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# The global crisis of institutional legitimacy

August 22, 2011 @ 2:21 am

By Felix Salmon

While watching another Arab government get toppled on Sunday evening — this time that of Muammar Gaddafi, in Libya — I was also reading George Magnus's excellent note for UBS, entitled "The Convulsions of Political Economy"; you can find it *chez* [Zero Hedge](#) <sup>[1]</sup>.

Convulsions is right — not only in the Arab world, of course, but also in Europe and the US. And the result is arguably the most uncertain outlook, in terms of the global political economy, since World War II ended and the era of the welfare state began.

As Magnus says:

It seems that we are having sometimes esoteric tiffs between Keynesians and Austrians about if and how governments should sustain jobs and growth. But, deep down, we are having a much more significant debate as we are being forced to redefine what we think about the rights and obligations of citizens and the State.

Most fundamentally, what I'm seeing as I look around the world is a massive decrease of trust in the institutions of government. Where those institutions are oppressive and totalitarian, the ability of popular uprisings to bring them down is a joyous and welcome sight. But on the other side of the coin, when I look at rioters in England, I see a huge middle finger being waved at basic norms of lawfulness and civilized society, and an enthusiastic embrace of "going on the rob" as some kind of hugely enjoyable participation sport. The glue holding society together is dissolving, whether it's made of fear or whether it's made of enlightened self-interest.

In Europe, the speed with which the transmission has been thrown violently into reverse is nothing short of astonishing. The whole second half of the 20th Century was devoted to building strong European institutions which would maximize cooperation and minimize mistrust and finger-pointing between member states. Great statesmen put European unity on a par with narrow national self-interest, and the resulting institutions — the euro, of course, but also things like the Schengen Agreement and the European Convention on Human Rights — transformed the blood-soaked continent of the 1940s into a peaceful and prosperous model for how disparate countries could successfully work together to the benefit of them all.

And the US, of course, the global hegemon, a continent unto itself, stood as a beacon for the rest of the world: 300 million disparate people coming together to create something unprecedented — an economic, political, and military colossus built on solidly democratic principles. *E pluribus unum*.

But countries and institutions can ultimately survive only with the will and consent of those they govern — and that consent is evaporating around the world. Europeans have no love for Europe's institutions, be they the euro or the ECB or the EFSF. Unemployment, in much of Europe, has reached the point of no return — the point at which it becomes endemic, stubbornly immune to attempts to tackle it. In turn, that results in broad-based cynicism and disillusionment when it comes to politics and politicians generally.

And then on this side of the pond we have Rick Perry — harbinger and prime example of the way in which mistrust in federal institutions has moved from the fringe to the mainstream. Indeed, what we see with Perry is far more than mistrust — he actually denies most federal institutions their existential legitimacy, and has written a [book](#) <sup>[2]</sup> explaining at length how everything from Social Security to federal bank regulation is in fact unconstitutional.

When Perry [accuses](#) <sup>[3]</sup> Ben Bernanke of treachery and treason, his violent rhetoric ("we would

treat him pretty ugly down in Texas”) is scary in itself. But we shouldn’t let that obscure Perry’s substantive message — that neither Bernanke nor the Fed really deserve to exist, to control the US money supply, and to work towards a dual mandate of price stability and full employment.

For the first time in living memory, someone with a non-negligible chance of winning the US presidency is arguing not over who should head the Fed, but whether the Fed should even exist in the first place.

Looked at against this backdrop, the recent volatility in the stock market, not to mention the downgrade of the US from triple-A status, makes perfect sense. Global corporations are actually weirdly absent from the list of institutions in which the public has lost its trust, but the way in which they’ve quietly grown their earnings back [above pre-crisis levels](#) <sup>[4]</sup> has definitely not been ratified by broad-based economic recovery, and therefore feels rather unsustainable. Meanwhile, the USA itself has undoubtedly been weakened by a shrinking tax base, a soaring national debt, a stretched military, and a legislature which has consistently demonstrated an inability to tackle the great tasks asked of it.

It looks increasingly as though we’re entering Phase 2 of the global crisis, with 2008-9 merely acting as the appetizer. In Phase 1, national and super-national treasuries and central banks managed to come to the rescue and stave off catastrophe. But in doing so, they weakened themselves to the point at which they’re unable to rise to the occasion this time round. Our hearts want government to [come through and save the economy](#) <sup>[5]</sup>. But our heads know that it’s not going to happen. And that failure, in turn, is only going to further weaken institutional legitimacy across the US and the world. It’s a vicious cycle, and I can’t see how we’re going to break out of it.

**Update:** [emptywheel](#) <sup>[6]</sup> responds.

**Update 2:** as does [Ezra](#) <sup>[7]</sup>.

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# The future of online advertising

November 14, 2011 @ 6:24 am

By Felix Salmon

I gave a talk on Thursday at the [AppNexus Summit](#) <sup>[1]</sup> in front of a few hundred digital advertising types. The first part of the talk was a macro overview, but when the Q&A session started, all that anybody wanted to talk about was my take on online media. And given how granular the discussions over the course of the rest of the day were going to be, I wanted to push back a bit against some of the unexamined assumptions which I encounter most of the time when I meet online-media people.

The first is that there's something necessary and inevitable about ad-driven models dominating the online media industry. That's certainly how things have worked out to date, but there was nothing inevitable about it. From the very early days of the World Wide Web, many extremely smart people pushed very hard to develop a workable micropayments architecture online. Ads looked like a non-starter: as Gary Wolf put it in his [history](#) <sup>[2]</sup> of *Wired*, "the computer screen was low resolution; the ads themselves were tiny, and they disappeared as soon as the user scrolled down". A few sponsors would buy ads in order to understand the new medium, but there was never anything particularly promising in online banners.

Meanwhile, people were happily paying small sums for newspapers, for magazines, for coffee, for any number of fast-moving consumer goods. And websites were about as fast-moving a consumer good as the world had. A simple and painless online payments system was clearly the way that the web was going to make money. The only problem was — and is — that the payments world is old, and slow, and very resistant to change; rumor has it that Mastercard actually twisted Marc Andreessen's arm so that he would remove his <payments> tag from the early versions of the Mozilla browser.

With the US payments system being stuck on ACH for the foreseeable future, payments online have been clunky and unwieldy, based around expensive and cartelized credit-card transactions; the only real competitor, PayPal, is a for-profit company, a wholly-owned subsidiary of eBay which doesn't clear at par and which has many other obstacles to being adopted as a broad-based payments architecture.

So one of the big reasons why online advertising has done so well is simply the negative one: online micropayments were a disaster, and never took off. But they're much more compelling as a business model, and there's a decent chance that at some point in the future the financial system as a whole is going to get its act together and put together something which actually works and which people are happy to adopt. At which point, the online ad industry will face a major threat.

My second point was that black-hat SEO advertisers, like the ones who got in touch with [Hamilton Nolan](#) <sup>[3]</sup> last month, do at least serve one purpose: they show just how valuable simple links — as opposed to expensive branded ad campaigns — can be. Hamilton was being asked to insert links into blog posts he was writing; more recently, I got an email from someone named "Whitney Meyer" offering me \$50 every time I added a link to an *old* post of mine. Google's PageRank algorithm is a lot more sophisticated than it used to be, but the fact is that it still gives enormous weight to who's linking to whom, for very good reason. Links are what the web is built on, and a large part of why it's so incredibly powerful and popular.

Finally, after the obligatory plug for [Counterparties](#) <sup>[4]</sup>, I laid out my vision of what online advertising could be. Check out the front page of [Reuters.com](#) <sup>[5]</sup>: we have what is basically an ad unit at the bottom of the right-hand column which acts as an ad for Counterparties. It's got Counterparties branding, but the meat of it is four links to four different external sites. (As I write this, they're the NYT, the Guardian, the Economist, and the Huffington Post.) We *want* you

to click on those links; when you do, you leave Reuters.com, and you don't go to Counterparties.com. Instead, you go directly to HuffPo, or wherever. Reuters gets no traffic when you click on that link: indeed, we're sending you away. That's a *good* thing: we're providing a valuable service for our readers, pointing them to great content. If you believe in putting the audience's needs first, this kind of thing is a no-brainer.

What we have cobbled together is something really rather novel: an ad unit that smart readers actually *want* to click on. I've been looking at ads online for over 15 years now, and I've never wanted to click on one, with the exception of a handful of very bloggish sponsored posts at Gawker Media, which were interspersed seamlessly between inferior original editorial posts. It's a known fact in advertising circles that only idiots click on ads — and yet advertisers still think that click-through rates mean something, and that a higher click-through rate means a better ad. It's the measurement fallacy: people tend to think that what they can measure is what they want, just because they can measure it. And it's endemic in the online advertising industry.

In fact, with very few exceptions, I've never even wanted to *look* at online ads: its quite astonishing, the degree to which we've collectively trained ourselves to ignore ads when we bring up a web page. And what that says to me is that online advertising is missing something really huge.

At one point in the Q&A session, I asked the audience to raise their hands if they read *Vogue* magazine; maybe three or four people, in a crowd a hundred times that size, did so. Most of the people in the audience literally *didn't know* that when people buy *Vogue*, they *want* to read the ads; in a very real sense, the editorial is something which just gets in the way.

Leaf through a glossy fashion magazine like *Vogue*, and you'll find dozens of pages of ads at the front of the book, with basically zero editorial content to break them up. If advertisers thought that readers only looked at ads insofar as they were adjacent to editorial, then they would ask for placement opposite editorial. But that's not what happens: the ads all cluster at the front, the editorial gets relegated to the back, and readers spend more time looking at ads than they do looking at editorial features. In fact, the most avid readers of the editorial shoots are the *advertisers*, who use them for ideas when they're planning their next campaign.

*Vogue* is a prime example of the power of advertising: if, as an advertiser, you know how to give people something they want, then you don't need to rely on second-best stratagems like adjacency. And no one ever clicked on an ad in *Vogue*. Which is one reason why Gawker's former ad chief Chris Batty once proposed that all ads on Gawker Media should be images only, and not clickable at all — it would force advertisers to create something good, instead of chasing after clicks from idiots.

Because it's so easy to measure things like impressions and click-through rates, the online ad industry has missed the real power that advertising can have, and its practitioners tend to sneer at old-media ad money as being largely wasted, in contrast to the carefully quantified campaigns one sees online. One questioner at the conference proposed that ad spend could soon be counted simply as a cost of goods sold in accounting statements, since technology had made the relationship between adspend and sales so transparent.

But there's something very powerful about brand advertising — something which helps explain why so much more money still gets poured into TV ads rather than online campaigns. Part of it is that TV ads are glossier and more self-contained, not competing for attention with simultaneous editorial content. And another part of it is that Americans have demonstrated quite clearly that they prefer lean-back to lean-forwards: cable TV is still a higher priority for the vast majority of the country than is broadband access. And the content they prefer to ingest in a lean-back way includes advertising.

So what's an advertiser to do, online? My idea is to move away from the idea of getting people to click on ads, but at the same time to treat with suspicion the idea that it's possible to deliver a beautiful, self-contained brand proposition online in the same way that you can in *Vogue* or on TV.

Instead, take a leaf out of the book of sites which really have generated a huge amount of loyalty online — sites like Drudge, or Reddit, or Techmeme, or Fark, or any number of other aggregators and curators with enormous followings. Millions of people *love* these sites, and visit them with astonishing regularity. Why? Because they send them to fantastic third-party content.

It's easy to create an ad unit which is primarily links to third-party sites; I'm sure with a bit of

effort and creativity you could put one together which is even better than the Counterparties unit on Reuters.com. Start placing that ad over the web, and people will, for the first time, actually have a reason to want to look at your ad; when they see it, they're even likely to click on it! Sure, that click won't take them to your site — but it's still a great measure of engagement. And they will love you for sending them to great content.

And what if it's too hard for you to put together a dynamically-updated list of great content to link to? In that case, you could always ask the people who do it well if they'd be willing to put together a white-label version of their own links for you. [The Browser](#)<sup>[6]</sup> might be a good place to start — or you could even ask us at Counterparties. And our partners at [Percolate](#)<sup>[7]</sup> are already doing something similar for corporate clients. Here's how they put it:

In a digital world, we believe brands can be signals. Pointing consumers to valuable information that is not necessarily about the brand directly, but speaks to the brand promise and consumer mindset.

I'm not saying that online advertisers should drop everything and just start linking to third-party sites. But I *am* saying that it's worth a try — it's an idea worth experimenting with. If you do it, and you start getting lots of positive feedback from consumers, you're probably doing something right. And you might just have discovered a way to build your brand online, even if you're not necessarily a particularly digital company.

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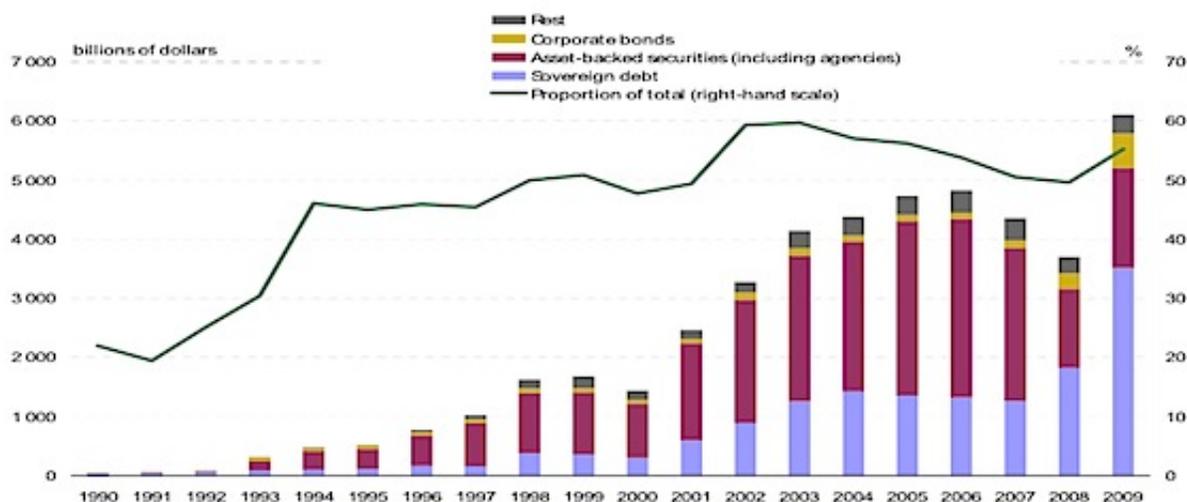
## The horrifying AAA debt-issuance chart

July 15, 2011 @ 3:06 pm

By Felix Salmon

[This](#) <sup>[1]</sup> is why I love FT Alphaville in general and Tracy Alloway in particular: she'll dutifully read 14 pages into something [entitled](#) <sup>[2]</sup> "The Basel Committee on Banking Supervision Joint Forum Report on Asset Securitisation Incentives" before coming across this chart and immediately realizing just how important it is.

World issue of AAA fixed-income



Source: Dealogic and CNMV. (1) The category "others" includes mortgage bonds, preferred shares and other long-term fixed-income instruments.

I've put a bigger version [here](#) <sup>[3]</sup> for people who want to pass it around in all its horrifying glory, but it's also worth spelling things out, because it might not be immediately obvious.

The big-picture thing to remember when looking at this chart is something which I've [said](#) <sup>[4]</sup> many times before — that it wasn't an excess of greed and speculation which led to the financial crisis, but rather an excess of overcaution, with an attendant surge in demand for triple-A-rated bonds. On a micro level, triple-A securities are safer than any other securities. But on a macro level, they're much more dangerous, precisely because they're considered risk-free. They breed complacency and regulatory arbitrage, and they are a key ingredient in the cause of all big crises, which is leverage.

At the left-hand side of the chart we see that global issuance of triple-A bonds was more or less nonexistent back in the early 90s. All those Treasury bonds, all those agency securities from Fannie and Freddie, all that Japanese debt — add it all up, and it still comes to essentially zero by the standards of what seems normal today. Check out the left-hand y-axis: it goes up in *\$1 trillion* increments. And we're not talking stock, here, we're talking flows: this chart is issuance *per year*.

(It's pretty easy to see, looking at this chart, how a company like Pimco can find itself with over \$1 trillion in assets under management: that's now just a small fraction of the bonds issued

each year.)

Now zoom back, and look at the chart as a whole: it's going up and to the right, which says two things. Firstly, the amount of debt in the world is soaring. That's a bad thing, because debt is much more systemically dangerous than equity. And secondly, the amount of triple-A debt in the world is soaring as well. Which is a worse thing, because triple-A debt is much more systemically dangerous than most other debt.

Then look at the green line. Triple-A debt wasn't a huge part of the bond market back in the early 90s, but for the past decade it has invariably accounted for somewhere between 50% and 60% of total global fixed income issuance. That's possibly the most horrifying bit of all: it simply defies credulity for anybody to be asked to believe that more than half the bonds issued in any given year are essentially free of any credit risk.

Finally, look at the way that the maroon bars — structured products, basically — have given way to a scarily large purple bar at the far right of the chart. That's sovereign debt, and it tells you all you need to know about where the next crisis is likely to come from.

In a nutshell, triple-A debt is dangerous; there's far too much of it; its growth seems out of control; and the triple-A problem has now become a sovereign-debt problem, in a world where sovereign-debt crises are the most damaging crises of all.

All that said, there are two things worth bearing in mind which make the chart slightly less horrific. The first is that for reasons I don't understand, the chart ends in 2009, a crisis year when sovereigns pulled out all the stops in their attempt to prevent a global Depression. We're more than halfway into 2011 at this point, there's no good reason why the chart couldn't include 2010 as well. And that might show 2009 as being a bit of an aberration. Does anybody have the numbers for total triple-A bond issuance in 2010, and how much of that was sovereign?

And secondly, any kind of debt-issuance chart is likely to go up and to the right to some extent, just because borrowing needs never go away, and old debt needs to get rolled over. The total stock of triple-A debt isn't increasing by this many trillions of dollars per year, and it would be great to see a second chart of how much that is increasing, and how much of it is sovereign.

Still, flows matter. If sovereigns start being downgraded from triple-A status, debt is going to get a lot more expensive, and those rollovers — which cost very little in the current interest-rate environment — will really start to bite. And the invidious thing about debt is that it doesn't go away. Deleveraging is painful, and is often accompanied by inflation or default. And the more debt you have to start with, the more painful deleveraging is going to be. Prepare yourselves.

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## Don't ignore Tim Cook's sexuality

August 25, 2011 @ 7:47 pm

By Felix Salmon

[Tim Cook](#) <sup>[1]</sup> is now the most powerful gay man in the world. This is newsworthy, no? But you won't find it reported in any legacy/mainstream outlet. And when the *FT*'s Tim Bradshaw did no more than broach the subject in a single [tweet](#) <sup>[2]</sup>, he instantly found himself [fielding](#) <sup>[3]</sup> a barrage of responses criticizing him from so much as mentioning the subject. Similarly, when Gawker first reported Cook's sexuality in January, [MacDailyNews](#) <sup>[4]</sup> called their actions "petty, vindictive, and just plain sad."

But surely this is something we can and should be celebrating, if only in the name of diversity — that a company which by some measures the largest and most important in the world is now being run by a gay man. Certainly when it comes to gay role models, Cook is great: he's the boring systems-and-processes guy, not the flashy design guru, and as such he cuts sharply against stereotype. He's like Barney Frank in that sense: a super-smart, powerful and non-effeminate man who shows that being gay is no obstacle to any career you might want.

One of the issues here is that most news outlets cover Cook as part of their Apple story, and Cook's sexuality is irrelevant to his role at Apple. And so the other story — the fact that the ranks of big-company CEOs have just become significantly more diverse — is being overlooked and ignored. And that's bad for the gay and lesbian community more broadly.

The institution of the closet is one of fear — one where people would rather be ignored than noticed, because they fear the negative repercussions of being known to be gay. It's an institution which Cook, like any gay man born in 1960, knows at first hand. But now the risk of being ignored is bigger in the other direction: if the world can't see gay men and women in all their true diversity, if the only homosexuals they know of are the flamboyant ones on TV, then that only serves to perpetuate stereotypes.

As the Apple story moves away from being about Steve Jobs and becomes much more about Tim Cook, we're going to see a lot of coverage of Cook, the man. He is, after all, not just one of the most powerful gay men in the world; he's one of the most powerful *people* in the world, period. The first instinct of many journalists writing about Cook will be to ignore the issue of his sexuality. It's not germane to his job, they're only writing about him because of the job he holds, and therefore they shouldn't write about it.

On top of that, Cook is not exactly open about his sexuality, and Apple has never said anything about it. Cook's formative years, professionally speaking, were the 12 years he spent at IBM between 1982 and 1994 — and at that company, in those days, coming out was contraindicated from a career-development perspective. Mike Fuller, a gay VP at IBM, [told](#) <sup>[5]</sup> the *Advocate* in 2001 that he knew "IBM employees who worked for the company in the 1980s who told me they left IBM because they weren't comfortable coming out at work"; this comes as little surprise. After all, the years that Cook spent at straight-laced IBM coincided with the height of the AIDS panic, when people were worried about sharing toilet seats with homosexuals. It would be hard to come out at *any* company in that kind of atmosphere.

But thankfully we've moved a very long way from those days. Homosexuality is no longer something shameful, to be coy or secretive about — especially not when you've risen to the very top of your profession. In fact, it's incumbent upon a public-company CEO *not* to be in the closet.

Four years ago — a long time itself, in the history of gay rights and public acceptance thereof — John Browne resigned as CEO of BP under a shameful cloud. The reason for his downfall was not that he was gay, but rather that he was in the closet. As I [explained](#) <sup>[6]</sup> at the time, in

trying desperately to remain comfortably in the closet, he ended up lying repeatedly to the UK High Court – and that is why he had to resign.

Back then, there were no public-company CEOs on Out magazine's gay power list; this year, [Cook topped the list](#) <sup>[7]</sup> even before he became CEO of Apple. Keeping his sexuality a secret is no longer an option. And so the press shouldn't treat it as though it's something to be avoided at all costs. There's no ethical dilemma when it comes to reporting on Cook's sexuality: rather, the ethical dilemma comes in *not* reporting it, thereby perpetuating the idea that there's some kind of stigma associated with being gay. Yes, the stigma does still exist in much of society. But it's not the job of the press to perpetuate it. Quite the opposite.

: For a better and more heartfelt version of this post, read [Joe Clark](#) <sup>[8]</sup> from back in February: "When you tell us it's wrong to report on gay public figures," he writes, "you are telling gays not to come out of the closet and journalists not to report the truth."

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