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Germany revives athlete schools in a quest for gold

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Risky consumer stocks may be key to a U.S. rebound

MONEY & INVESTING | PAGE 19

What's News—

Business & Finance

U.S. productivity has grown at an estimated annual rate of 2.5% so far this year, defying the usual behavior of going up in good times and down in bad. U.S. unemployment in July hit a four-year high and job losses continued for the seventh consecutive month. Pages 1, 11

■ **Investors may wager** on European government debt and sell U.S. Treasurys, betting on a narrowing yield gap. Page 1

■ **British Energy and EDF** are holding out hope their marriage can still happen despite its collapse last week. Page 3

■ **Siemens is selling** an 80.2% stake in its cordless handset unit, its last remaining telecom-equipment business. Page 4

■ **Hedge funds seem** set to post their worst monthly performance in six years, as successful strategies run into trouble. Page 1

■ **Manufacturing contracted** in most of the euro zone as tight credit and high oil prices stoked recession fears. Page 11

■ **GM posted a net loss** of $15.5 billion, the third biggest in its history and another major blow to the auto maker's turnaround effort. Page 5

■ **U.S. auto sales dropped** in July, with the Big Three reporting sharp falls. BMW and Nissan posted lower profits. Pages 5, 7, 8

■ **Yahoo CEO Yang won** strong backing from shareholders at the annual meeting, as did Chairman Roy Bostock. Page 6

■ **A rebound strategy** that tilts toward U.S. consumer-discretionary stocks may make sense for investors with a time horizon of a year or two. Page 19

■ **Time Warner completed** the internal work necessary to separate its AOL unit's dial-up access and content businesses. Page 8

■ **Total's net profit** jumped 39% as rising upstream production allowed it to gain from surging prices. Page 7

Markets 4 p.m. ET

MARKET	CLOSE	NET CHG	PCT CHG
DJIA	11326.32	-51.70	-0.45
Nasdaq	2310.96	-14.59	-0.63
DJ Stoxx 600	280.24	-3.52	-1.24
FTSE 100	5354.7	-57.2	-1.06
DAX	6396.46	-83.10	-1.28
CAC 40	4314.34	-78.02	-1.78
Euro	$1.5568	-0.0035	-0.22
Nymex crude	$125.10	+1.02	+0.82

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World-Wide

Bush leaves Monday for an Asian visit highlighted by his attendance at the Beijing Olympics but also aimed at reassuring China's nervous neighbors that the U.S. still stands with them. Page 9

■ **The IOC praised** Beijing's Olympic preparations, but Games organizers came under fire over censorship and other issues. China's Hu held his first-ever news conference with foreign journalists, and authorities unblocked several Web sites. Pages 10, 29

■ **Panicked pilgrims stampeded** at a mountaintop Hindu temple in northern India, killing at least 145 people, police said.

■ **Ahmadinejad said** Iran won't give up "a single iota of its nuclear rights," rebuffing an informal deadline set by U.N. Security Council members for Tehran to curb uranium enrichment.

■ **Al Qaeda confirmed** in a Web statement the death of al Masri, an explosives and poisons expert, and three other al Qaeda leaders, apparently in a U.S. airstrike in Pakistan last week. Page 3

■ **Pakistan and Afghanistan** agreed to cooperate on stopping cross-border terrorism, Pakistan said, amid accusations that members of Pakistan's spy agency helped a militant group bomb India's embassy in Kabul. Page 9

■ **Iraqi leaders failed** Sunday to resolve differences over how to govern oil-rich Kirkuk, despite U.S. pressure. The dispute is blocking provincial elections.

■ **A U.S. Army scientist** who killed himself as he was about to be charged with 2001 anthrax poisonings was described as "homicidal" by an ex-therapist. Page 2

■ **A Hamas raid** on a Fatah stronghold in Gaza on Saturday left 11 people dead and dozens wounded. Nearly 200 Fatah fighters fled to Israel, and Abbas ordered them to return Sunday.

■ **Zimbabwe's rival** political parties resumed power-sharing talks Sunday in South Africa.

■ **A U.K. jury failed** to reach verdicts in the case of three British Muslims accused of helping to plan the London subway and bus bombings in 2005.

■ **At least nine climbers**, some struck by an avalanche, were feared killed on K-2, the world's second-highest mountain.

EDITORIAL & OPINION

Plane talk

EADS chief Louis Gallois on the global aerospace business. The Journal Interview. Page 14

Key data defy U.S. woes

Worker productivity maintains growth in face of downturn

By Brian Blackstone

THE OUTLOOK

Recessions don't usually look like this, at least when it comes to productivity.

In the six U.S. recessions since 1970, worker productivity, or output per hour, grew a sluggish 0.8%, on average. But since the end of last year, even amid economic weakness, productivity is estimated to have grown an average 2.5% at an annual rate.

That defies productivity's usual behavior of going "up in good times and down in bad times," says Georgia State University forecaster Rajeev Dhawan.

Productivity's path isn't just an academic debate. That productivity is staying strong even in bad times has big implications for economic growth, inflation, employment and, ultimately, living standards. For example, strong productivity growth, by countering inflation pressures from energy and commodities, allows the U.S. Federal Reserve to keep interest rates lower than it otherwise might, helping it stoke the economy.

But "it's a bit of a two-edged sword," said Chris Varvares of Macroeconomic Advisers, since efficiency gains could mean that companies can get by with fewer workers, exacerbating unemployment in the short run.

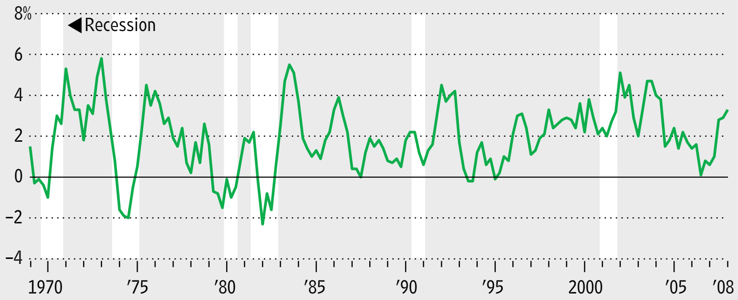
Some economists say the current healthy growth in productivity reflects a shift in the economy from less productive domestic sectors like home building and into exporting industries, which tend to be highly efficient. That shift has been aided by the weak dollar, which has made U.S. exports more competitive.

"It's a compositional story," said Dale Jorgenson, a productivity expert at Harvard University in Massachusetts. Productivity, he explained, is "languid" in construction, so the decline of building as a share of the economy in recent quarters "is cer-

Please turn to page 31

Bumpy productivity

U.S. productivity growth; change from previous year



Sources: U.S. National Bureau of Economic Research; U.S. Labor Department

Hedge funds show warts in July results

By Cassell Bryan-Low

In the world of hedge funds, it is getting harder to hide from the financial crunch.

Since the first tremors of the crunch began, some of the most elite money managers, which cater to wealthy individuals and institutions such as pension funds, have generated strong returns by focusing on specific areas, such as commodities, emerging-market stocks or betting against troubled banks.

But as hedge funds as a group look set to turn in their worst monthly performance since July 2002, even those investment strategies that had been doing well have run into trouble. Some previously high-flying funds are sustaining declines in the double digits. Several managers are down more than 20% for the year.

Consider London-based **Boyer Allan Investment Management** LLP, which specializes in Asian stocks and whose flagship $1 billion **Boyer Allan Pacific Fund** is down about 28% for the year through the end of July, after turning in a 52% gain in 2007. And at London-based **RAB Capital** PLC, two funds that focus on natural-resources and energy—the $1.4 billion **Special Situations Fund** and $751 million **RAB Energy**—are down 32.5% and 27.4%, respectively, through July 24.

Hedge funds as a whole are still outperforming the broader market this year, but they potentially performed worse in July. Preliminary data from Chicago-based Hedge

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Investors likely to wager on Europe, sell Treasurys

By Min Zeng

The focus of bond investors shifts this week to the meetings of three major central banks: the U.S. Federal Reserve, the European Central Bank and the Bank of England.

All three are expected to leave their key rates unchanged, but that image of stability is misleading. For investors looking to establish longer-term positions, betting on a narrowing gap between U.S. and European yields—by buying European government debt and selling U.S. Treasurys—may be the way to go.

On Friday, 10-year U.S. Treasurys yielded 3.95%, compared with 4.33% on 10-year German government debt. Ten-year U.K. government debt yielded 4.85%.

Friday's 0.38-percentage-point spread between U.S. and German 10-year yields was down from 0.52 percentage point a week earlier and nearly 0.7 percentage point set July 2, the widest gap since 2002. The 0.9-point spread between U.S. and U.K. 10-year debt was off from 1.17 points July 2, the biggest gap since 1997.

"The yield spread will continue to flatten, especially the 10-year sector," said Amitabh Arora, head of global interest-rate strategy in New York at Lehman Brothers. He predicted the 10-year gap between the

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LEADING THE NEWS

Fed policy makers to confront trio of challenges

Key rate may hold amid weak growth, inflation, credit woes

BY SUDEEP REDDY

U.S. Federal Reserve policy makers are facing a triple threat in the economy. Inflation is too high because of soaring global commodity prices, growth is too slow as the weak job market, bleak housing sector and high fuel prices threaten the outlook for consumers, and credit markets remain in disrepair as the financial system struggles through its worst shock since the Great Depression.

How to balance those risks will be the focus of the Fed's policy meeting on Tuesday. The central bank is expected to leave the benchmark federal-funds rate, charged on overnight loans between banks, unchanged at 2%.

Most Fed policy makers believe the next move in interest rates is up, but their views about timing vary. Two officials, including one who currently votes on the rate-setting Federal Open Market Committee, indicated ahead of the June meeting a desire to raise rates immediately. Several others since then have signaled an interest in tightening policy before long to address higher inflation and the risk of a price spiral.

But most officials, while still concerned about inflation risks, are more worried about restoring stability to the financial system to prevent more threats to economic growth. The mood in financial markets has worsened during the past six weeks, though it has been punctuated by brief waves of optimism. Fears about banks' health are raising the risk that lending to consumers and businesses could be restrained for an extended period. The Fed's aggressive measures designed to ease the credit crisis—a series of new lending tools, in particular—have helped, but not enough.

The crisis over government-sponsored mortgage giants Fannie Mae and Freddie Mac has worsened some financial conditions. Mortgage rates, for instance, are back to where they were a year ago—even though the federal-funds rate was 5.25% at the time—while the availability of home loans is much lower. That could hurt an already bleak housing outlook, which would threaten consumer spending even more as the job market sours.

Fed officials, caught by surprise repeatedly over the last year, are deeply uncertain about the economy's course. Despite a bump in second-quarter growth, they realize consumer spending may hit potholes by year's end as the government's stimulus program fades.

Top Fed officials have walked away from their suggestion at the June meeting that the risks of weaker growth "appear to have diminished somewhat." The troublesome mix of inflation and growth problems led the Fed's policy committee to avoid explicitly stating the balance of risks in the statement after their June meeting. That may be the course again.

INDEX TO PEOPLE

This index lists the names of businesspeople and government regulators who receive significant mention in today's Journal.

For more people in the news, visit CareerJournal.com/WhosNews

INDEX TO BUSINESSES

This index of businesses mentioned in today's issue of The Wall Street Journal Europe is intended to include all significant references to companies. First reference to these companies appear in boldface type in all articles except those on page one and the editorial pages.

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Scientist's suicide leaves anthrax questions in U.S.

WASHINGTON—The suicide last week of a U.S. Army biological-weapons scientist opens a new and perhaps final chapter in the anthrax attacks that created a sense of siege in the U.S. soon after the Sept. 11, 2001, terrorist attacks.

Associated Press

Bruce E. Ivins, a biodefense researcher, is seen in 2003, at Fort Detrick, Md.

Bruce E. Ivins, a 62-year-old scientist at the Army's Fort Detrick biological-weapons lab in Frederick, Md., emerged as the prime suspect in a case that had foiled investigators for years. He was about to be charged with five counts of murder. A person describing herself as Dr. Ivins's therapist, in an application for a restraining order, described him as "homicidal."

Dr. Ivins had became distraught in recent weeks as law-enforcement scrutiny intensified, and he was hospitalized last month after threatening suicide, a family member said. He died Tuesday from a prescription-drug overdose.

The mailing of deadly disease spores to congressional offices and the news media killed five people and sickened 17 others. It launched a seven-year federal investigation that repeatedly took missteps and met with dead ends.

An Ivins family lawyer, Paul Kemp, said his client was innocent, "and we would have established that at trial." He added, "The relentless pressure of accusation and innuendo takes its toll in different ways on different people. In Dr. Ivins' case, it led to his untimely death."

Former U.S. Senate Majority Leader Tom Daschle, whose office was a target of the anthrax attacks in 2001, said Sunday the suicide of the government's main suspect doesn't mean the case is over, the Associated Press reported. He said the FBI hasn't given him any new updates. He also raised questions about the quality of the investigation, noting that the government recently paid out almost $6 million to a former Army scientist, Steven Hatfill, who accused authorities of unfairly targeting him in the anthrax case.

The U.S. Justice Department said only that "substantial progress has been made in the investigation by bringing to bear new and sophisticated scientific tools." U.S. officials wouldn't offer further detail.

In 2006, Federal Bureau of Investigation Director Robert Mueller ordered a new look at the case. Agents began re-examining years of evidence, witness statements and hunches. The effort was "one of the most complex and comprehensive ever conducted by law enforcement," the FBI said.

Dr. Ivins was part of a team of weapons experts that the task force turned to to examine evidence and spore samples from postal facilities. He became a suspect when investigators re-examined a 2002 anthrax spill at the lab that he didn't report when it happened, according to an Army report on safety lapses.

Friends and former colleagues at Fort Detrick expressed skepticism that Dr. Ivins was responsible for the attacks. They described an eccentric and gregarious workaholic who, through diligent and careful work, became one of the country's premier anthrax experts.

"He was probably one of the few people in the country that was really conversant about anthrax," said Jeff Adamovicz, his former supervisor in the bacteriology division. His research proved critical to the development of a second-generation anthrax vaccine, colleagues said. Dr. Ivins was an important contributor to the anthrax investigation, helping test specimens as thousands of samples poured in. His knowledge of the bacteria was so deep that he could by sight rule on whether cultured specimens were relevant to the investigation.

Dr. Ivins's possible motive remains unclear. The Associated Press reported Friday that it might have been a misguided effort to test vaccine work that was under way at the lab.

Dr. Ivins was also viewed by investigators as emotionally unstable. But ex-colleagues said that might have been a reaction to intensifying scrutiny.

Richard Spertzel, who was deputy commander of the Army's biodefense lab in the 1980s and knew Dr. Ivins, was skeptical that anyone working at the lab or Fort Detrick could have made the form of anthrax used in the mailings. It would have required techniques and specialized equipment that a person couldn't have kept secret there.

—Susan Schmidt contributed to this article.

LEADING THE NEWS

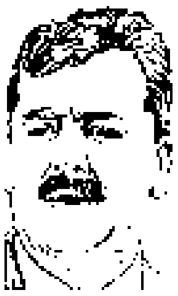
Al Qaeda posting confirms death of bomb expert

By Alan Cullison

KABUL, Afghanistan—In a blow to al Qaeda in Pakistan, the terrorist group confirmed Sunday that one of its top weapons researchers, Abu Khabab al-Masri, was killed, apparently in a U.S. missile strike.

For more than a decade, Mr. Masri moved in the top echelons of al Qaeda as a bomb maker and innovator of the group's mostly feckless attempts to build viable chemical and biological weapons. While his expertise is replaceable, Mr. Masri's death further degrades the old guard who were trusted by al Qaeda leaders Osama bin Laden and Ayman Zawahri.

Al Qaeda confirmed Mr. Masri's death in a posting on Islamist Web sites Sunday, calling him an "expert" who left behind a generation of students. He was rumored to have been killed in a missile strike in a village in Pakistan's northern tribal areas.



Yousuf Raza Gilani

The timing of Mr. Masri's death in the attack coincided with a visit to the U.S. by Pakistan's new prime minister, Yousuf Raza Gilani, who is under pressure to do more to combat Islamists on Pakistan's border with Afghanistan.

Mr. Masri, who carried a $5 million bounty on his head, was part of a well-educated Egyptian cadre in al Qaeda that has developed and directed some of the group's most spectacular attacks. Experts say he likely helped train the suicide bombers who attacked the USS Cole in Yemen in 2000 and assisted in the failed mission of Richard Reid, a British citizen, who tried to blow up a trans-Atlantic airline flight with a bomb concealed in his shoe in 2001.

A chemist by training, Mr. Masri started in al Qaeda as a bomb maker but branched out into the development of biological and chemical weapons after the terror group settled in Afghanistan in the 1990s. There he was entrusted with part of al Qaeda's so-called yogurt project to develop weapons of mass destruction, and operated a training camp in the village of Derunta. He tried unsuccessfully to develop an anthrax weapon and, with Dr. Zawahri, tried to develop poisons that could kill more quickly by mixing them with chemicals that caused them to be absorbed into the skin more rapidly.

It isn't clear how much of the research bore results, though U.S. authorities said Mr. Masri did gas some dogs at the Derunta training camp. U.S. authorities said he provided hundreds of Mujahidin with hands-on training in the use of poisons and explosives and distributed training manuals showing how to make chemical and biological weapons.

Bruce Hoffman, a terrorism specialist and professor at Georgetown University, noted that one of Mr. Masri's students was Kamal Bourgass, who was convicted in 2005 of trying to spread poisons on streets in the U.K. "He had his hands in a lot of different things," Mr. Hoffman said.

In April, U.S. officials confirmed that another senior al Qaeda planner, Abu Obaidah al-Masri, alleged mastermind behind the 2005 London transportation bombings, died in Afghanistan last year of hepatitis.

British Energy, EDF hopeful

Merger falls through at last minute but discussion continues

By Dana Cimilluca And David Gauthier-Villars

Electricité de France SA and **British Energy Group** PLC are holding out hope that their marriage can still happen, despite a last-minute collapse of a $24 billion plan that could reshape Britain's energy industry.

British Energy's purchase by EDF fell apart late Thursday night after two major British Energy shareholders objected to the price, according to people familiar with the situation. Friday, neither side was ready to pronounce the deal dead, with British Energy issuing a statement indicating that talks are continuing. A person close to EDF said the company still wants to pursue talks.

British Energy shares, after dropping 7.5% on the news, rebounded a bit and were down 4% at 700 pence ($13.81) at the close of trading in London.

Officials at EDF, who believed they had the support of British Energy's board, were stunned to receive a call Thursday night informing them that the board wouldn't approve the deal, people familiar with the matter say. EDF's board had already approved the deal, and the company had said it would hold a news conference in Paris Friday morning.

The deal would have given British Energy shareholders a choice of about 765 pence a share in cash or a combination of about 700 pence and a certificate, valued at roughly 65 pence, that could rise in value depending on performance. The British government, which has a roughly 35% stake in British Energy, was in favor of the deal, valued at £12 billion ($23.7 billion).

When British Energy ran the agreement Thursday past **Invesco Asset Management** Ltd. and **M&G Investments**, they balked, according to a person familiar with the matter. The two institutional investors together own about 23% of the nongovernment shares, and the prospect of opposition was enough to dissuade British Energy's board from endorsing the deal. Representatives for the funds declined to comment or couldn't be reached.

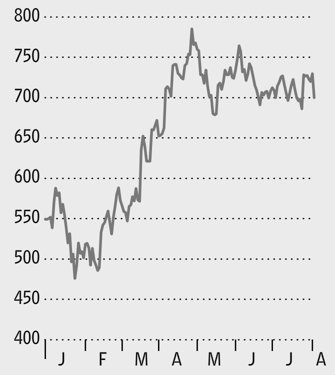
Besides presenting an embarrassment for both sides, failure of the deal could delay ambitious U.K. government plans to build a new fleet of nuclear-power plants to plug a looming energy gap.

—Selina Williams contributed to this article.

DAILY SHARE PRICE PERFORMANCE

British Energy

On the London Stock Exchange
Friday's close: 700 pence, down 4%



Source: Thomson Reuters Datastream

CORPORATE NEWS

HOME IMPROVEMENT

Kingfisher sells Italy unit to Adeo for $868.4 million

Kingfisher

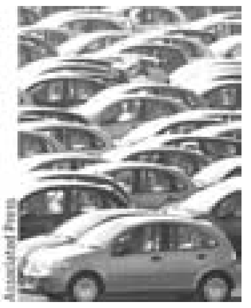
KINGFISHER PLC, Europe's biggest home-improvement retailer by sales, said it sold its underperforming Italian business, Castorama, for £440 million ($868.4 million) to closely held French company **Groupe Adeo** SA.

Castorama opened its first store in Italy in 1988 and now has 31 stores and more than 2,200 staff there. For the year ended Feb. 2, the business posted a retail profit of £29 million and sales of £314 million. It had net assets of £341 million.

Proceeds will be used to reduce U.K.-based Kingfisher's net debt of around £1.5 billion, said Chief Executive Ian Cheshire. *—Lilly Vitorovich*

AUTOMOBILES

Fuel prices start to take a toll on sales in France


Associated Press

FRENCH new-car registrations for July suggest that skyrocketing fuel and energy prices are starting to take their toll on second-half auto sales.

Renault SA's new-car registrations fell 0.2% last month from a year earlier to 183,014 vehicles, compared with a 1.6% rise in June, said the French auto manufacturers association. Sales of the Renault brand alone were down 3.7%. Rival **PSA Peugeot-Citroën** SA saw a 0.9% rise in sales last month—a marked slowdown after a 3.7% increase in June. Overall French registrations of new cars fell 0.2% in July to 183,014 vehicles, compared with a 1.6% rise in June. *—David Pearson*

AVIATION

European venture to buy Airbus plant in Germany

Associated Press

A FACTORY operated by Airbus in Laupheim, Germany, will be sold to Germany-based **Diehl Group** and **Thales** SA of France, officials said.

Herbert Wust, whose Diehl Foundation is part of a venture with Thales, said the plant would be operated by the venture starting Oct. 1.

The sale of the Laupheim site is part of Airbus's restructuring program, aimed at cutting costs and boosting profitability after expensive delays to the superjumbo A380 and the midsize A350. Airbus parent **European Aeronautic Defence & Space** Co. said the plant has 1,100 employees and produces cabin linings, compartments and air ducts for planes. *—Associated Press*

Showtime for MySpace

Investors want to see if super-targeted ads boost the bottom line

BY AMOL SHARMA AND EMILY STEEL

WHEN NEWS CORP. reports its fiscal 2008 earnings Tuesday, investors will scrutinize the company's plans to generate more advertising revenue from the enormous amount of traffic on its MySpace social-networking Web site.

One initiative could be critical to MySpace's success: a system that lets marketers aim their ads at particular groups of users.

ADVERTISING

As part of this "hypertargeting" system, MySpace has analyzed the profiles of its users to gauge their interests and then categorized them into more than 1,000 "buckets," including rodeo watchers, scrapbook enthusiasts and "Dancing with the Stars" viewers.

"The beautiful thing about MySpace is that people go on every day and share with us what they're passionate about, what their interests are," says Adam Bain, who heads the hypertargeting initiative.

The marketing service was launched last fall, and feedback from some early advertisers has been positive. Concert promoter **Live Nation** Inc. says the Coldplay summer-tour page on its Web site got a good bump in traffic after the company bought display ads on MySpace directed at fans of Coldplay, as well as those of bands with overlapping audiences, like Modest Mouse and Death Cab for Cutie.

But it's far from clear that the ad-targeting service will allay growing concerns about the business prospects of MySpace and other online social networks. Because a significant number of MySpace user profiles contain suggestive or otherwise edgy photos or language, many big marketers still worry that their ads could end up alongside inappropriate material. They also worry that social-networking users tend to ignore ads.

Privacy concerns about online ad targeting also pose an issue. MySpace rival Facebook faced a wave of complaints from consumers when it unveiled a new advertising feature last year that updated users' friends about online purchases the users had made. Last Friday, a congressional committee asked 33 technology companies, including **Google** Inc., **Microsoft** Corp. and **Yahoo** Inc., to provide information about their ad-targeting policies.

The stakes are high for MySpace and **News Corp.**, which acquired the site three years ago for $580 million just as MySpace was becoming a Web phenomenon. The site has become one of the Web's biggest destinations, with 118 million unique monthly visitors, according to Internet tracking firm comScore Inc. But questions are growing about News Corp.'s ability to turn that huge audience into big profits. Earlier this year, the company said its Fox Interactive Media division, which includes MySpace, would miss its $1 billion revenue target for fiscal 2008. Research firm eMarketer expects MySpace, which accounts for most of the division's revenue, to bring in about $755 million this year. (News Corp. also owns Dow Jones, publisher of The Wall Street Journal.)

Much of MySpace's current revenue is coming from splashy ads on the MySpace home page, such as a recent campaign to promote the latest Batman film, "The Dark Knight." But there's a limit to how many of those kinds of ads MySpace can sell, because the home page has only one spot for ads. Another big source of revenue is Google, which agreed to make payments to MySpace totaling a minimum of $900 million over three years for the right to broker sponsored links on the site. But halfway through the deal, both sides have hinted that performance has been disappointing, with few users clicking on the ads Google displays in response to searches.

James Kiernan, a media buyer at Starcom MediaVest who has handled hypertargeting campaigns for a dozen or so **Procter & Gamble** Co. brands on MySpace, says he has seen the approach yield a 25% to 30% increase in consumer response compared with regular ad buys. MySpace, which has cheap advertising rates by industry standards (only a few dollars at most for one thousand displays of an ad, compared with the $50 or $60 per thousand charged by some sought-after niche sites), says it can charge roughly double those rates by offering targeting. "The closer you get to the audience you want, the better you get in terms of clicks or sales of the product," says Sean Muzzy, senior partner and media director at digital-ad agency Neo@Ogilvy.

But there are plenty of skeptics. Big brands are experimenting with hypertargeting—Adidas ran a campaign aimed at MySpace soccer fans, while McDonald's bought ads targeted at coffee drinkers—but no one is committing huge sums yet. The biggest concern among marketers is that social-network users simply aren't in the mood to pay attention to ads while they are exchanging messages with friends or looking at photos.

For some marketers, especially small ones, more-generic targeting suffices. The New York Health & Racquet Club spent $5,000 on a MySpace campaign that displayed 2.3 million ads to users on the site. Though the health club could have chosen to target ads at people who say in their profiles that they enjoy rock climbing, yoga or working out, it chose instead to simply target by age and ZIP codes near its facilities. The club said it was relatively happy with the campaign, which generated roughly 1,000 clicks, a response rate of just 0.04%.

Mr. Bain argues that the hypertargeting system won't just pay off by boosting ad sales. It's also a way for marketers to glean valuable information about their target audience. If the advertiser wanted to reach scrapbooking hobbyists, for example, it could find 236,475 of them on MySpace. But the system also shows that 99% of them are female, and lists several other hobbies they tend to be interested in, including sewing, baking and watching the TV show "Grey's Anatomy."

"We're in a position to help them refine the research they're doing about their customers," Mr. Bain says.

Siemens hangs up

The German engineering conglomerate has jettisoned unprofitable telecommunications-equipment holdings - formerly its biggest source of revenue - in stages over the past three years:

June 2005: Siemens sells its mobile-handset business, with about €5 billion in annual revenue, to Taiwan's BenQ.

June 2006: Siemens agrees to fold the largest part of its telecom unit, with about €9 billion in revenue, into a 50-50 joint venture with Finland's Nokia.

November/December 2006: German police raid Siemens to investigate suspicious transactions at its telecom unit, triggering a bribes-for-business scandal. Siemens identifies €420 million in questionable payments at the unit and postpones the start of the Nokia joint venture for three months.

July 2008: Siemens sells a 51% stake in another telecom-equipment business, with about €3 billion in revenue, to U.S.-based Gores Group. Three days later it sells an 80.2% stake in the last telecom-equipment business still under its control, with about €800 million in revenue, to Germany's Arques Industries.

Sources: Siemens; WSJ reporting

Siemens to sell majority of cordless-handset unit

BY MIKE ESTERL

Siemens AG will sell a majority stake in the last remaining telecommunications-equipment business under its control as the German conglomerate restructures to narrow its focus and raise profit.

Europe's largest engineering company by revenue said Friday that it will sell an 80.2% stake in its cordless-handset unit, which had about €800 million ($1.24 billion) in sales last year, to Germany's **Arques Industries** AG. Siemens didn't disclose financial terms but said it expects to book a "double-digit million" euro loss when the deal closes in September.

The divestment process, carried out in stages since 2005, has reshaped a company that began as a 19th-century manufacturer of telegraph equipment and still generated about €20 billion in annual revenue from telecom equipment earlier this decade. In more recent years, Siemens's telecom business racked up big losses as lower-cost rivals snapped up market share.

Siemens's telecom unit also sparked a massive bribes-for-business probe that burst into public view after a German police raid in late 2006. The Munich-based conglomerate has since flagged more than €400 million in suspicious transactions in 2000 to 2006 at its telecom businesses and was fined €201 million by a German court last October for bribes paid in Nigeria, Russia and Libya.

The sale of the cordless-handset unit came just three days after Siemens said it found a buyer for a 51% stake in a larger business that sells a broad range of telecom equipment to corporate customers. That business, which Siemens is selling to U.S.-based **Gores Group** LLC, has annual revenue of about €3 billion.

The rapid-fire transactions underscore Chief Executive Officer Peter Löscher's desire to book as many restructuring costs as possible in Siemens's current fiscal year, which ends Sept. 30. The asset sale to Gores also is slated to close next month and result in a negative financial impact of as much as €1 billion for Siemens in the current quarter.

Mr. Löscher left U.S.-based Merck & Co. to take the reins at Siemens in July 2007 as part of a management shake-up at the German conglomerate in the wake of the bribery scandal. Last year, the CEO collapsed Siemens's myriad businesses into three divisions: industry, energy and health care.

The company outlined plans last month to cut 16,750 jobs worldwide, or about 4% of its work force, and further streamline operations.

FOCUS ON AUTOS

Loss adds to GM pressure

Board meets Monday amid new questions about chief's future

By John D. Stoll And Neal E. Boudette

DETROIT—**General Motors** Corp., in another major blow to its turnaround effort, on Friday reported a $15.5 billion net loss for the second quarter.

The huge quarterly loss—the third-biggest in GM's history—marks the latest chapter in the long, rough slide of the auto maker, a company that once dominated the world automotive industry. It comes at a time when the entire business is in turmoil amid the U.S. economic slowdown. GM and its two Detroit rivals are being forced to ratchet back or phase out their leasing programs, long a linchpin of sales, because declining car values are undermining the economics of the business.

But even foreign brands are skidding. **Nissan Motor** Co. said Friday that net profit fell 43% its fiscal first quarter, as increased sales to emerging markets failed to make up for the negative effect of a stronger yen and a downturn in the U.S. market. **BMW** AG, also hurt by the weak U.S. market, reported second-quarter profit fell 33%. About a week ago, **Ford Motor** Co. posted a second-quarter loss of $8.7 billion.

GM's board has a regularly scheduled dinner meeting on Monday. Chairman and Chief Executive Rick Wagoner and other executives are expected to attend. The board has been briefed on the second-quarter loss and is expected to look at the results in detail.

Board members Armando Codina, George Fisher, the lead independent director, and several other members didn't respond to repeated calls for comment.

One board member, reached by phone, said he isn't yet familiar with details of Monday's agenda or who will be in attendance but expects the company's condition to be a topic of conversation. "Things are tough, and it's a hard road for them."

GM's performance, which was worse than analysts expected, increases the pressure on Mr. Wagoner to show he can steer the company back to profitability. From 2005 to 2007, GM lost a cumulative $50 billion. In the first two quarters of 2008, it has lost an additional $18 billion.

In the U.S. market, GM has been hurt by the sharp drop in sales of trucks and sport-utility vehicles as consumers seek shelter from high gasoline prices by shifting to small cars and more fuel-efficient vehicles. Lower truck sales caused a $9.9 billion decline in GM's North American revenue, to $19.8 billion from $29.7 billion. On Friday, the company said U.S. vehicle sales in July fell 26%.

GM burned through a less-than-expected $3.6 billion in cash during the quarter. However, that still shrinks its war chest of readily available cash and assets—the money it needs to pay its bills and guard against downturns—to $20.5 billion. Analysts scrutinize this number to gauge whether the company has enough funds to stay afloat.

The earnings were further depressed by an unexpected loss in Asia, a region that had been generating steady profits. GM also lost $2 billion covering unprofitable auto leases, which lost value amid the tumbling popularity of used SUVs and trucks. It took $2.8 billion in charges related to former parts division Delphi Corp. and $3.3 billion related to a buyout offer that cut 19,000 people from the payroll last quarter.

As recently as July, GM's board voiced strong support for Mr. Wagoner, who has been CEO for most of the decade. Mr. Wagoner had planned to have the U.S. operation on its feet by 2008—but a weak economy and unexpected market-share declines spoiled that agenda.

In light of GM's extraordinary losses, some analysts say they have been discussing whether Mr. Wagoner can keep his job. "It has been a question for the last couple of years," said Kenneth A. Elias, a partner at Maryann Keller & Associates, LLC, an automotive consulting firm. Since Mr. Wagoner began trying to turn around the company in 2005, "GM hasn't made the moves to resuscitate the business in North America."

A spokesman for GM referred questions about the chief executive's job security to Mr. Wagoner, who declined to comment.

GM's quarterly loss was a reversal from a year earlier, when it reported net income of $891 million. Its per-share loss was $27.33, compared to earnings of $1.56 per share a year earlier.

Mainly because of lower U.S. sales, revenue fell to $38.16 billion from $46.7 billion. GM reported strong profit from its unit covering Latin American, Africa and the Middle East, and a modest profit in Europe.

Its Asian operations lost $65 million, which GM blamed on higher costs for hedging against fluctuations in currency values. Overall, GM's auto operations lost $4 billion.

The second-quarter report revealed many areas of concern, particularly about GM's cash. The company said it has enough cash and available assets to last through 2009, but that is "not particularly reassuring," said Calyon Securities analyst Mark Warnsman. "Clearly, GM will need to take concrete action within the next year or so to improve its balance sheet."

The company said Friday it needs to keep $11 billion to $14 billion on hand at month's end to pay its bills and cover fluctuations in cash flow. It said it plans to draw down $1 billion from its available credit lines, in a move to top off its available cash.

Because it is selling far fewer trucks—which have much higher profit margins than cars—and because it lost $2,000 per vehicle due to leasing-related write-downs, GM's revenue per vehicle sold in second quarter plummeted to $17,940, down from $21,575 a year earlier. That is also $1,200 lower than where transaction prices were in the same period in 2004, which was before GM implemented a plan to boost per-vehicle revenue by cutting some of the discounts and deals it was offering to car buyers.

Problems with its leasing contracts began to surface only in June. GM, like other auto makers, relied heavily on lease deals to sell trucks and SUVs. But as the used-car market floods with such vehicles, and resale values plummet, leasing gets much less lucrative for an auto maker. That's because the contracts are based on accurately predicting a vehicle's value when the lessee turns it back in.

Mr. Wagoner and his chief lieutenant, President and Chief Operating Officer Frederick "Fritz" Henderson, have unveiled a plan to cut costs by $10 billion and raise about $5 billion to steady the company over the next 18 months.

Mr. Wagoner has appeared to take a step back from the day-to-day operations of the company over the past few months. In the spring, the board promoted Mr. Henderson to chief operating officer. He had been GM's chief financial officer. He took over responsibility for GM's company's global auto operations, a duty that had belonged to Mr. Wagoner.

Some investors have become restless. Earlier in the second quarter, when Southeastern Asset Management, which owns at least 7% of the auto maker, held its annual meeting, the fund's president, Staley Cates, faced complaints about its stake.

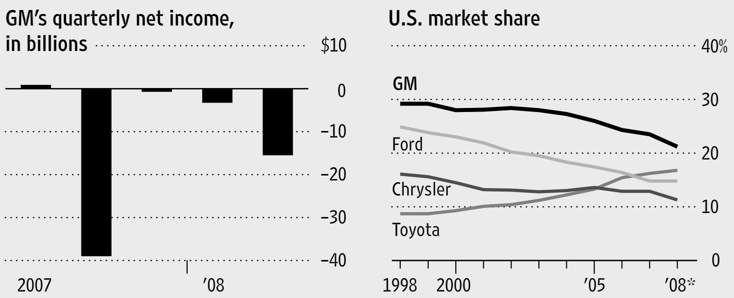
Some Southeastern investors see GM as one of the firm's few "stubborn" holdings, Mr. Cates said. They "bring up the stubbornness question of 'should we stay with these things so long?' " he said.

He said computer maker Dell Inc. and telecommunications company Level 3 are two other holdings considered "stubborn." Southeastern sees long-term upside in GM, Mr. Cates said, but acknowledged the next few quarters "look dismal."

—Sharon Terlep contributed to this article.

Sputtering

General Motors' $15.5 billion second-quarter loss comes amid the auto maker's continued sales slide.



*Through July

Sources: the company (net income); Autodata (market share)

WSJ.com

Online today

John Stoll discusses the growing financial woes at GM, at **WSJ.com/Video**

BMW 7 series

Losing traction

Rising incentives see profits veer off track. Average incentive spending per car in the U.S.

Manufacturer	June '07	June '08	Percentage change
Mercedes-Benz	$3,474	$4,692	+35%
BMW	2,874	4,680	+63
Audi	2,709	4,085	+51
GM	2,864	2,643	−7
Ford	3,772	2,569	−32
Acura	2,031	1,841	−9
Lexus	816	1,557	+91

Source: Autodata Corp.

BMW shifts its strategy as net profit slumps 33%

By Edward Taylor

Luxury-car maker **BMW** AG issued a hefty profit warning Friday and signaled a return to more conservative sales tactics, reversing a policy of using steep discounts and cheap leases to win U.S. market share.

The German company said it would cut production and raise prices globally, especially in the U.S., as it disclosed that second-quarter net profit fell 33% to €506 million ($786.3 million) from €751 million in the year-earlier period. Revenue was down less than 1% to €14.6 billion.

Like other premium German brands selling in the U.S., BMW faces an increasingly tough choice between trying to protect profitability and holding on to market share, industry analysts say.

In recent years, BMW has pushed aggressively to sell cars in the U.S., using discounts and easy leasing terms. That trend accelerated during the past year as the U.S. market turned sour, forcing brutal price competition to draw customers into showrooms.

Auto executives and analysts warn that BMW, Mercedes-Benz and Audi, the luxury brand of **Volkswagen** AG, all risk losing their most valuable asset—their exclusivity—by copying the hard-sell high-volume tactics U.S. car makers have used for decades. BMW now appears to be struggling to return to its previous sales strategy known as "pull"—making customers line up to wait for cars and pay full price, attracted by the belief they are getting an exclusive product.

"Any premium auto maker that strives to push volume for its own sake runs the risk of losing exclusivity," says Vic Doolan, president of Volvo Cars North America until March 2005, and president of BMW of North America until July 1999.

BMW said Friday it wants to "retain its position as the world's leading premium manufacturer." In 2005 BMW eclipsed **Daimler** AG's Mercedes-Benz to become the world's biggest-selling premium auto maker by sales, in part as a result of its aggressive sales tactics. But the Munich-based company said "volume growth will not be pursued at the expense of profitability. In the light of the ongoing weakness of the U.S. dollar and market, sales volumes will be reduced in the U.S. on a targeted basis as part of a new strategy for this region."

BMW has been among the most aggressive companies in its use of discounts to sell cars in the U.S., offering an average $4,680 per car in June, up 63% from June 2007. Rival Mercedes-Benz offered $4,692 of discounts, roughly 35% more than in June 2007. Audi, which offered $4,085 per car in June, ramped up its incentives by 50%, figures supplied by Autodata Corp. show.

The incentives are higher than those of **Ford Motor** Co. and **General Motors** Corp., but they are also higher than those for Lexus, which offered incentives of $1,557 per car in June, and Acura, which offered discounts of $1,841. Lexus is made by **Toyota Motor** Corp., and Acura is a product of **Honda Motor** Co.

Cheap leasing deals have also hurt BMW's profits. In the second quarter, BMW booked a charge of €459 million related to its leasing business, following a €236 million charge in the first quarter.

A sharp downturn in auto markets in recent weeks means BMW won't meet its previous profit target for 2008, the company said, warning that 2009 will also be a tough year. BMW said it expects the operating margin in its automotive division to reach "approximately 4% or higher" in 2008, compared with 6.4% in 2007.

BMW's bid to boost sales volumes appears to have been eroding the company's profitability for some time. While its auto sales rose to 1.5 million cars in 2007 from 1.05 million cars in 2002, operating margins for that segment shrank to 6.4% at the end of 2007 from 9.2% in 2002. Currency factors, rising investments in fuel-efficient technology, the rising price of raw materials, as well as slumping demand in the U.S., have contributed toward eroding profits, the company says.

Rather than seeking to top the 336,000 cars BMW sold in the U.S. in 2007, sales-volume figures are "likely to be lower than a year ago," the company said. On a group level, BMW has decided to "reduce production volumes and increase selling prices."

Rival auto maker Audi recently reduced its sales target in the U.S. to 95,000 units from the 100,000 in sales it previously had targeted for this year, a spokesman for the company said Friday. Daimler, the Stuttgart, Germany-based parent company of Mercedes-Benz, late last month gave a profit warning and also said it would give increased emphasis to growing volumes profitably.

CORPORATE NEWS

Armored vehicles drive BAE

Earnings climb 14%, boosted by demand in Iraq, Afghanistan

By Monica Mark

LONDON—**BAE Systems** PLC reported a 14% rise in first-half profit, lifted by demand for armored vehicles in Iraq and Afghanistan.

The company, which has been helped by continued overseas action by the U.S. and U.K. militaries, particularly demand for mine-resistant vehicles, said Friday that net profit rose to £586 million ($1.16 billion) from £515 million a year earlier.

The U.K. company's results were boosted by a £61 million gain on the disposal of its surveillance-and-attack business, which provides broadband high-power transmission and radio-frequency systems for military aircraft.

Revenue from continuing operations rose 12% to £7.75 billion from £6.89 billion.

Earnings were driven by the growth of BAE's land-and-armaments business. The company has expanded the unit's annual sales to more than $10 billion from sales of less than $1 billion in 2004, mainly through acquisitions in the U.S. The purchases have boosted BAE's presence in the huge U.S. defense market, and the company now generates about half of its sales from its U.S activities.


Reuters

Demand for **armored vehicles** in Iraq and Afghanistan lifted BAE's first-half profit.

BAE's weakest performer was its U.K.-based programs-and-support unit, where revenue fell 19% to £1.9 billion.

Analysts have been concerned BAE could be affected by political pressure on defense budgets, particularly in the U.K. The company had warned that some defense programs may be stretched over a longer time frame to reduce the cost in any single year.

But BAE said Friday it is confident about its outlook thanks to its large order book, despite "budget pressures in many defense markets." It added that it expects strong second-half growth.

The company's order book rose 30% to £41.1 billion at the end of the first half from a year earlier.

"Building on the first-half performance, the previously anticipated growth outlook for 2008 as a whole is expected to benefit further from the current high demand for armored wheeled vehicles to meet operational requirements," the company said.

BAE shares ended up 2.2% at 460 pence ($9.08) in London trading Friday.

The company reported a £387 million cash outflow from operating activities, compared with an inflow of £165 million a year earlier, after it was hit by a £500 million write-down related to the acquisitions of MTC Technologies Inc. and Tenix Defence. BAE said it expects a return to an inflow in the second half. The company's cash flows can be volatile because of the size of defense contracts.

BAE is the subject of a U.S Justice Department investigation into the company's compliance with anticorruption laws. The U.S. is probing allegations of illegal payments to the Saudi Arabian royal family to help secure a large Saudi contract in the 1980s. Late last year, the U.K. government called off a probe into BAE's weapons sales to Riyadh on security grounds, but investigations of sales to other countries recently has weighed on BAE's stock price.

Enel profit rises 44% on Endesa stake

By Liam Moloney

ROME—Italian utility **Enel** SpA said its first-half net profit jumped 44%, boosted by the consolidation of its stake in Spanish utility **Endesa** SA, a lower tax rate and hydroelectric generation in its home market.

The Rome-based company said net profit climbed to €2.85 billion ($4.43 billion) from €1.98 billion in the year-earlier six months. Revenue grew 55% to €29.32 billion from €18.86 billion.

Looking ahead, Enel said that 2008 and 2009 earnings before interest, taxes, depreciation and amortization (Ebitda) will come in ahead of expectations, thanks to the contribution from its stake in Endesa. Enel bought Endesa last year in partnership with Spain-based conglomerate **Acciona** SA.

Enel now expects 2009 Ebitda to top its March estimate of €13.8 billion, and the 2008 figure will be above market expectations of €13.3 billion, Chief Executive Fulvio Conti said in a conference call with reporters. The company posted Ebitda of €10.02 billion for 2007.

WestLB analyst Katharina Cholewa said Mr. Conti's comments were "very positive."

Enel's net debt totaled €51.29 billion as of June 30, down from €57.07 billion as of March 31. Its debt-to-equity ratio is 2.04, compared with 2.29 in March. Mr. Conti confirmed the company aims to trim its net debt to less than €50 billion by the end of 2008.

The company borrowed cash to pay for its stake in Endesa, in what was the world's biggest purchase of a utility. The takeover, carried out jointly with **Acciona**, valued Endesa at €42.5 billion.

Enel's share price is down about 13% over the past three months—slightly better than the 17% drop in Italy's S&PMib Index—as corporate-governance issues with Acciona over Endesa have rattled investors and concern has mounted over the company's high level of debt.

Debt reduction and the company's relationship with Acciona over Endesa are at the top of analysts' agenda for Enel. Mr. Conti on Friday brushed aside speculation of a spat with Acciona over Endesa.

The company said it plans to pay an interim dividend of 20 European cents per share, unchanged from last year, on Nov. 27. Enel is sticking to its policy of a minimum annual dividend of 49 European cents per share in the coming years, said Mr. Conti, adding that there was no need to lift this figure.

Yahoo's board wins support from shareholders

By Jessica E. Vascellaro

Yahoo Inc. faced little criticism at its annual meeting over the issue that had been expected to be center stage: its rejection of multiple deal offers from **Microsoft** Corp.

Shareholders overwhelmingly endorsed the board, with Yahoo Chairman Roy Bostock receiving a 79.5% favorable vote, up from roughly two-thirds last year. Chief Executive Jerry Yang received an 85.4% favorable vote, down from more than 90% last year but still a strong endorsement for a leader who has faced calls for his resignation.

The results suggest that investors who have been harping about the company's handling of Microsoft negotiations are moving on—or have decided to sell their stock. Yahoo shares have fallen roughly 30% from when Microsoft withdrew its $47.5 billion, $33-a-share offer, to acquire the company in May. The company's stock traded essentially flat Friday at $19.80 in 4 p.m. composite trading on the Nasdaq Stock Market.

The meeting, in San Jose, Calif., was a tame follow to a bitter battle. Investor Carl Icahn, who settled his proxy fight for the company last month, didn't attend the two-hour meeting. Under the settlement, Mr. Icahn and two other directors will join Yahoo's board.

While Mr. Bostock addressed months of negotiations with Microsoft in detail, investors didn't dwell on the topic, besides a few brief or passing remarks. Shareholders instead pressed management on human-rights issues, executive compensation and its strategy against **Google** Inc.

The meeting didn't address who will join the board with Mr. Icahn.

Chávez plan to take over Santander unit is risky

By John Lyons

Venezuelan President Hugo Chávez's decision to nationalize a local unit of Spanish giant **Banco Santander** SA is among the riskier acts of his decade-old presidency, touching on local confidence in the banking system.

Banking affects Venezuelans more personally and immediately than oil, telecommunications and other strategic industries in which Mr. Chávez has intervened. The move could backfire if depositors lose confidence in the government's ability to protect their savings, and yank their money.

In Venezuela, as in many Latin American nations, mass withdrawals at one bank have a way of snowballing into a systemic bank run that puts the economy and political system in play. Mr. Chávez has firsthand experience with this phenomenon. He came to power on a wave of broad voter discontent rooted in the economic chaos that followed a bank collapse in 1996.


Hugo Chávez

So far, there is little evidence that history is about to repeat itself. But Mr. Chávez appeared to recognize the risks last week, when he dispatched Information Minister Andrés Izarra to reassure depositors. Mr. Izarra said in a prepared statement that the takeover of the local bank, Banco de Venezuela, would be legal and wouldn't jeopardize the bank or the economy. "Our government guarantees the financial strength of the system," he said.

One key question will be whether Mr. Chávez will use the nation's vast oil wealth to acquire more banks. Big international lenders, including **Citigroup** Inc. and Spain's **Banco Bilbao Vizcaya Argentaria** SA, also have units in Venezuela. Further acquisitions may not be received well, observers said.

While in the U.S. the government is seen as a guarantor of bank stability, nationalizations are viewed with deep skepticism in many Latin American nations, where official corruption and incompetence are pressing issues. Many Venezuelans already blame government mismanagement for a host of problems ranging from food shortages to the declining productivity of the oil industry.

"Chávez said the bank's deposits will now be in the government's hands, but the problem is there may be people who think that's not such a good thing," said Alejandro Grisanti, a senior Latin America economist who follows Venezuela at Barclays Capital Inc.

Mr. Chávez announced last week that the government would buy Banco de Venezuela, the nation's third-largest bank in terms of deposits, back from Santander at a "fair" price. The bank was privatized in the 1990s. Santander had been in talks to sell it to a local banking group. After learning of the talks, Mr. Chávez decided Venezuela would buy it, he said.

Santander confirmed that it had been in talks with a private group but was now negotiating a sale to the government.

The Spanish government said Friday that it wouldn't get involved.

The specter of nationalization has loomed over the banking sector, and Banco de Venezuela, in particular, for a long time. Banco de Venezuela has a big network of branches that may be used to more efficiently distribute welfare payments and subsidies. Buying it fits with Mr. Chávez's strategy of getting more control over government bank accounts.

While Mr. Chávez is taking pains to present the nationalization as a legal purchase of a bank that was already for sale, Venezuela's history of banking crises will make buttressing confidence over the long term a trickier task. The recent experience that Venezuelans have with banking collapses has conditioned them to act faster to pull their deposits when they sense danger.

Gauging public reaction won't be straightforward either. Official data on deposits in the banking system reflecting the period directly after the nationalization announcement won't be available for about two months, analysts said. Other indicators of confidence weren't encouraging. For example, Venezuela's longer-dated bonds fell on the announcement.

Santander is selling at a key moment for the banking system. The government is set to publish a long-awaited revision of bank regulations expected to increase government controls.

Venezuelan banks have been highly profitable under Mr. Chávez, but the operating environment has changed in the past year. The industry was squeezed, for instance, by the government's decision to move deposits from private banks to government banks. Today, 65% of government deposits are in private banks, compared with 80% a year ago.

Meantime, bank executives have privately questioned the quality of some loans that banks hold. Banks are required to dedicate nearly 47% of their loans to politically sensitive areas such as agriculture. What's more, credit-card and commercial lending may have overheated as Venezuelans took on debt as a hedge against 30% inflation rates.

One senior Venezuelan bank executive said that while some banks' balance sheets look like a pristine mountain lake from afar, up close they turn out to be a thin layer of blue water covering toxic sludge.

Marketplace

A Big Blue world

IBM's global program combines community service, leadership > **Page 29**

CORPORATE NEWS

British Airways takes hit

Rising fuel expenses, decreased traffic sink net profit 90%

By Kaveri Niththyananthan

LONDON—**British Airways** PLC reported a 90% drop in first-quarter net profit because of falling demand and surging fuel costs, lowered its full-year revenue forecast and cut winter capacity.

The British flag carrier, which last week announced a proposed merger with Spain's **Iberia Líneas Aéreas de España** SA, said fuel prices have doubled in the past year and it expects the bill to top £3 billion ($5.95 billion) this year after reaching £706 million in the fiscal first quarter ended June 30.

"The combination of unprecedented oil prices, economic slowdown and weaker consumer confidence has led to substantially lower first-quarter profits," Chief Executive Willie Walsh said.

Friday in London, BA shares advanced 3.75 pence, or 1.5%, to 259 pence. BA said higher fuel prices and lower traffic pulled down its net profit to £27 million in the first quarter from £274 million in the year-earlier period. Revenue rose 2.8% to £2.26 billion, but the airline cut its revenue-growth target for the full year to 3% from the previous 4%.

BA is considering **raising fares** to tackle fuel costs eating into margins.

Deutsche Bank said the cut equates to a loss before interest and taxes of £37 million, or break-even at the earnings-per-share level.

With fuel prices up 49% in the latest quarter, BA is considering raising fares further to tackle fuel costs eating into profit margins. Mr. Walsh said: "We would consider increasing prices, given the fuel increases. That may come through higher fuel surcharges or higher fares."

Analysts are in the midst of downgrading forecasts after BA's chairman, Martin Broughton, warned at the carrier's annual general meeting that it would be challenging for the company to report a profit this year.

BA said it had revised its capital-expenditure plans and will stay focused on cost control. It will cut winter capacity 3.1%, but Mr. Walsh said no planes would be grounded. Instead, it will likely reduce less-popular flights.

The airline also said it was ordering six new Boeing 777-300ER aircraft for delivery beginning in 2010. The planes will give the company more flexibility in the long-haul fleet, BA said.

BA's chief executive also gave an update on the progress of clearing a possible joint venture with **AMR** Corp.'s American Airlines with U.S. antitrust authorities. A spokesman for BA confirmed its chief executive told analysts, "We hope to be in a position to apply for ATI [antitrust immunity] within two weeks." The spokesman added, "He said there was no guarantee, however, that they would get this."

The two airlines have previously failed to get an exemption from antitrust authorities, because of their dominance at Heathrow Airport. A merger or joint venture would give BA greater access to the U.S. and Pacific regions.

Lufthansa strike ends with wage deal

By Jan Hromadko

Deutsche Lufthansa AG said it reached a wage deal with the powerful services union ver.di that ended a six-day strike over pay that led to numerous flight cancellations.

Ground staff at the German airline will get a 5.1% pay increase, retroactive to July 1, and an additional 2.3% raise from July 1, 2009, as well as a one-time bonus of as much as 2.4% of annual salaries. The payment is a profit-sharing agreement, said Lufthansa, meaning its full-year profit will determine the exact amount.

The airline had offered to increase wages by 4.6% in the year that began July 1 and 2.1% the following year, while ver.di had sought a 9.8% increase.

"This is the best wage deal that has been agreed in Germany this year," said ver.di member Thomas Wissgott, who is also a member of the supervisory board of Lufthansa's logistics unit Lufthansa Cargo AG.

Feelings were more mixed at the airline. Lufthansa said the increase will cost it about €40 million ($62 million) for the remainder of this year and €100 million next year.

The agreement will be a serious burden for the company, Stefan Lauer, a Lufthansa board member and the head of personnel, said in a statement. It was the deal's long validity of 21 months that made it acceptable, he added.

Staff reimbursement is a major cost for airlines, and the deal comes at a time when carriers around the world are seeing their profits pulled down by waning demand on the back of the economic downturn and surging fuel prices.

Relief that the strike was coming to an end initially elevated Lufthansa stock Friday, but it edged lower to €14.71 at the close.

"The agreement should lift some of the uncertainty under which the stock has suffered in the recent past," said LBBW analyst Per-Ola Hellgren, adding that Lufthansa should be able to compensate for higher personnel costs through savings elsewhere.

A Lufthansa spokesman said the airline hadn't yet been able to estimate the total cost of the strike and that management therefore couldn't say whether the burden would threaten the company's full-year financial targets.

Though the strike ended Saturday, six days after walkouts commenced, a Lufthansa spokeswoman said it could take as long as two weeks for entire flight operations to normalize.

For cabin staff, the airline agreed to a similar wage deal. However, this agreement requires additional consent between ver.di and cabin-crew union UFO, which represents more than half of flight attendants. UFO, which has a separate wage agreement with Lufthansa that expires Dec. 31, called the deal "totally unacceptable" and said it wouldn't sign such an agreement.

—Kirsten Bienk and Roman Kessler contributed to this article.

Nissan's profit drops 43% despite Mideast demand

By John Murphy

TOKYO—**Nissan Motor** Co. posted a 43% drop in net profit for its fiscal first quarter, as increased sales to emerging markets failed to make up for the impact of a stronger yen and a downturn in the U.S. market.

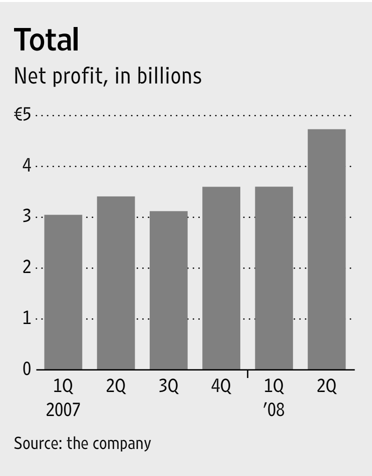
The auto maker's results underscore the strain on the global auto industry as high gasoline prices and an economic slowdown continue to damp new-vehicle sales in the U.S., the world's largest auto market. U.S. industry sales were hit by a plunge in demand for trucks and sport-utility vehicles in the quarter, which ended June 30.

Nissan, Japan's No. 3 auto maker by sales volume after **Toyota Motor** Corp. and **Honda Motor** Co., reported net profit of 52.8 billion yen ($490 million) for the quarter, down from 92.3 billion yen a year earlier. Sales fell 4.1% to 2.347 trillion yen from 2.446 trillion yen. The company maintained its full-year outlook for a 30% drop in net profit because of higher raw-material costs and a continued decline in the U.S. auto market.

Globally, Nissan's sales rose 6.9% for the quarter to 936,000 vehicles, lifted by demand in the Middle East and China. Those gains were offset by the yen's strength against the U.S. dollar, which sliced 54.7 billion yen off operating profit for the quarter. Nissan also set aside 42 billion yen in residual-value risk on its leased vehicles in the U.S. and Canada. Because of falling used-car prices in those markets, Nissan can't make the revenue it had projected on reselling its vehicles when they are returned at the end of their leases.

Sales slipped 1.5% to 253,000 vehicles in the U.S., where consumers spurned its lineup of larger vehicles, including the Pathfinder SUV and Titan full-size pickup truck.

A view of French oil giant Total SA headquarters in Paris



Total, StatoilHydro ride oil prices to big profits

By Adam Mitchell And Elizabeth Cowley

PARIS—French oil and gas company **Total** SA reported a 39% jump in second-quarter net profit, as rising upstream production, including new fields in Congo and the North Sea, allowed the company to gain from surging prices.

Meanwhile, Norwegian oil and gas company **StatoilHydro** ASA reported a 37% increase in second-quarter earnings, also lifted by the surge in oil and gas prices, but its shares fell as analysts voiced concerns over increasing production costs.

Total said net profit rose to €4.73 billion ($7.35 billion) from €3.41 billion a year earlier, as sales increased 23% to €48.2 billion. The earnings report covered the three months ended June 30, before oil prices started falling.

Total's production of hydrocarbons rose 1.3% from a year earlier to 2.35 million barrels of oil equivalent a day. Production growth in the quarter was helped by start-ups at the Jura gas and condensate field in the North Sea and the Moho Bilondo oil site in Congo.

Chief Executive Christophe de Margerie said Total's performance was "driven by the upstream segment, which demonstrated once again the strong sensitivity of its results to high hydrocarbon prices." He said "European refining margins were high, sustained by strong demand for distillates."

Oil and gas prices have risen over the past year. According to figures published by Total on July 15, the average price of Brent crude oil surged 76% in the second quarter from a year earlier to $121.20 a barrel. The average natural-gas price shot up 48% to $7.29 per million British thermal units, Total said.

Total's refinery throughput declined 2% in the second quarter, partly because of a maintenance turnaround at the company's Leuna refinery in Germany.

Total's shares fell 1.2%, to €48.79, in Paris Friday.

Also benefiting from high oil prices, Norway's StatoilHydro said net profit jumped to 18.77 billion Norwegian kroner ($3.65 billion) in the second quarter from 13.71 billion kroner a year earlier. The 2007 earnings include Hydro's oil and gas portfolio. Statoil completed its acquisition of Hydro assets Oct. 1, making the latest earnings the company's first second-quarter results incorporating the Hydro portfolio. Revenue increased 34% to 170.61 billion kroner.

The surge in oil and gas prices was partially offset by increased operating expenses as well as negative net financial items and higher taxes.

StatoilHydro's cost of production per barrel of oil equivalent soared 47% in the year ended June to 46.10 kroner from 31.40 kroner in the prior year, pushed up by restructuring costs relating to its merger with Hydro, the start-up of new fields and general industry pressure.

StatoilHydro's shares fell 6.7% to 157.50 kroner in Oslo.

Chevron's earnings rise by 11%

By Isabel Ordoñez

Chevron Corp. posted an 11% rise in second-quarter profit thanks to high oil prices, extending a string of big profitable quarters for oil companies.

But the second-largest U.S. oil company by market value also echoed the themes of weak refining performance and production declines that tarnished quarterly results of peers **Exxon Mobil** Corp. and **Royal Dutch Shell** PLC last week.

Chevron posted net income of $5.98 billion, or $2.90 a share, compared with $5.38 billion, or $2.52 a share, a year earlier, which included a gain of 32 cents a share from asset sales. Revenue rose 48% to $82.99 billion. The California company's refining operations posted a loss of $734 million, compared with earnings of $1.3 billion last year, primarily due to the effects of a planned crude-unit shutdown for maintenance.

Chevron's total oil and natural-gas production was down 3.4% to 2.54 million barrels of oil equivalent a day, from an average of 2.63 million barrels a year earlier.

Chevron's output, like that of its peers, felt the effects of international production-sharing contracts that reduce the amount of output attributed to companies as oil prices rise.

Chevron Chief Financial Officer Steve Crowe said the company could meet its target of 2.65 million barrels of oil equivalent a day only if the price of oil averaged $70 a barrel for the year. Crude oil for September delivery rose $1.02, or 0.8%, to $125.10 a barrel on the New York Mercantile Exchange Friday.

Chevron's charges in the second quarter were $580 million, which included corporate-tax items and increased charges for environmental remediation costs associated with sites that previously had been closed or sold.

—David Benoit contributed to this article.

CORPORATE NEWS

AOL is closer to splitoff

Work is completed to separate dial-up, content businesses

By Merissa Marr

Time Warner Inc. has completed the internal work necessary to separate its AOL unit's dial-up-access business from its advertising and content business, the company is expected to announce Wednesday. Now it will get serious about plotting the Internet unit's next steps, including whether to sell one or both of the businesses.

For months Time Warner has been exploring options for the two sides of AOL, including whether to sell or combine the businesses in a partnership with other companies. But talks have been held back by uncertainty about what the revenue and liabilities are for each of the two sides, which made it hard for outsiders to put a value on the businesses.

Clarifying the future of AOL has been one of the top priorities for Time Warner Chief Executive Jeff Bewkes since he took the job seven months ago. AOL has long been a drag on Time Warner's stock because of the decline of its Internet-access business and uncertainty about prospects for its ad-based business.

Investors will scrutinize Time Warner's second-quarter results, also due to be released Wednesday, for clues as to the health of AOL ad businesses. In particular investors will want to see whether the businesses, which include online ad-sales firm Advertising.com, are weathering the economic slowdown.

Mr. Bewkes started the complex process of separating the dial-up business from the portal side earlier this year. He had hoped to complete it by the end of the second quarter, he said in the spring, although it took about a month longer. The separation was largely a bookkeeping exercise, requiring staffers to figure out how to divide revenue, staff and liabilities for businesses that have long been closely intertwined.

By dividing the Internet-access business, which has been declining for years, from the rest of AOL, Mr. Bewkes hoped to better spotlight the value of the advertising and content businesses, now regarded as AOL's core business.

Preparations for the split took on greater urgency after **Microsoft** Corp.'s bid for **Yahoo** Inc., which prompted Yahoo to contemplate teaming up with AOL as a way to fend off the software behemoth. Microsoft has since turned its attention to AOL as well.

After months of off-and-on talks with both Microsoft and Yahoo, Time Warner continues to hold informal discussions with the two companies, according to people familiar with the situation. A concrete deal hasn't yet surfaced with either company.

Discussions with Yahoo, the most advanced of the two, envision Yahoo folding in AOL, with Time Warner getting a minority stake in the combination, the people said. The Yahoo discussions have valued AOL at around $10 billion, excluding the dial-up business. In contrast, Time Warner's current stock price—around $14—suggests a value of no more than $3 billion to $4 billion for the ad-sales and content businesses, analysts say.

Once Time Warner concludes discussions about the ad-based business, it will turn to the dial-up business, people familiar with the situation said. The company already has had informal contact with possible buyers, including rival **EarthLink** Inc. It is exploring a securitization, whereby it would raise money on the back of anticipated cash flow from the business.

Analysts value the business at $2 billion to $3 billion, but Time Warner is expected to seek considerably more than that in any sale discussion, according to people familiar with the situation. Despite having been in decline for several years, the business is still profitable and generates a predictable stream of cash. It serves 8.7 million subscribers, while EarthLink, the second biggest dial-up service in the U.S., serves 2.2 million.

EarthLink's chief executive, Rolla Huff, has told investors he is looking to make deals with other dial-up operators as a way to boost the company's cash generation, reasoning that old technologies always stick around longer than people expect.

U.S. auto sales sink; Big Three suffer

By Matthew Dolan

U.S. auto sales dropped 13.2% in July from the same month last year as sales of trucks and sport-utility vehicles kept falling, and a tight credit market kept customers out of showrooms while forcing auto makers to back away from leasing vehicles.

Vehicles sales totaled 1,136,176 cars and light trucks, according to Autodata Corp. The seasonally adjusted, annualized sales pace was 12.55 million vehicles, much lower than expected and a worrying sign for an already embattled auto industry. The year-earlier level was 15.48 million.

Sales are on a pace not seen since the recessionary period of the early 1990s. Sales of about 16 million vehicles in a year are considered healthy.

The downtrend again hit a wide swath of auto makers, with the Big Three taking the brunt of it. **General Motors** Corp., reported that its sales of cars and light trucks declined 26% to 231,314.

Ford Motor Co.'s sales dropped 13% to 155,866, likely the company's worst July since the early 1980s, according to company sales analyst George Pipas. **Chrysler** LLC reported a 28.8% drop to 98,109.

In another weak month for a once strong performer, sales at **Toyota Motor** Corp. fell 11.9% to 197,424 vehicles.

Honda Motor Co. has bucked the trend in recent months, thanks to the popularity of its small cars such as the Civic and Fit. But sales fell 1.6% to 138,744, surprising analysts. Sales of Honda passenger cars rose 14%, although truck sales plummeted 22%. **Nissan Motor** Co. claimed one of the few bright spots in the market, with an 8.5% gain in July U.S. sales to 95,319, a figure observers attributed to large incentives for consumers.

Auto makers reiterated that they could have sold more vehicles in July but lacked enough of the models that customers wanted. GM officials forecast that vehicle shortages might cost the industry as much as 300,000 units in lost sales this year. Sales of crossover vehicles—a segment hurt by the dropping residual values of trucks and sport-utility vehicles—also fell. GM's total truck sales tumbled 35%.

The auto makers continue to rely on incentives to unload bulging inventories of trucks and SUVs on its dealer lots. Ford's Jim Farley, global vice president for marketing and communications, said the auto maker will ratchet up truck incentives in August, and GM officials said they would revive incentives that had expired.

Ford is pursuing its leasing customers, enticing them with new deals designed to persuade them to buy their next vehicle. Chrysler is extending discounted six-year financing to more products.

Customers such as Tracy Stone, a 35-year-old from Fremont, Neb., are taking advantage of those deals. He bought a GMC Sierra truck in early July because the discounts were too good to resist. The sticker price was $20,000; Mr. Stone, who manages his own machine-parts business, bought the vehicle for $14,000. "It's a disposable truck," he said. "Four years and you can throw it away, seriously."

Mr. Farley said trouble in auto sales would be further complicated by a constricting credit market, which had forced auto makers to reduce leasing availability. GM officials played down those concerns. "I think the tightening has already taken place. I don't see it getting worse," said Mark LaNeve, GM's sales chief.

Overall, July sales were pushed down by a weak economy, tightening credit and a soft housing market, all factors likely to hurt auto sales in the months ahead, too. At the same time, auto makers are seeing a shift: American consumers long enamored with trucks and SUVs are now looking for fuel-efficient cars. *—Kate Linebaugh contributed to this article.*

Nortel's loss for quarter triples

By Sara Silver
And Ben Dummett

Nortel Networks Corp.'s second-quarter loss widened sharply, hit by restructuring charges and slower spending by U.S. telecom carriers; shares fell sharply Friday.

Nortel posted a loss of $113 million, or 23 cents a share, compared with a loss of $37 million, or seven cents a share, in the year-earlier quarter. The latest results include restructuring charges of $67 million, a loss of $21 million primarily from interest-rate swaps and a gain of $34 million from currency fluctuations. The year-earlier results included a regulatory-investigation expense of $35 million, a gain of $69 million due to changes in foreign-exchange rates and restructuring charges of $36 million.

Revenue rose 2.3% to $2.62 billion, but $314 million of that was previously deferred revenue, which produces sales in accounting terms but no new cash.

Nortel shares fell 15% to $6.52 in New York Friday.

GLOBAL BUSINESS BRIEFS

Schneider Electric SA

Acquisitions, sales growth bolster full-year forecast

France-based **Schneider Electric** SA, which makes equipment for electrical distribution, reported a 17% rise in first-half earnings, helped by strong organic growth and price increases, and raised its full-year growth forecast. Net profit rose to €851 million ($1.3 billion) from €729 million a year earlier, while revenue was up 8.4% to €8.95 billion. Acquisitions and strong sales growth in Europe offset the effects of the weaker dollar, which hit sales by €481 million, the company said. As a result, Schneider increased its full-year outlook, saying it now expects organic revenue growth, which strips out new acquisitions and exchange-rate fluctuations, of at least 8%. Since the start of the year, Schneider shares have lost about 24% of their value.

Alliance & Leicester PLC

Alliance & Leicester PLC, which is being acquired by Spain-based **Banco Santander** SA, said it swung to a net loss in the first half, weighed down by write-downs and higher funding costs. The U.K. mortgage lender posted a net loss of £23.9 million ($47.2 million), compared with a net profit of £184 million a year earlier. The bank blamed market turbulence for £209 million in impairments and fair-value declines on credit investments and said that higher funding costs since the start of the credit crunch took an additional £70 million off profit. Net-interest income fell 14% to £355 million, while total income was down 21% to £578 million. For the full year, A&L said it expects funding costs to be £150 million higher than in 2007. Pending shareholder approval, the deal is expected to be completed in October.

Ahold NV

Ahold NV reported a slight drop in second-quarter sales, but its shares rose after the food retailer kept its full-year forecast as many peers in the U.S. issue profit warnings. The Amsterdam-based retailer, which operates the Stop & Shop and Giant-Landover supermarket chains in the U.S. and Albert Heijn in the Netherlands, said sales fell to €5.78 billion ($8.98 billion) from €5.83 billion a year earlier, hurt by the weak U.S. dollar. Stripping out currency fluctuations, sales rose 7.3%. Ahold said sales growth in Europe and the U.S. was helped by price cuts and promotions. Ahold stock was up 5.8%, or 43 European cents, to close at €7.75 in Amsterdam Friday. Ahold is due to report full second-quarter earnings Aug. 28.

Linde AG

Linde AG posted a 49% jump in second-quarter net profit, helped by growth in its engineering and gases divisions as well as lower taxes. The Germany-based industrial-gases and chemicals company posted net profit of €215 million ($334.1 million), up from €144 million a year earlier, partly because of tax savings related to its acquisition of BOC Group in 2006. Net revenue increased 10% to €3.34 billion from €3.03 billion. The company said it expects sales at its engineering and gases divisions to grow despite the economic slowdown, with earnings outpacing sales. Linde confirmed its target for 2010, with an operating profit of €3 billion and a return on capital employed of at least 13%.

Fortis NV

Dutch-Belgian bank and insurance company **Fortis** NV said Gilbert Mittler, a member of its group executive committee, will take a new role as special adviser to acting Chief Executive Herman Verwilst. The move follows the ouster of Jean-Paul Votron as chief executive officer last month, after Fortis was forced to raise €8.3 billion ($12.9 billion) to strengthen its financial position by suspending dividends and issuing new shares. In his previous position, Mr. Mittler was responsible for finance, risk and general counsel, a post that will now be divided into three departments. New Chief Financial Officer Lars Machenil, Chief Risk Officer Fred Bos and General Counsel Jeannine Quaetaert will report directly to Mr. Verwilst, the company said.

Bulgari SpA

Italian luxury-goods company **Bulgari** SpA said net profit fell 8.8% in the second quarter, hit by higher taxes and operating expenses. The Rome-based company said net profit totaled €31.4 million ($48.8 million), down from €34.4 million a year earlier. Despite economic challenges, Bulgari said revenue rose 4.8% to €274.7 million, as sales of its biggest product segment, jewelry, rose 10%, while perfume sales grew 32%. Still, the company saw declines in watch sales and sales from the Americas. Bulgari said it expects full-year sales, operating profit and net profit to come in at the lower end of its previous forecast range. Bulgari has said it expects full-year growth of 8% to 12% in sales and net profit in 2008.

Hongkong Land Holdings Ltd.

Singapore-listed **Hongkong Land Holdings** Ltd. said its first-half underlying net profit rose 56% from a year earlier on higher rental income from Hong Kong and Singapore. But chairman Simon Keswick said income from commercial properties may increase at a slower pace in the second half, as rents in Asia reflect the impact of the weaker global economy and volatile financial markets. Hongkong Land, a unit of Singapore-listed conglomerate **Jardine Matheson Holdings** Ltd., said its underlying net profit for the six months ended June was US$242 million, up from $155 million a year earlier. Gains from the revaluation of investment properties rose to $1.41 billion from $1.16 billion. First-half revenue fell 19% to $319.2 million from $392.9 million.

HCL Technologies Ltd.

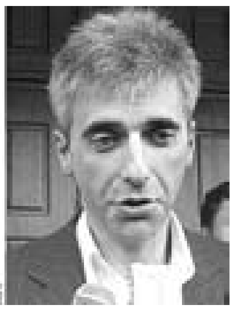
HCL Technologies Ltd., India's fifth-largest software exporter by sales, said its fiscal fourth-quarter net profit plunged 71%, hurt by foreign-exchange losses on a weaker rupee. Net profit in the April-June period slumped to 1.41 billion rupees ($33.4 million) from 4.86 billion rupees a year earlier. The company recorded a foreign-exchange loss of three billion rupees in the quarter, compared with a gain of 2.5 billion rupees a year earlier. The rupee lost more than 7% against the U.S. dollar in the just-ended quarter. Revenue rose 35% to 21.68 billion rupees, said the company, which reports its results according to U.S. accounting standards. Other net income, including from investments in mutual funds, fell to 355 million rupees from 369 million rupees a year earlier.

—Compiled from staff and wire service reports.

ECONOMY & POLITICS

RUSSIA

Khodorkovsky ex-partner is convicted of murders



A MOSCOW court convicted a former business partner of jailed tycoon Mikhail Khodorkovsky of conspiracy in five contract murders on Friday and sentenced him to life in prison.

The Moscow City Court found Leonid Nevzlin, left, guilty of five counts of murder, five of attempted murders, and one of armed robbery.

In emailed comments relayed by a spokeswoman, Mr. Nevzlin, who has been living in self-imposed exile in Israel since 2003, described the case against him as reminiscent of "Stalin's terror."

Judge Valery Novikov ordered Mr. Nevzlin to serve his sentence in a high-security prison. Israel has refused Russian requests for his extradition. *—Associated Press*

U.S.

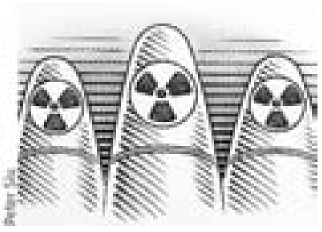
Rate of new HIV infections underestimated for decade

THE U.S. HAS BEEN underestimating the rate of new HIV infections by 40% for nearly a decade, officials of the U.S. Centers for Disease Control and Prevention said. The CDC now says an estimated 56,300 people a year are becoming infected with the virus, up from the old rate of 40,000 people a year.

More than one million people in the U.S. are infected with human immunodeficiency virus, or HIV. Some 33 million people worldwide are living with HIV-AIDS and another 25 million have died from it, most of them in sub-Saharan Africa. The new rate is based on improved counting and statistical methodology by the CDC. *—Marilyn Chase*

INDIA

U.N. inspection deal eases way for U.S. nuclear pact



THE BOARD of governors of the United Nations' atomic watchdog unanimously approved an inspections agreement with India that is a key precondition to completing a nuclear deal between India and the U.S.

"It's an important day for India," Indian Prime Minister Manmohan Singh said on Indian television. Thanking members of the International Atomic Energy Agency's board after the vote, he said the nuclear deal with the U.S. "is good for India and the world."

The deal could see the U.S. supply India with nuclear fuel and technology for civilian purposes.

Bush aims to soothe allies on trip to Asia

Region is concerned about China's might and U.S.'s priorities

BY JOHN D. MCKINNON
Washington

U.S. PRESIDENT George W. Bush leaves for a visit to Asia on Monday that will help mark China's emergence on the world stage but will also seek to reassure longtime allies in the region that the U.S. still stands with them. To some of China's nervous neighbors, though, the U.S.'s actions—or lack thereof—don't always match its words.

The highlight of Mr. Bush's trip will be his four-day stop in Beijing to attend the Olympics—perhaps the most visible symbol yet of China's rapid rise as an international player. He is expected to publicly cheer America's Olympic athletes while privately pressing Chinese leaders for substantive progress in granting more political rights to its people, particularly in restive Tibet.

He plans to urge Chinese President Hu Jintao, for example, to use an expected new round of talks in October to invite the Dalai Lama, the exiled Tibetan spiritual leader, to return to his homeland and take an active role in making the region's development more equitable for Tibetans.

But Mr. Bush's trip—thought to be the first time that a sitting U.S. president has attended an overseas Olympics—has added to the anxiety of some of China's already-nervous neighbors. Mr. Bush gives a major speech in Bangkok on Thursday that seeks to underscore U.S. interests in Asia broadly. That will follow a quick stop in South Korea to highlight its growing commercial and cultural ties with the U.S. and to push for a free-trade pact that is stalled in the U.S. Congress.

Previewing the speech in a roundtable interview with Asian reporters, Mr. Bush acknowledged the concern of some longtime allies. "If I were Thailand, I'd be asking, 'What about us? Will you remember other nations?' " he said in response to a question. "And the answer is, 'Absolutely.' "

Despite occasional complaints in Asian capitals of a perceived lack of U.S. attention, Mr. Bush insisted that his administration's policy has produced better relations with everyone in the region. "Our foreign policy has been robust in the Far East," he said. "Not many presidents could say, in the history of U.S. diplomacy, that relations with South Korea, Japan, China and Thailand are strong and robust. A lot of times, if you're friends with one, you made it hard to be friends with another."

Many of America's oldest allies in the region, such as Thailand, where Mr. Bush will mark the 175th anniversary of U.S. relations, worry that U.S. attention is consumed by problem areas elsewhere, such as the Middle East and Afghanistan, as well as local Asian trouble spots—notably North Korea.

At the same time, as part of its strong free-trade agenda, the Bush administration has sought better relations with all governments in the region, including traditional allies such as Japan, South Korea and Taiwan and emerging powerhouses like China and India. As Asia's interrelated markets have developed, neighbors have begun to see the need to have better relations generally in the region.

Now, though, countries like Japan, South Korea and Thailand fear that the live-and-let-live U.S. attitude toward Asia is encouraging China to assert its military might in addition to its economic power. They point, for example, to China's increasingly far-ranging navy, which is pushing farther into the Pacific. That could lead to confrontations, some analysts say, for example over the vital sea lanes that are lifelines for many Asian countries, Japan in particular.

"There's a concern that we've stood by and watched" as China has modernized its military, says Michael Auslin, an Asia expert at the conservative American Enterprise Institute. Increasingly, "many nations...feel trapped" in the shadow of China's military influence.

Beijing-bound U.S. President George W. Bush is seen here with Olympic softball pitcher Jennie Finch.

China's military spending, while growing rapidly, remains far smaller than that of the U.S., both in absolute terms and as a percentage of gross domestic product. The U.S. has been encouraging Japan to bolster its own defensive capabilities to better serve as a regional counterweight to China.

China's growth also has earned it diplomatic leverage, not just on regional security issues but on global ones such as climate change and trade policy.

"There is some worry, especially among the Japanese, that the U.S. is going to be too focused on China," says Adam Segal, the Maurice Greenberg senior fellow for China studies at the Council on Foreign Relations.

While the Bush-administration officials have fostered strong relations with Japan, India and China all at once—a feat previously regarded as nearly impossible—"there is still something...to the critique that they were overly focused on the Middle East," Mr. Segal says. While perceived U.S. slights to Asia have been largely symbolic ones, "symbols matter in Asia policy." Some allies in Southeast Asia also view the rise of India with concern, says Christopher Griffin of the American Enterprise Institute. But expansion of U.S.-Indian security cooperation should help ease those worries, he adds.

The White House consciously chose Bangkok as the most appropriate location to address the concerns. Thailand has been a reliable ally, and it recently assumed the rotating chairmanship of the Association of Southeast Asian Nations.

But the speech is aimed at East Asia more broadly. It will highlight what the administration views as America's strong relations, and the improvements that have occurred in relations with some big and vital countries, such as India and Indonesia. It also will underscore the improvements in political freedoms in places like Mongolia.

In particular, the president likely will reassure the region that countries can develop their relations with China while hedging against China's rise as a military power through the network of U.S.-backed security alliances.

—Gordon Fairclough in Shanghai contributed to this article.

U.S. ties Pakistan intelligence to Kabul attack

BY JAY SOLOMON

WASHINGTON—Officials in the Bush administration say renewed tensions between India and Pakistan could be damaging U.S. efforts to conquer the Taliban and achieve stability in Afghanistan.

These concerns surfaced Thursday when the U.S. charged that Pakistan's intelligence agency helped militants carry out an attack last month on the Indian Embassy in Kabul that killed 58 people.

Pakistan and Afghanistan agreed Sunday to cooperate in efforts to stop cross-border terrorism, Pakistan's Foreign Ministry said. Pakistan Prime Minister Yousuf Raza Gilani met Afghan President Hamid Karzai on the sidelines of the South Asian Association for Regional Cooperation in Sri Lanka, according to the Associated Press.

They agreed to develop "a common strategy to overcome the challenges posed to the security and stability of both countries by terrorism and extremism," the ministry said in a statement, released at the conclusion of the summit. The eight SAARC member nations adopted a regional antiterrorism cooperation agreement and approved the immediate establishment of a food bank to cope with regional shortages triggered by rising prices.

Indian Prime Minister Manmohan Singh said Saturday that the recent attack on the embassy in Kabul and a string of bombings in Indian cities "are gruesome reminders of the barbarity that still finds a place in South Asia. It remains the single biggest threat to our stability," he said, according to the AP.

U.S. officials said Thursday they concluded that elements of Pakistan's Inter-Services Intelligence, or ISI, aided the July 7 attack, based on telecommunications intercepts linking Pakistani intelligence officials to Afghan insurgents.

The U.S. officials said India's security services drew similar conclusions based on their own telecommunications intercepts and intelligence.

Pakistan's government Friday said it needs to purge Taliban sympathizers from its intelligence service but denied that the ISI helped militants in the bombing, the AP reported.

Since the collapse of the Taliban regime in the U.S.-led war that followed the Sept. 11, 2001, attacks in the U.S., India and Iran have expanded their influence in Afghanistan. Some U.S. officials say they are concerned that the growing roles of Pakistan's rivals in Afghanistan are feeding the ISI's desire to support the Taliban and other insurgent groups.

ECONOMY & POLITICS

China takes media steps

Hu gives briefing to foreign press; Web sites unlocked

By Rebecca Blumenstein, Andrew Batson And Geoffrey A. Fowler

Getty Images

Chinese President Hu Jintao, at a meeting Friday with foreign reporters in Beijing, defended his country's efforts in hosting the Olympic Games.

BEIJING—China made two gestures toward greater openness as President Hu Jintao held his first news conference ever with foreign journalists, while authorities unblocked several Web sites that they had censored in recent weeks, provoking blistering international criticism.

Mr. Hu, appearing stiff but confident in a rare gathering with the media Friday, said he hoped the Olympic Games would leave an enduring legacy for China, and help convince the world that its most populated country is committed to a peaceful rise to prosperity.

"We will never pursue an expansionist role," President Hu told a group representing 25 news-media organizations from around the world. "The development we pursue is peaceful, open and cooperative by nature. China's development in no way threatens the interests [of other nations]."

Mr. Hu lifted hopes the Olympics could pave the way for more changes within China, saying he would press forward with both economic and political overhauls, as well as policies to tackle China's environmental problems.

The Games have been widely described as China's coming-out party, a chance to showcase its formidable economic achievements to the world. But they have brought unprecedented scrutiny to the way China is run. Opposition to its policies in Tibet and Darfur exploded in ugly protests during the Olympic-torch relay in Europe and the U.S. Critics charge that its leaders haven't lived up to commitments to improve human rights, clear Beijing's smoggy air and lift Internet restrictions ahead of the Games.

Without fanfare, several previously banned Web sites, including ones run by human-rights group Amnesty International and the Chinese version of Wikipedia, were suddenly accessible Friday inside the Games' main news center. The sites were also available, albeit inconsistently, in cities around China.

Web access for journalists covering the Games had become a contentious issue for the International Olympic Committee this week, when access to sites critical of China's government were blocked in Olympic venues. The IOC had previously said it received assurances from Beijing that Internet access for reporters covering the Games would be completely uncensored.

Mr. Hu defended China's efforts on the Olympics and said its government and people "have been working in real earnest to honor the commitments made to the international community." He added they have worked closely with the IOC since China was awarded the Games in 2001.

"I don't think that politicizing the Olympic Games will do [any] good," Mr. Hu said. He urged that those with differences "enter into consultations on an equal footing to narrow our differences and expand our common ground on the basis of mutual respect."

On the economic front, Mr. Hu voiced concerns about persistently high inflation that has sent food prices soaring, but signaled his administration's commitment to pursue growth as well. "We must maintain steady, relatively fast development and control excessive price rises as the priority tasks of macro development," he said.

Despite continuing economic challenges both at home and abroad, Mr. Hu said, "we will continue to press ahead with comprehensive reform in this country, including political reform. By so doing we want to enhance the socialist democracy and continue to build a socialist country under the rule of law."

As he entered the room, Mr. Hu, who has long shunned the public spotlight, shook hands with each of the journalists in attendance, who waited in line for his arrival.

Just as the moves toward openness signaled progress, they also demonstrated China's penchant for control. Although reporters from some news-media organizations, including The Wall Street Journal, Reuters, Agence France-Presse and NBC News, were invited to attend, many foreign journalists weren't.

The news conference could signal a greater public role for Mr. Hu, especially as political jockeying for his successor begins in earnest in the coming three to four years, said Victor Shih, a professor at Northwestern University in Illinois. Mr. Hu's predecessor, Jiang Zemin, spoke mostly in joint appearances with foreign leaders or highly scripted interviews.

To choose the next leader, "they will have to negotiate an outcome somehow," said Mr. Shih. "It will help Hu Jintao if he has a higher profile in foreign policy."

U.S. lawmakers pushing bill for offshore drilling

By Stephen Power And Ian Talley

WASHINGTON—A group of Democratic lawmakers is banding with Republicans to draft legislation that would ease the federal moratorium on offshore oil drilling while ending a tax break for oil companies.

The effort highlights the eagerness of some Democrats to break a deadlock in Washington over energy policy as Congress heads for a monthlong recess without having passed legislation to address high gasoline prices.

Many party leaders, including Democratic presidential candidate Sen. Barack Obama, have criticized proposals by President George W. Bush and the Republicans' presumptive presidential nominee, Sen. John McCain, to lift the offshore-drilling ban. But opinion polls indicate rising support among voters for increased domestic drilling, including in coastal areas where such activity is currently prohibited.

In a move that could signal a possible softening of Sen. Obama's position, his campaign on Friday issued a statement praising the bill but stopped short of an endorsement.

A spokesman for Sen. McCain said that while he "applauds the bipartisan effort," he wouldn't support the proposal because "he cannot and will not support legislation that raises taxes."

On Friday, 10 senators—five Democrats and five Republicans—announced legislation to open to drilling additional acreage in the Gulf of Mexico off Florida's western coast. The legislation would allow Virginia, North Carolina, South Carolina and Georgia to "opt in" to allowing drilling off their shores if their legislatures approve.

At the same time, the bill would raise billions of dollars for various conservation and energy-efficiency programs by making oil companies no longer eligible for a manufacturing tax credit. Some estimates have put the potential savings from such a move at $13 billion over 10 years.

The manufacturing tax credit seeks to encourage job creation in the U.S. by giving a tax break to all domestic manufacturers that produce goods in the country, including oil companies.

Within minutes of the senators' unveiling of the bill, Sen. Obama's campaign released a statement that praised the proposal as "a good faith effort" and "an important step in the process of reducing our dangerous dependence on foreign oil."

Asked whether Sen. Obama's comments signal an intention to support a relaxation of the ban, an Obama campaign spokesman said, "He welcomes this compromise as a first, bipartisan step....If a group of senators come to him with a good-faith effort to solve a major challenge like this one that contains some steps he doesn't like, he's not going to reject it out of hand." A person familiar with the matter said Sen. Obama is likely to elaborate in the coming days on steps he would pursue as president to boost domestic energy production.

Although Sen. Obama said he remained "skeptical" that new offshore drilling would reduce gasoline prices in the short term, his comments opened the door to working with the group. He said he welcomed "the establishment of a process that will allow us to make future drilling decisions based on science and fact."

There were signs that the measure could attract support from other Democratic leaders. While Senate Majority Leader Harry Reid (D., Nev.), said he didn't agree with all of the provisions in the proposal, he said, "I am hopeful this plan can begin to break the current legislative stalemate on the Senate floor."

The legislation would steer $7.5 billion to help auto makers and auto-parts makers retool their factories and another $7.5 billion to develop alternative-vehicle technologies, such as advanced batteries.

Those provisions—which aim to have the nation's vehicles using 85% nonoil fuel sources within 20 years—are similar to proposals that Sen. Obama has made in recent weeks.

A repeal of the manufacturing tax credit for oil companies, along with a proposed requirement that oil firms that haven't paid royalty fees on certain leases in the Gulf of Mexico ante up billions of dollars in payments, could prove more contentious. It was unclear how energy companies and their congressional allies would react.

Economic-aid debate heats up

By Amy Chozick And Elizabeth Holmes

With the U.S. unemployment rate hitting a four-year high, Sen. Barack Obama and Republican rival Sen. John McCain ratcheted up the debate about how to bolster the ailing economy.

The Democratic presidential contender called for an "emergency energy rebate" of as much as $1,000 to middle- and low-income families to be paid out as early as this fall and financed through a windfall-profits tax on oil companies. Sen. McCain reiterated his plan promoting corporate tax cuts while criticizing his opponent's economic proposals.

The comments came during a week when Sen. Obama sought to refocus his campaign on the economy, including high gasoline prices, a big concern for voters. But it remains to be seen how feasible either candidate's economic plan is. The next president will face an estimated $482 billion deficit in the fiscal year starting October 2009, and growing concerns over how to fund the country's Social Security and Medicare systems.

Friday, the Labor Department reported that the U.S. lost another 51,000 nonfarm jobs in July, bringing total job losses for the year to 463,000. That raised the unemployment rate to 5.7% in July from 5.5% in June.

"You can't afford to wait for relief. Right now, people are suffering," Sen. Obama said Friday at a town-hall meeting in St. Petersburg, Fla.

The economic plan the Illinois senator announced on Friday essentially repackaged ideas that he had been promoting already. Sen. Obama had previously called for a windfall-profits tax on oil companies, but he specified that the tax should last for five years and pay for rebates of $500 to $1,000 to lower-income families.

Sen. Obama said the rebate could help families offset the increased costs of gas and heating bills. The senator's existing economic plan also calls for a $1,000 tax rebate for certain households.

A second part of his plan, the senator said, is aimed at helping "jump-start job creation and [helping] local communities that are struggling due to the economic downturn." Under this effort, $25 billion would go toward state governments that face big budget shortfalls, and another $25 billion would be invested in the country's infrastructure and schools.

Sen. McCain reiterated his "Jobs for America" plan, unveiled in early July, that includes tax cuts for individuals and businesses of all sizes.

"To get our economy running at full strength again, we need to stay focused on creating jobs for our people, and protecting paychecks from the rising costs of food, gasoline and almost everything else," he said. "Above all, we need to get a handle on the cost of oil and gasoline and to regain energy independence for America."

Obama invites compromise on offshore-drilling bill

By Amy Chozick

CAPE CANAVERAL, Florida—Barack Obama said he would support an expansion of offshore drilling as part of a broader bipartisan U.S. energy bill, a more flexible approach than the Democratic presidential contender has previously demonstrated.

Sen. Obama, who has opposed further offshore drilling, on Saturday told reporters he "remains skeptical" of drilling provisions in pending legislation designed to lessen dependence on foreign oil and ramp up development of alterative energy, but he said he would be willing to compromise.

"If we can come up with a genuine bipartisan compromise in which I have to accept some things I don't like or the Democrats have to accept some things they don't like...that's something I'm open to," he said.

The issue of offshore drilling has sparked heated debates between Sen. Obama and his likely Republican rival, John McCain.

Sen. McCain supports expanded drilling off the nation's coastlines as a way to lower gasoline prices and help the economy. He has criticized Sen. Obama for opposing expanded drilling.

The McCain campaign saw an opening on Saturday to attack Sen. Obama for flip-flopping. "We hope Barack Obama will realize that his ongoing opposition to John McCain's realistic energy solutions and additional offshore drilling is wrong," campaign spokesman Tucker Bounds said in a statement.