kitchen of Kuleto's Italian Restaurant in downtown San Francisco, where she prepped a salad of blood oranges, blue cheese, and beets and rolled out freshly made pasta that would feed some 600 diners. Exhausted but exhilarated, she shed her toque at 6 p.m. and sat down to a meal in the dining room. Clark is no chef. She's a mother of two from Sacramento who, in late January, drove two hours with her husband and kids and paid $150 to toil in Kuleto's kitchen, staying in the adjacent Villa Florence Hotel. Clark was participating in the Chef for a Day program, which lets amateur cooks work in the restaurant's kitchen to raise money for the San Francisco Food Bank (sffoodbank.org/pdfs/chef4aday.pdf). "I'm not crazy enough to be a chef," says Clark, a former food photographer who loves to cook. "But I'm so interested in how it all works."

That enthusiasm is shared by a growing number of Americans who enjoy a steady diet of TV cooking shows and celebrity chefs. Like Clark, who combined her Chef for a Day stint with a visit to in-laws, they are fueling a boom in culinary travel.

Fine dining has long been a critical aspect of travel, as anyone who has ever planned a trip around a hard-to-get restaurant reservation can attest. Americans spent $131 billion on food while traveling domestically in 2004, more than they did on lodging, according to the Travel Industry Association of America. But these days vacationers are looking for more than just a good meal. They want to learn about their food's ingredients, understand how it's made, and even participate in the preparation.

Hotels, restaurants, and cruise lines are responding with innovative programs that offer food enthusiasts unique culinary experiences. From diving for your lobster dinner to cooking alongside your favorite chef, the offerings go beyond conventional cooking classes. "The behind-the-scenes experience is very important," says Jacques-Olivier Chauvin, chief executive of Paris-based Relais & Chateaux, the association of hotels known for fine dining and accommodations.

The Rosens of Raleigh, N.C., have become ardent culinary travelers. Three years ago, on a vacation in Italy, they stopped off at Dolada, a Michelin two-star restaurant and hotel in Pieve D'Alpago north of Venice. They enjoyed the meal so much they extended their stay by four days and persuaded the chef to teach them to cook specialties such as gnocchi. "We found out cooking as a family can be fun," says Alan Rosen, a radiologist.

For their next vacation, Rosen and his wife, Susan Levy, a psychiatrist, along with their three children, ages 8, 13, and 17, spent a week at a Four Seasons resort and cooking school in Chiang Mai, Thailand. Under the tutelage of chef Pitak Srichan, they learned to make dishes such as pad thai and banana blossom salad (fourseasons.com/chiangmai).

The Four Seasons and other luxury chains have been in the forefront of the trend. Like the Chiang Mai cooking school, which opened in 2003 and costs $150 a day per person, most of the Four Seasons' 70 properties offer epicurean programs tailored to particular locations. At the Terre Blanche resort in Tourrettes in Provence, guests learn the basics of French cooking at nearby La Pitchoune, where Julia Child once whipped up soufflés. The Taste of Provence package, which includes breakfast, one dinner for two, three nights' lodging, and a trip to the local market, in addition to the cooking school, starts at $1,200.

BEACH BARBECUE

FOR A MERE $3,000 per couple, not including lodging, visitors to the Four Seasons Nevis in the Caribbean can take part in a new "Dive & Dine" program. Available to groups of two to six certified divers, it features a brief seminar on local marine life and a private dive with Chef Cyrille Pannier. He instructs guests on the fine art of lassoing local spiny lobster and later cooks up the catch at an intimate beach barbecue. "The experiences we are creating are very much in response to that intensified love of food," says Elizabeth Pizzinato, director of corporate public relations at Four Seasons Hotels Inc., based in Toronto.

At Relais & Chateaux, the culinary experience has always been important. Surveys have shown that 83% of guests come for the food. Lately its properties are offering fresh options. At Restaurant l'Oasis

(THIS PAGE) WWW.RELAISCHATEAUX.COM; (OPPOSITE PAGE, CLOCKWISE FROM LEFT) COURTESY FOUR SEASONS; TERRY MCCARTHY; COURTESY FOUR SEASONS; COURTESY HOLLAND AMERICA LINE

EPICUREAN EXPLORATION

For culinary tourists, the kitchen is the key destination

« THAILAND
Chef Pitak Srichan instructing guests at the Four Seasons in Chiang Mai

SAN FRANCISCO
Halibut entrée at Kuleto's, which has the Chef for a Day program

NEVIS
At the Four Seasons, guests can dive for their lobster dinner

THE HIGH SEAS
Holland America brings leading chefs to do cooking demos

near Cannes in southern France, diners can accompany the chef on his 6 a.m. rounds to the fish market. At Le Manoir aux Quat'Saisons in Oxford, England, travelers can sample rare herbs from the hotel's garden and take home cuttings.

Such culinary flourishes not only make a trip more memorable but also open windows. Epicurean travelers are often looking for an authentic experience. "You can really learn about the culture through the cuisine," says Michael Coon, travel director for the Culinary Institute of America's Worlds of Flavor program, which operates tours of 12 to 18 amateur and professional cooks designed to give an insider's view of Vietnam, Italy, and Mexico, among other places (worldsofflavor.com).

Some cruise ships now have food-show-like kitchens

Cruise line companies are applying that lesson to a mass audience. After extensive research identified food and wine as a growing area of interest among its customers, Holland America Line started equipping each of its ships with state-of-the-art Culinary Arts Centers, similar to the kitchens on food shows, at a price of $1 million each. Through a partnership with *Food & Wine* magazine, the cruise line brings in leading chefs and experts to conduct cooking demonstrations relating to ports of call—margaritas and quesadillas for the Mexican Riviera, seafood stews in the Mediterranean. This season's lineup includes Iron Chef Cat Cora and Aaron Sanchez of New York's Paladar restaurant (hollandamerica.com).

MARITIME MENU

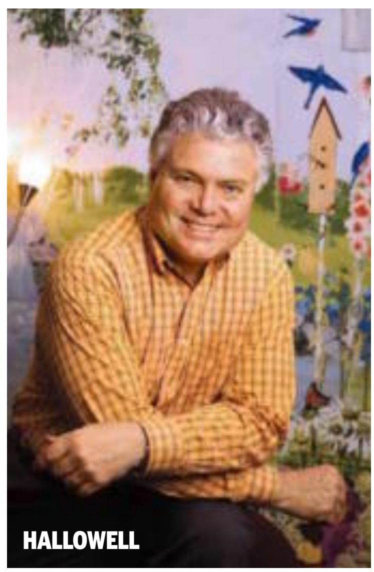
Would-be gourmets can bring that experience home with them. Back in her spacious kitchen in Sacramento, former Chef for a Day Clark still marvels at how the staff at Kuleto's was able to prepare food so meticulously in such cramped quarters. She makes the blood orange salad for her family and hopes to return someday for the early-morning pastry shift.

Rolling dough and prepping vegetables for four hours may not be everyone's idea of a good time. But for more and more foodies, it sounds like the perfect vacation.

Zen and the Art of Thinking Straight

Author Ed Hallowell has some solutions for the frazzled and overwhelmed

ARE YOU SUFFERING from any of these symptoms? You frequently feel rushed and impatient, you're easily distracted, you're forgetful, and you have little time for creative thought. If so, Dr. Edward Hallowell, a Sudbury (Mass.) psychiatrist, has a diagnosis: You're probably suffering from environmentally induced attention deficit disorder, brought on by technology and activity overload. Hallowell spoke to Associate Editor Anne Tergesen about the solutions he outlined in his new book, *CrazyBusy: Overstretched, Overbooked, and About to Snap—Strategies for Coping in a World Gone ADD* (Ballantine Books; $24.95).



HALLOWELL

What are the consequences of living in our attention deficit society?

Everybody is trying to do more in less time. People literally channel surf through the day. During conversations, part of our minds are elsewhere. We want to move on. When you gradually take on more and more, it can reach a point where everything, even good things like friendship, starts to feel like a burden. In that mode, you won't function well at work or interpersonally.

Are business people vulnerable?

Yes. They are conditioned to never complain. They want to be good team players. So when they're asked to do more, they suck it up and work harder until they become so frazzled, they're not enjoying the work and performance trails off. It's a safe bet that anyone who works and has kids also understands these issues. They're juggling deadlines, games, rehearsals, and school meetings. They're worrying about how the grocery shopping, cooking, and laundry will get done. People want to do all these activities. But they take on more than they can reasonably do. E-mail tends to facilitate the overscheduling.

What's the solution?

Do not allow the world to have access to you 24/7. Set aside time to work before you check your e-mail or snail mail or voice mail, before you allow the world to intrude on your fresh and focused state of mind. Turn off your BlackBerry and cell phone. Stretch or have a five-minute conversation. When you sit down again, you'll be focused.

What else do you recommend?

Prioritizing is crucial. If you don't, you'll find yourself spread so thin you'll only be able to see your good friends on the first Tuesday in February. Give yourself permission to end relationships and projects that drain you. Do what you're good at and delegate the rest. This is important, because when we do what we're good at, the work can take on the quality of play. Keep in mind that some of our best thoughts come when we're doing nothing. Downtime is a forgotten art.

(L TO R) COURTESY HOLLAND AMERICA LINES; SHAWN G. HENRY

An Alternative for Cancer Patients

For-profit treatment centers are competing with community and teaching hospitals. **BY MICHAEL ARNDT**

TEENA PATTERSON WAS diagnosed with inoperable cancer in January, 2004. Thinking she had gallstones, the hairdresser from Council Grove, Kan., went to see her family physician for a sonogram. The doctor discovered her liver was spotted with tumors. For six months, Patterson and her husband, Steve, a truck driver for Frito-Lay, traveled 60 miles each way to Topeka every three weeks for chemotherapy. The drugs shrank the growths, but Patterson lost faith in her oncologist when he told her she asked too many questions.

Then her sister-in-law passed along a videotape she had ordered after seeing a commercial for Cancer Treatment Centers of America (CTCA). Patterson was immediately drawn to its message of holistic healing and personalized care. After confirming that her insurer, Blue Cross & Blue Shield Assn., would cover treatment at the for-profit chain, she was soon on a plane to CTCA's Midwestern hospital outside Chicago for continued chemotherapy and radiation. Patterson, 50, returns to the facility once a month for an infusion of chemotherapy drug Erbitux and a checkup. She still has end-stage cancer. But the tumors appear to be in remission, and she feels good. She credits the CTCA staff. "Their way with people is wonderful," she says. "They really want you to succeed."

IN REMISSION Patterson credits the CTCA staff for her morale and sense of well-being

For years the provider choice for cancer patients has been either a community hospital or a big-name teaching institute. Now there's a third way: for-profit cancer hospitals. Many are local or limited-treatment outfits, such as physician-owned Arizona Oncology Services, which has 11 Phoenix-area clinics that offer only radiation therapy. But Aptium Oncology, a Los Angeles subsidiary of drugmaker AstraZeneca, just opened its ninth outpatient center, in Elizabeth, N.J., giving it properties in four states. U.S. Oncology of Houston, which has 97 facilities in 33 states, boasts that it treats more cancer patients than any other organization in the country.

For many people, particularly those with rare forms of the disease, the medical-school centers remain the preferred option. The National Cancer Institute accredits 39 comprehensive cancer centers in the U.S. Among them: Northwestern Memorial Hospital's Robert H. Lurie Comprehensive Cancer Center in Chicago and the Mayo Clinic in Rochester, Minn. These giant institutions may not be as convenient as the neighborhood hospital—half the states, in fact, don't have an NCI-designated comprehensive center—but they have the budgets for multimillion-dollar radiological machines and other high-tech equipment, not to mention acclaimed medical practitioners and unrivaled access to experimental drugs and procedures.

Most important, they may come out ahead on effectiveness. Although there are no national data ranking cancer facilities by survival or recurrence rates,

CALLIE LIPKIN (2)

KNOWHOW EDGE A new study says specialist centers often have expertise the all-purpose community hospitals lack

studies have shown that patients do better when their surgeons have performed the same operations over and over again. For example, Dr. William J. Catalona, director of Northwestern's clinical prostate-cancer program, has performed 4,700 nerve-sparing prostate removals, and is still doing 25 to 30 a month. "You look at our centers and the magnitude of the faculty and the research, and there's got to be some very fundamental differences" over the for-profit chains, says Patricia J. Goldsmith, senior vice-president of business development at the National Comprehensive Cancer Network, which represents 19 centers.

Still, a just-published study by health and science consultancy RTI International in Research Triangle Park, N.C., finds that for-profit facilities may be an acceptable alternative. The government-funded report, in the January/February issue of *Health Affairs*, notes that, by their nature, specialist centers often have the expertise and high volumes that all-purpose community hospitals lack. Plus, since they're usually smaller, they can be more personal in patient treatment. "Quality of care is not just dependent on the guy who cuts," says Leslie Greenwald, a senior scientist at RTI and the study's lead author. "It's the nurse who takes care of you and the lab personnel; it's the whole package."

EXPANSION PLANS

OF ALL THE for-profit cancer centers, U.S. Oncology is the biggest and fastest-growing. The company, taken private in a $1.6 billion buyout in 2004, opened five centers last year in partnership with local doctor groups and other investors, increasing its annual revenue to $2.5 billion. Its site in Maplewood, Minn., is typical. One of seven in the Minneapolis-St. Paul area in the Minnesota Oncology Hematology Professional Assn., the facility each week treats roughly 200 outpatients already diagnosed with cancer. Lab work is done on the premises, with results promised in 30 minutes.

The clinic does no surgery, but it offers chemotherapy, including drugs in experimental trials, and radiation treatment. The infusion area is utilitarian: a row of 18 vinyl recliner chairs in a linoleum-tiled room with six TVs suspended from the ceiling and plastic trash cans on the floor. Its radiological equipment, though, includes a state-of-the-art linear accelerator that can zap a tumor from almost any angle with sub-millimeter precision. The machine, from Varian Medical Systems, lists for $5 million. The Minnesota network has two other selling points: Most insurance plans, including Medicare, cover its services, and it is convenient.

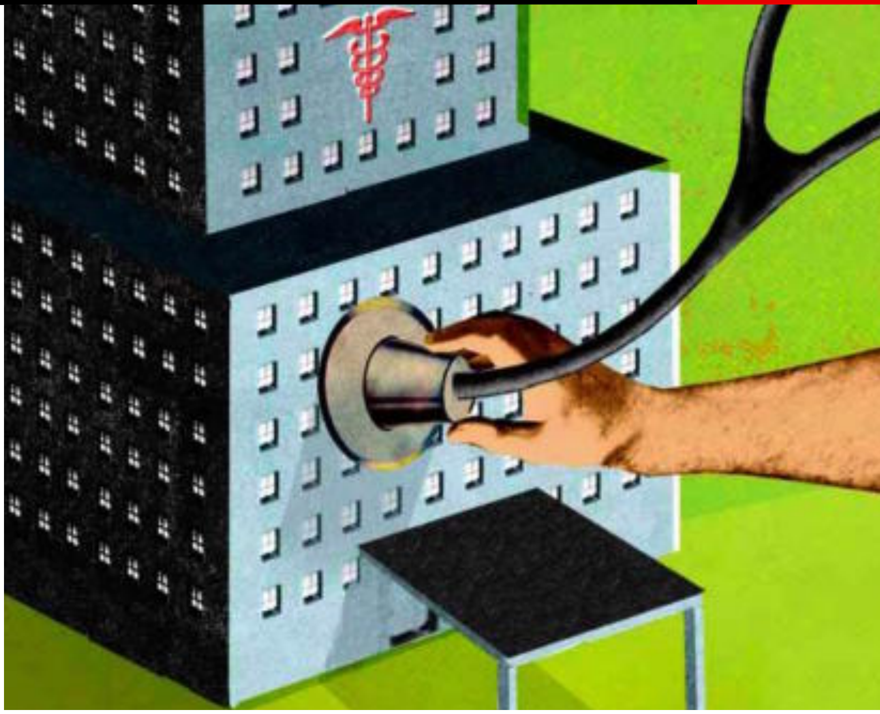
While it's also profit-driven, CTCA is more like a mini-version of Boston's Dana-Farber Cancer Institute than an outpatient-only chain. Its facilities provide chemotherapy, radiation treatment, and stem-cell transplants, but they also have state-licensed hospital rooms. Patients, who travel an average 540 miles one way, can check in and be treated over days if necessary. The centers also have operating rooms and their own oncology surgeons. The company, in Schaumburg, Ill., which began in 1988 with a former community hospital in Zion, Ill., has hospitals in Tulsa and Philadelphia. CTCA has applied for a hospital license in Seattle, where it has an outpatient facility, and plans to expand to Atlanta.

Giant teaching centers point to their R&D advantage

The privately held company eschews physician referrals and advertises to people with late-stage cancer, promising to do almost anything they want to combat the disease. In its Midwestern Regional Medical Center in Zion, the professional staff—radiologists, nutritionists, physical therapists, nurses, pharmacists, a pastor, and even a laughter therapist—meet three times a week to review each patient's condition. In smaller teams, they go from room to room daily to check on patients.

Charges can add up quickly, just as they would at a comprehensive cancer center. Patterson says that after 18 months of treatment at CTCA, including an eight-week stay last summer for radiation and $28,000 a month for her current course of chemotherapy, she is about to max out on her $1 million lifetime coverage through her husband's health-care plan. She is now shopping for a new policy, with higher premiums and deductibles. Still, Patterson has no thoughts about going somewhere else. For her, and for plenty of other cancer patients, the third way is the right way. ■

BusinessWeek online For a table comparing cancer treatment hospitals, go to businessweek.com/extras



Is Your Hospital Heart Healthy?

Before making that appointment with a cardiologist, it pays to do some homework. **BY HOWARD GLECKMAN**

YOU JUST HAD YOUR ANnual physical. Your family doctor says he wasn't happy with your electrocardiogram and wants you to see a cardiologist for tests.

Before you make an appointment, you might want to check out local hospitals to see which rate best at treating heart disease. Why do that? If you eventually need surgery or other intensive treatment, you want to make sure your cardiologist will do the work at a top-ranked facility.

Where do you start? While objective hospital ratings are in their infancy, heart disease is one illness for which the quality of care can be gauged. For instance, it is widely believed that patients with heart disease should be given drugs called ACE inhibitors or ARBs. So hospitals that prescribe them get higher ratings than those that don't.

> This is one specialty for which quality of care can be objectively rated

One good resource is Hospital Compare, operated by the federal Centers for Medicare & Medicaid Services (CMS). It allows you to search local facilities to see how well they treat both heart disease and heart attacks (www.hospitalcompare.hhs.gov). While on the site, compare infection rates, which are a powerful predictor of hospital quality. Avoiding nasty bugs should be a top priority for anyone about to be admitted to a hospital.

The Joint Commission on Accreditation of Health Care Organizations (JCAHO, pronounced Jayco) is another good place to turn. This private, nonprofit organization sets standards for patient care and safety, and certifies hospitals and other medical care providers. Its site, jcaho.org, is full of information, although it isn't easy to navigate. Click on Quality Check, plug in your zip code, and you'll find a link to your local hospitals. From there, you can look at an individual facility or compare several. For each hospital, look at how they rate for heart-attack care and heart-failure care.

Another national resource is the Leapfrog Group (leapfroggroup.org), which rates hospitals on a handful of high-risk procedures, including heart bypass surgery. Leapfrog, funded by major employers and some insurers, does not cover as many hospitals as CMS, in part because it rates only those hospitals that volunteer to respond to its surveys. Hospital Compare, by contrast, uses more extensive Medicare claims information and other sources. Leapfrog does tell you exactly how many heart surgeries are performed at each hospital, useful since hospitals that do lots of these procedures tend to have the highest success rates.

BROADENING THE SEARCH

DR. VINCE BUFALINO, a Naperville (Ill.) cardiologist, warns consumers to be careful when they evaluate the sites. Take the numerical grades that Hospital Compare provides. Patients need to remember there is no real difference between a hospital that scores 94 and one that scores 92, says Bufalino. The sites "should be one bullet point in your evaluation."

You can also check your health insurer's site. Most now include some guidance for choosing a hospital, although few provide the detail that you'll find at Hospital Compare or JCAHO. Many insurers will rank a hospital in their top tier but not tell you much about why.

Finally, if you do need surgery, you might want to get some general information on heart disease and its treatment. There are plenty of good, informative Web resources, including the American Heart Assn. (americanheart.org), WebMD (webmd.com), and the National Institutes of Health (medlineplus.gov).

Rating hospitals for heart care is still an imperfect process. And informed patients may want to know a lot more about the facilities and the staff than they can learn on the Web. But check out these sites before you see the cardiologist. Then you'll be prepared to start asking your specialist questions. ■

BRIAN STAUFFER

The Currency Game: Home Version

Foreign exchange for retail investors? New online trading sites make it affordable. **BY ADRIENNE CARTER**

RODNEY NORMAN LIVES a few miles from the Las Vegas strip. But the 40-year-old independent film producer is not much of a gambler—unless you count his penchant for foreign currency trading. Three years ago, Norman put $250 into an online trading account and doubled that when he became comfortable with price charts and economic indicators. He now spends a few hours a day exploring the market for ideas and has steadily built up the account to about $25,000, betting mainly on the U.S. dollar, Swiss franc, and British pound.

Until recently, foreign currency trading, known as forex or FX, was largely the domain of professional traders and high-net-worth individuals. But many new Web sites now offer accounts with minimums as low as $250, making it affordable for savvy individuals to play. Although there are dozens of sites, it's best to stick with the largest and most established, FOREX.com and FXCM.com

Similar to commodities or options, the forex market is a way to diversify or hedge a portfolio. Since you make money by playing the relative movement of one currency against another, there's no such thing as a bear market in currencies.

But forex is a 24-hour market, and it moves more quickly than the stock market, with currencies sometimes going up, down, and sideways in the course of hours. Indeed, it's not for buy and hold investors. Some 80% of traders are in and out of their positions in a week or less. Given the dynamics, you should play only with money you can afford to lose.

THE STAT

$250

The minimum needed to open a forex trading account

All trades involve pairs of currencies, typically among "the majors": the U.S. dollar, euro, Japanese yen, Canadian dollar, Swiss franc, British pound, or Australian dollar. If you think the U.S. dollar will weaken against the yen, you would sell dollars and buy yen. FX is largely commission free, with the trading cost built into the spread between the bid and ask price. Leverage is also common: If you have $5,000 in a margin account with leverage of 100 to 1, you can buy up to $500,000 of currency. That can amplify your gains and losses.

Let's say you decide the U.S. dollar (USD) is undervalued relative to the Swiss franc (CHF). In that case, you would buy dollars and sell francs in anticipation of a rising exchange rate. The current bid/ask price for USD/CHF is around 1.2895/1.29, meaning you can buy $1 for 1.29 francs. Using leverage and putting up $1,000 of your $5,000 margin account, you buy one lot—the equivalent of buying $100,000 and selling 129,000 francs.

"IT'S A BRUTAL, BRUTAL WORLD"

IF THE EXCHANGE rate rises to 1.2935/1.2940 and you want to realize profits, you would sell $100,000 and get 129,350 francs, netting 350 francs. At prevailing rates, the profit would be around $270, or 27% on that $1,000 trade. Conversely, if you were wrong and the rate dropped to 1.2855/1.2860, you would lose $350, or 35%. Should the rate continue to fall, your margin account could be wiped out.

Currently, some investors, including Warren Buffett, are betting against the U.S. dollar in light of a rising current account deficit. Pros are bullish on the Canadian dollar. The country has an account surplus and is benefiting from strength in the oil market.

Even though currency traders look at long-term macroeconomic trends, the short-term nature of FX means they rely heavily on technical analysis. They study price charts to forecast which direction a currency is headed. They also pay close attention to economic indicators such as gross domestic product, nonfarm payrolls, and housing starts.

Forex is a global minefield that can trip up some of the smartest minds, as it has Buffett of late. "It's a rush because the market moves so quickly," says T.J. Marta, senior currency strategist at RBC Capital Markets. "But it's a brutal, brutal world." As such, a disciplined trading strategy with entry and exit points is critical. Stop loss and limit orders help keep trades within a range and curb losses. It's worth testing trades at an online demo, available at most e-brokers, before putting money at risk.

Newcomer HedgeStreet offers online products known as Hedgelets that let you make daily or monthly bets on the dollar in relation to the euro, pound, franc, or yen (hedgestreet.com). There is no leverage, and the Hedgelets limit potential losses and gains—between $0 and $50 per contract. Prices are reasonable; HedgeStreet charges $1.50 for the first 30 contracts. If forex makes you nervous, this is a somewhat tamer way to trade in currencies. ■

JOHN KUCZALA

EDITED BY MONICA GAGNIER

TIME OFF

MODERNISM MEETS THE OLD SOUTH

THE INSTITUTION THAT bills itself as the oldest public art museum in the South has just opened a modern glass-and-stone edifice designed by Israeli-Canadian architect Moshe Safdie.

Known as the Jepson Center for the Arts, the 64,000-square-foot building marks the first expansion in the 119-year history of Savannah's Telfair Museum of Art. The $30 million facility adds 66% more space to the museum's two National Historic Landmark buildings in the Georgia city's historic district.

JEPSON CENTER Snazzy new look

Among the features of the Jepson Center are two large spaces for major traveling exhibits, a hands-on gallery for young people, a 200-seat auditorium, two outdoor sculpture terraces, a café, and a store (telfair.org).

In the Jepson's inaugural exhibits, you can view recent assemblages and collages by Robert Rauschenberg, as well as a tribute to Savannah's artistic heritage. The Rauschenberg show runs through June 4, while the Savannah exhibit closes May 14.

Also on display through May 21 is the Kirk Varnedoe Collection, 20 works on paper by such contemporary artists as Frank Stella, Richard Serra, and Jeff Koons. The collection is a gift from sculptor/photographer Elyn Zimmerman in memory of her husband Varnedoe, a Savannah native who was a curator at the Museum of Modern Art.

COLLEGE SAVINGS PLANS

On Equal Footing

SAVING FOR COLLEGE via prepaid plans that allow parents to lock in tuition at today's rates has always had a big drawback: Every dollar in the plan can cost parents and students a dollar of financial aid. On the other hand, every $1 in a Section 529 college savings plan—which allows parents to invest money that grows tax-free, provided it's used for schooling—only knocks 5.6¢ off of financial aid.

In a recently passed budget bill that goes into effect on July 1, Congress put the two types of college savings plans—prepaid and savings—on equal footing. As a result, families will lose only 5.6¢ in aid for every dollar in each kind of account.

Of the 19 prepaid plans on the market, 18 are sponsored by states. The other is the privately backed Independent 529 Plan, which locks in today's tuition at 255 participating private universities, including Princeton and Rice. Many state prepaids require the beneficiary or account owner to be a resident of the sponsor state. If a student opts for a private or out-of-state school, many pay out the equivalent of average in-state public college tuition. *–Anne Tergesen*

THE OTHER RED MEATS

IF YOU LOVE beef, but not the fat and calories, try the lean red meats popping up at specialty food stores. D'Artagnan recently began distributing buffalo, ostrich, and venison to gourmet grocers. They are higher in protein than beef and much lower in fat (table). Buffalo tastes the most like beef, while venison is more gamy and ostrich is a bit sweet. Your only beef might be the price. Buffalo tenderloin is about $35 per pound, vs. $17 for the same cut of top-of-the-line prime beef. *–Lauren Young*

3.5 OZ. SERVING (COOKED)	CALORIES	FAT	CHOLESTEROL	PROTEIN	PRICE/LB.
Buffalo	143	2.4g	82mg	28.4%	$35.00
Ostrich	140	2.8	65	26.9	22.50
Prime Beef	255	15.3	86	27.5	17.00
Venison	150	2.4	79	30.0	29.25

Data: D'Artagnan

(TOP) CHRISTOPH VORLET; (LEFT) RICHARD LEO JOHNSON/ATLANTIC ARCHIVES

BY GENE G. MARCIAL

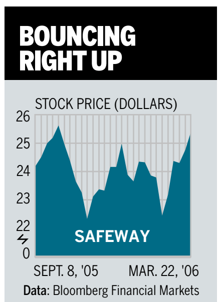
HEALTHIER VITTLES LURE SHOPPERS INTO SAFEWAY'S AISLES.

BOB EVANS FARMS HAS BEEN SERVING UP HEFTY GAINS LATELY.

WILL OPPONENTS BLOCK A BUYOUT AT DRUGMAKER ANDRX?

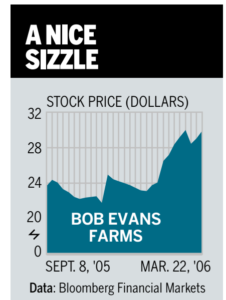
Safeway: On Safer Turf

AFTER THREE YEARS of sluggish sales and crimped earnings, Safeway (SWY) is back. The supermarket chain was "sailing in treacherous waters," says Hitesh Kuvelkar, an analyst at investment firm First Global, but has "recovered smartly." In 2005's fourth quarter, earnings jumped 15% on a sales rise of 7.2%. Safeway's stock, up from 22 in mid-February to 25.33 on Mar. 22, should outperform the market, says Kuvelkar. "We see substantial upside" from the current price, he says. What impresses Kuvelkar is Safeway's focus on operating margins, which have leaped from 1.6% in 2004 to 3.3% in 2005, and are estimated to hit 3.9% for the year 2006. That will translate into operating earnings of $1.64 a share in 2006, Kuvelkar figures, compared with $1.40 in 2005. The key to the chain's improved margins is keeping costs down in the face of rising fuel prices, he says. Safeway has also seen sales volume improve, thanks to its new "lifestyle" format at many of its 1,800 stores. The campaign offers better-quality products, such as natural and organic foods, and greets customers with a more pleasant store environment, according to analysts. Joseph Agnese of Standard & Poor's, who rates Safeway a "buy," lauds the improving sales trends, and he also points to restructured union contracts that will stabilize labor costs. Agnese says Safeway's valuation will improve as it continues to recover the business it lost after the September, 2004, strike in California.



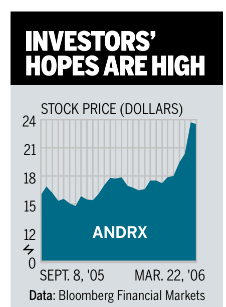
The Right Recipe At Bob Evans

INVESTORS ARE digging into shares of casual-dining operator Bob Evans Farms (BOBE), whose stock has popped from 22 in November to 29.89 now. "Its recipe for a turnaround appears solid," says David Sowerby, portfolio manager at investment firm Loomis Sayles, which owns shares. Sales at Bob Evans' 585 family-style restaurants in 19 states are on the rise. Profits in its most recent quarter nearly doubled from a year ago, owing to cost cutting, less price discounting, more advertising, and an improved menu. The company, with little Street coverage, beat earnings forecasts in the two previous quarters, notes Sowerby. He sees Bob Evans, which also makes sausages and other food products, sustaining its double-digit earnings growth next year, with the stock hitting 38. Jonathan Waite of KeyBanc Capital Markets, who tags the stock a "buy," forecasts earnings of $1.21 a share in 2006 (ending Apr. 30) and $1.45 in 2007, compared with $1.04 in 2005. He says the real upside will come from sales and fundamental improvements.



Andrx: Many Hurdles Before the Deal Is Done

GENERIC-DRUG MAKER ANDRX (ADRX) agreed on Mar. 13 to be acquired by Watson Pharmaceuticals, No. 3 in generics, for $1.95 billion, or 25 a share, all in cash. But MMI Investments, the biggest stakeholder, with 12.3%, plans to oppose the deal, which is still awaiting regulatory approval, and others could follow suit. Hours before the announcement, MMI had bought 420,000 shares at 20.96 to 21.60 apiece. When the news broke, "I was shocked," says MMI President Clay Lifflander, who had been buying almost weekly since December. Shareholders usually are overjoyed when a buyout takes place. But Lifflander says the timing is bad. In early September, the Food & Drug Administration halted the approval of new Andrx generics, estimated to have market potential of $2 billion, over questions on the Andrx production facilities. Lifflander says the FDA may lift the ban after another plant inspection. When that happens, the value of Andrx will skyrocket, he says, and the stock, now at 23.69, could be worth 40 in 12 to 18 months. "Andrx will have to convince me about the deal's advantage to shareholders." Amy Stevens of Susquehanna Financial Group, who rates Andrx "neutral," says "it remains a possibility the deal won't go through."



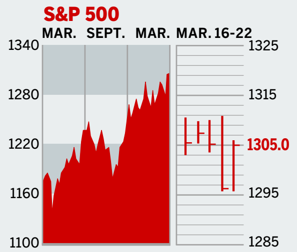
BusinessWeek online Gene Marcial's Inside Wall Street is posted at businessweek.com/investor at 5 p.m. EST on the magazine's publication day, usually Thursdays.

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.

PHOTOGRAPH BY ETHAN HILL; CHARTS BY ERIC HOFFMANN/BW

Personal Business Figures of the Week

STOCKS



COMMENTARY

The markets had a mixed showing as some blue-chips reported better-than-expected profits. Among the winners: Home Depot, JPMorgan Chase, and Marathon Oil. The gains pushed the Dow Jones industrial average to 11,317.4, a gain of 1% for the week. The Standard & Poor's 500-stock index rose 0.2%, and the tech-laden NASDAQ Composite fell 0.4%.

Data: Bloomberg Financial Markets, Reuters

U.S. MARKETS

	MAR. 22	% CHANGE WEEK	YEAR TO DATE	LAST 12 MONTHS
S&P 500	1305.0	0.2	4.5	11.4
Dow Jones Industrials	11,317.4	1.0	5.6	8.1
NASDAQ Composite	2303.4	–0.4	4.4	15.8
S&P MidCap 400	781.3	–0.1	5.9	18.6
S&P SmallCap 600	386.5	1.0	10.2	19.4
DJ Wilshire 5000	13,131.1	0.1	5.1	13.5

SECTORS

BusinessWeek 50*	769.4	–0.1	3.7	10.3
BW Info Tech 100**	392.9	0.2	3.3	13.0
S&P/Citigroup Growth	615.7	0.2	3.2	8.8
S&P/Citigroup Value	686.0	0.1	5.9	14.0
S&P Energy	395.0	–0.9	6.0	16.1
S&P Financials	444.5	0.4	4.2	17.1
S&P REIT	173.7	–0.7	13.5	31.8
S&P Transportation	275.9	0.5	10.4	22.0
S&P Utilities	160.6	–1.3	0.6	10.4
GSTI Internet	190.0	0.2	–7.4	23.8
PSE Technology	872.0	–1.1	4.3	20.5

*Mar. 19, 1999=1000 **Feb. 7, 2000=1000

GLOBAL MARKETS

	MAR. 22	% CHANGE WEEK	YEAR TO DATE	LAST 12 MONTHS
S&P Euro Plus (U.S. Dollar)	1680.4	1.2	11.2	19.6
London (FT-SE 100)	6007.5	0.7	6.9	21.7
Paris (CAC 40)	5194.8	1.3	10.2	28.4
Frankfurt (DAX)	5932.3	0.6	9.7	37.3
Tokyo (NIKKEI 225)	16,495.5	1.1	2.4	39.3
Hong Kong (Hang Seng)	15,642.8	–0.5	5.2	13.5
Toronto (S&P/TSX Composite)	11,970.7	–0.7	6.2	24.1
Mexico City (IPC)	19,598.1	3.1	10.1	50.0

FUNDAMENTALS

	MAR. 21	WEEK AGO	YEAR AGO
S&P 500 Dividend Yield	1.78%	1.78%	2.00%
S&P 500 P/E Ratio (Trailing 12 mos.)	18.0	18.0	19.9
S&P 500 P/E Ratio (Next 12 mos.)*	15.1	15.1	15.8
First Call Earnings Revision*	0.08%	–0.67%	0.50%

*First Call Corp.

TECHNICAL INDICATORS

	MAR. 21	WEEK AGO	READING
S&P 500 200-day average	1239.5	1236.9	Positive
Stocks above 200-day average	66.0%	67.0%	Neutral
Options: Put/call ratio	0.69	0.74	Neutral
Insiders: Vickers NYSE Sell/buy ratio	5.47	5.46	Negative

BEST-PERFORMING GROUPS

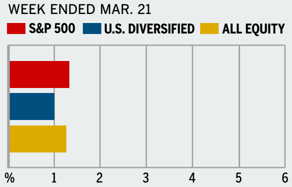
	LAST MONTH %		LAST 12 MONTHS %
Agricultural Products	13.6	Specialized Finance	59.1
Steel	12.7	Oil & Gas Refining	58.2
Constr. Materials	10.1	Human Rsrcs. & Emplmt.	56.2
Distillers & Vintners	9.0	Oil & Gas Equip.	55.4
Divsfd. Commercial Svcs.	8.8	Constr. Materials	52.5

WORST-PERFORMING GROUPS

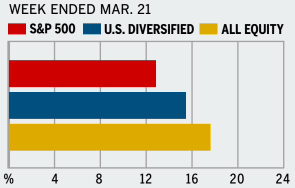
	LAST MONTH %		LAST 12 MONTHS %
Spclzd. Cnsmr. Serv.	–17.3	Automobiles	–26.3
Gold Mining	–16.3	Motorcycles	–16.6
Educational Services	–9.9	Broadcasting	–16.5
Homebuilding	–9.5	Diversified Chemicals	–14.6
Semiconductor Equip.	–7.9	Home Furnishings	–14.3

MUTUAL FUNDS

4-WEEK TOTAL RETURN
WEEK ENDED MAR. 21



52-WEEK TOTAL RETURN
WEEK ENDED MAR. 21



Data: Standard & Poor's

EQUITY FUND CATEGORIES

4-WEEK TOTAL RETURN	%	52-WEEK TOTAL RETURN	%
LEADERS		**LEADERS**	
Japan	5.1	Latin America	76.5
Diversified Pacific/Asia	4.5	Precious Metals	48.1
Real Estate	3.5	Diversified Emerg. Mkts.	44.1
Foreign	3.5	Japan	34.0
LAGGARDS		**LAGGARDS**	
Precious Metals	–2.6	Domestic Hybrid	9.5
Natural Resources	–2.6	Miscellaneous	10.9
Utilities	–1.3	Large-cap Blend	12.5
Latin America	–0.9	Large-cap Value	12.6

EQUITY FUNDS

4-WEEK TOTAL RETURN	%	52-WEEK TOTAL RETURN	%
LEADERS		**LEADERS**	
American Heritage	12.5	ProFunds Ultra Japan Inv.	91.2
ProFds. Sh. Prc. Mtls. Inv.	9.2	ING Russia A	86.3
Eaton Vance Grtr. India A	8.3	T. Rowe Price Latin Am.	79.9
Turnaround	7.9	Fidelity Latin America	76.8
LAGGARDS		**LAGGARDS**	
Ameritor Investment	–16.7	Ameritor Investment	–68.8
ProFunds Prc. Mtls. Inv.	–13.7	American Heritage Grth.	–33.3
Rydex Precious Metals	–5.9	Potomac Sm. Cap/Sh. Inv.	–32.0
AIM Gold & Prc. Mtls. Inv.	–5.5	ProFds. USh. Sm. Cap Inv.	–30.6

INTEREST RATES

KEY RATES

	MAR. 22	WEEK AGO	YEAR AGO
Money Market Funds	4.13%	4.09%	2.21%
90-Day Treasury Bills	4.68	4.61	2.86
2-Year Treasury Notes	4.74	4.68	3.83
10-Year Treasury Notes	4.70	4.73	4.64
30-Year Treasury Bonds	4.72	4.75	4.91
30-Year Fixed Mortgage †	6.25	6.28	5.93

†BanxQuote, Inc.

BLOOMBERG MUNI YIELD EQUIVALENTS

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

	10-YR. BOND	30-YR. BOND
General Obligations	3.93%	4.34%
Taxable Equivalent	5.61	6.20
Insured Revenue Bonds	4.00	4.53
Taxable Equivalent	5.71	6.47

THE WEEK AHEAD

FOMC MEETING *Tuesday, Mar. 28, 9 a.m. EST* » The Federal Reserve's Open Market Committee meets for two days to discuss monetary policy. This will be the first meeting for new Chairman Ben S. Bernanke. The unanimous view among economists surveyed by Action Economics is that the central bank will move the fed funds rate up, from 4.5% to 4.75%.

CONSUMER CONFIDENCE *Tuesday, Mar. 28, 10 a.m., EST* » The Conference Board's March consumer confidence index most likely edged up to 102 after easing to 101.7 in February. Consumer expectations about future economic conditions drove the February decline.

PERSONAL INCOME *Friday, Mar. 31, 8:30 a.m. EST* » Personal income probably increased 0.4% in February after a healthy gain of 0.7% in January. Consumer spending is forecast to have ticked up 0.1% in February. January spending shot up 0.9% on stronger auto sales and balmy temperatures.

FACTORY INVENTORIES *Friday, Mar. 31, 10 a.m. EST* » Manufacturing inventories most likely rose by 0.2% in February. In January, inventories grew by 0.5%. The inventory-to-sales ratio remains at a record low, which should prompt some additional factory activity.

The BusinessWeek production index eased to 269.4 for the week ended Mar. 11 but stood 12.9% above the year-ago level. Before calculation of the four-week moving average, the index inched up to 269.1.

BusinessWeek online

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

Index

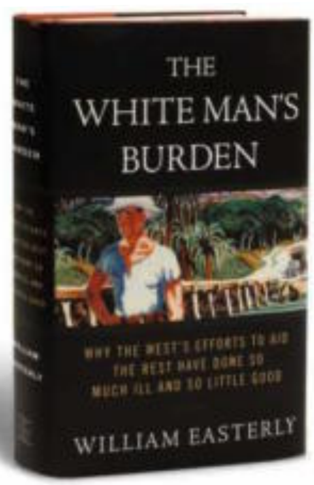
The Companies

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.

Throwing Money–and Missing

THE WHITE MAN'S BURDEN **Why the West's Efforts to Aid the Rest Have Done So Much Ill and So Little Good**
By William Easterly; Penguin Press; 436pp; $27.95

The international development community is still reeling from William Easterly's 2001 book, *The Elusive Quest for Growth*. In it, the former top World Bank economist demonstrated how the panaceas concocted by the West to save the Third World, such as huge injections of aid, conditional loans, population control, infrastructure spending, and debt forgiveness, have all failed to stimulate sustainable growth and cut poverty.



Easterly is at it again. In *The White Man's Burden*, he marshals a wealth of fresh studies, original statistical analyses, his own anecdotal reporting, and historical precedents to buttress his argument that today's foreign-aid system doesn't work. He shreds practically every new strategy by the World Bank, International Monetary Fund, U.N. agencies, and other donors aimed at lifting the world's poor out of misery. This book is disappointingly skimpy on solutions, but it is brilliant at diagnosing the failings of Western intervention in the Third World.

The real tragedy, says Easterly, isn't Western indifference toward the human crises in Africa and elsewhere, as many advocates of huge aid hikes claim. The problem is the development community's miserable record of treating the most basic needs of the poor. The West "spent $2.3 trillion on foreign aid over the past five decades and still has not managed to get 12¢ medicines to children to prevent half of all malaria deaths." Throwing greater sums at the problem under the existing system will actually be detrimental because "the current wave of enthusiasm for addressing world poverty will repeat the cycle of its predecessors: idealism, high expectations, disappointing results, cynical backlash." So before digging further into their wallets, rich donors should demand hard results and hold international aid agencies accountable.

Easterly's 16 years as a World Bank economist and his broad experience in developing nations make the critiques hard to dismiss. He is as harsh on U.S. conservatives as on free-spending liberals. He blasts the Bush Administration's antipoverty programs as naive and poorly conceived. He rips into the President's much-ballyhooed African AIDS initiative because it focuses mainly on expensive drugs while discouraging the use of condoms, whose widespread application could save many more millions of lives. He also ridicules neoconservatives who believe the U.S. can make poor failed states better places by forcibly removing dictators and imposing democracy and free-market economics.

Yet the author admits he has no big answers of his own. In fact, he says he's allergic to anything smacking of ambitious planning. The fatal flaw of big aid initiatives, he writes, is that they derive from rich Westerners' utopian agendas rather than input from the needy. Another problem with broad, collective goals is that no one agency bears responsibility for achieving anything concrete.

Instead, Easterly advocates "piecemeal interventions." For instance, donors should fund well-focused projects created by "seekers," highly motivated individuals who find creative ways to solve real-world problems. He profiles many grass-roots success stories that deserve help, from a private college in Ghana to an Indian outfit that cut HIV incidence by working with prostitutes. Aid agencies should focus on specific tasks, such as building roads and clinics or providing textbooks. Independent auditors should scrutinize sample projects in the field to see if they are delivering results. Poor villagers ought to decide for themselves what they need, receive cash vouchers supplied by donors, and use these to hire the most effective agencies to provide what's wanted.

These are great ideas. But would hundreds of thousands of independent microprojects really make a bigger impact—or be more cost-effective and freer of abuse—than if such efforts were coordinated through existing channels? More to the point, well-off, conscientious Westerners are unlikely to sit by and watch millions of Africans die of preventable causes as they wait for verifiably waste-free aid projects to materialize.

Easterly nails how Western aid fails to cut poverty, but he's short on solutions

Easterly's book also has some glaring omissions. What to make, for example, of the immense foundations guided by tycoons such as Bill Gates that aim to bring the focused, results-based methods Easterly advocates into the war on AIDS, tuberculosis, malaria, and other diseases? Nobody would label Gates a central planner, but he does believe in international coordination, high goals, and big expenditures. Surprisingly, the Bill & Melinda Gates Foundation isn't mentioned in this book.

Easterly's thesis may be overstretched. Still, he is right that we should be tough on aid agencies that don't deliver. *The White Man's Burden* is disturbing but essential reading for would-be Samaritans—and a powerful call for reform.

–By Pete Engardio

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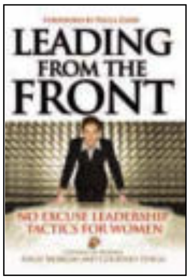
Leading From the Front



Co-founders of a successful leadership consulting firm, Angie Morgan and Courtney Lynch have helped hundreds of business women achieve their goals. Former U.S. Marine Corps Captains, the authors reveal 10 key practices to help transform readers into respected and efficient leaders.

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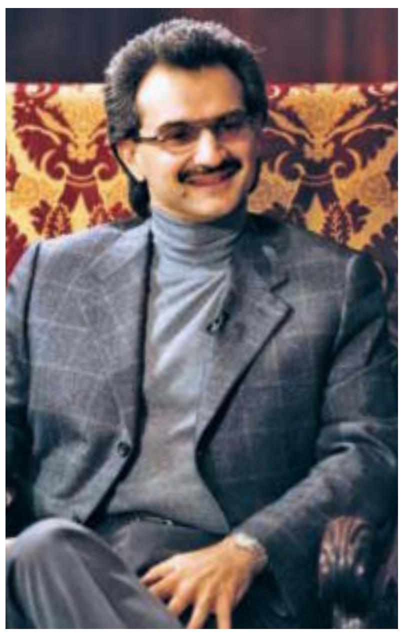
For Citi, 'No More Excuses'

SAUDI PRINCE ALWALEED bin Tal Alsaud, with a net worth estimated at almost $21 billion, is one of the world's richest men. But he is no passive prince, sitting back while the oil billions roll in. Alwaleed, 48, is an active investor, with stakes in Apple, Disney, Citigroup (with some $10 billion invested), and others. On Mar. 17 he announced that he would float an initial public offering for 30% of his holding company, Kingdom Holdings. The Prince, who was in Riyadh and spoke with me by phone, is a savvy businessman and a close observer of Middle East politics.



Lets talk about one of your big holdings, Citigroup. Several of the company's largest holders have recently been net sellers. What does [CEO] Chuck Prince need to do?
I met with Sandy Weill and Chuck Prince a month ago at the George V Hotel in Paris, and we discussed the promise from Chuck that he will deliver good results. If I can quote him, he said: "Prince, we have put the big problems of Citi behind us, and we have to move our shares to above 50."

So how long a grace period are you giving Chuck Prince?
The grace period is over. You can quote me on that. Right now we are looking to the results in the next few weeks and...I have full confidence that [Citi] will deliver. This is the No. 1 company in the world. It has equity of $400 billion and assets of $1.4 trillion. So no more excuses....Excuses are finished. Now we are at war. Citigroup has won the internal war by cleaning up all the Enron residuals, WorldCom, the European scandal. Now we have to win the external war...make good investments...and that should lift the price of the stock. That's it. I told him, as [Citi's] biggest shareholder, we have to win the external war. Thank you, Mr. Chuck Prince. Now, the Prince of Saudi Arabia tells the Prince of New York: Go to war, and I am backing you 100%.

Do you think the U.S. is taking a turn toward protectionism?
Let's not read too much into the Dubai Ports situation: Congress went into protectionist mode, but President Bush was willing to let the deal go through. If this is an isolated incident, then fine. But if the U.S. discourages foreign investment, then we can see an impact. Obviously the U.S. cannot afford to close its borders to debt and equity since foreigners are financing its debt. The reaction was not positive. Arab investors did not like the situation, and they are monitoring it very closely.

What kinds of investments may go elsewhere?
Already we are seeing a lot of money coming back to Saudi Arabia and being kept in the system. If the U.S. Administration and Congress keep vetoing foreign investment, obviously foreigners will go somewhere else. But I don't think it will happen. I hope we will see open deals.

You have asked the Saudi government to make some changes to enable investment there. Do you think it will happen?
The problem is that foreigners are not allowed to invest in the Saudi market, although they are allowed to invest in funds held by banks. Saudi Arabia has to begin selling parts of its holdings to the public...and not hold 70% of everything. They have to let foreigners invest in Saudi stocks. They have to continue to encourage the process of IPOs. And they have to expedite the process of teaching the public how to invest.

Let's talk about Iraq. What will be the impact of a civil war in Iraq?
In Iraq, what you are seeing is complete destabilization of the situation and the beginning of, God forbid, the seeds of a war between the Shiites and the Sunnis that could destabilize the whole region. Remember, you have Shiites all over the region: in Kuwait, Lebanon, Jordan.... So it's a very serious situation. Although we are not happy to have [U.S.] troops in Iraq now, it's too early for the U.S. to pull out.

What do you make of Hamas' victory in the Palestinian territories?
Honestly speaking, people look at it negatively, but I do not. I think that Hamas will come into the political system. [You could compare] Hamas to the IRA in Ireland. ■

Maria Bartiromo is the host of CNBC's Closing Bell.

(TOP TO BOTTOM) PHOTOGRAPH BY CRAIG BLANKENHORN/NBC UNIVERSAL; OWEN FRANKEN/BLOOMBERG NEWS

IdeasOutside Shot

BY DAVID HUETHER

The Case of the Missing Jobs

Manufacturing in America is producing and exporting more goods than ever before. In 2004 and 2005, manufacturing's expansion easily outpaced that of the larger U.S. economy. Yet after losing 1.5 million jobs during the 2001 recession, manufacturing has shed another 1.5 million workers—even as the rest of the economy has since added more than 5 million new jobs.

What's going on here? Why is manufacturing employment, at 14.2 million workers, at its lowest level in more than 50 years while manufacturing output is at an all-time high?

Some blame the outsourcing of American factory jobs to rapidly industrializing low-cost countries such as China and India. Others fault our growing trade deficit. And some posit that the current manufacturing recovery has not generated as robust a demand for U.S. goods as have previous post-recession upturns. But none of these interrelated factors has influenced manufacturing employment nearly as much as has continuously strong productivity growth.

Since 2001, with the aid of computers, telecommunications advances, and ever more efficient plant operations, U.S. manufacturing productivity, or the amount of goods or services a worker produces in an hour, has soared a dizzying 24%. That's 72% faster than the average productivity advance during America's four most recent recession-recovery cycles dating back to the 1970s. In short: We're making more stuff with fewer people.

U.S. manufacturing has for decades been the world leader in the productivity gains that drive living standards higher. But more recently, practically every manufacturing economy around the globe has posted strong productivity gains and experienced job losses as a result. Although you'll never hear it reported by protectionist pundits, China has actually lost more manufacturing jobs than America since 2000, with 4.5 million jobs gone vs. 3.1 million in the U.S. Among the top 10 industrialized economies (the U.S., Japan, Germany, China, Britain, France, Italy, Korea, Canada, and Mexico), which represent 75% of world manufacturing output, only Italy managed not to lose factory jobs since 2000.

Slower output growth and sizzling productivity have curbed factory job creation

It's certainly true that U.S. manufacturers face stiff competition in low- and mid-tech products from increasingly capable global rivals. Our trade deficit is a reflection of those competitors' collective capacity to deliver affordable consumer products to America and other international markets. But it's also true that persistently slow economic growth in Japan and Europe has limited demand for U.S.-made goods and thus worked to lower post-recession output from American plants, as did the uncertainties caused by the September 11 attacks, corporate scandals, and the buildup to war in Iraq during the early stages of our current expansion.

So, contrary to popular belief, it has been this lower demand and output, coupled with high productivity growth, that has conspired to depress the kind of manufacturing job creation we might otherwise have expected since 2002.

U.S. manufacturing output has increased a welcome 13% since the end of 2001. [It continues to grow: See page 27.] But that growth is barely half the average increase during the initial four years of the previous four recoveries. Remember, our manufacturing productivity has increased significantly faster than in earlier recoveries. You don't have to be an economist to see how this combination of far slower output growth and much higher productivity has been very bad for employment. Indeed, if manufacturing output and productivity growth rates during the current recovery had equaled those averaged during the previous four upturns, U.S. manufacturing would have created 3 million more jobs than it has, and employment would have recovered to its pre-recession level of 17.2 million by the end of 2005.

Fortunately, demand for American-made products has increased, and manufacturing's output has grown at a solid 4.8% annual pace during the past two years. Because that figure almost matched manufacturing's 5.1% productivity growth, factory employment has remained relatively stable. But U.S. manufacturers aren't about to invest any less in productivity improvements in future years. International competition won't let them. Looking ahead, the number of manufacturing jobs we create or lose will depend entirely on the global demand for U.S.-made products.

David Huether *is chief economist at the National Association of Manufacturers.*

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