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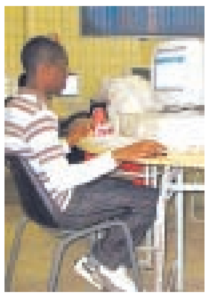

Microsoft is battling a low-cost rival for Africa

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Economists struggle to gauge the U.S. downturn

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Business & Finance

The U.S. Federal Reserve is poised on Wednesday to again cut its benchmark interest rate, possibly to 1%, as new reports on consumer confidence and home prices showed the nation's economy deteriorating sharply. Page 1

■ **The Dow roared higher** in late trading, closing up 11% despite gloomy news on consumer confidence. European markets rose as well. Pages 1, 20

■ **Oil prices and demand** continue to fall, but executives warn prices could ramp back up dramatically when the global economy rebounds. Page 19

■ **Persian Gulf states** are less flexible about investing in the West as their investment funds face big paper losses amid recent global stock declines. Page 3

■ **Russia stepped in** to resolve a dispute between one of the country's richest men and Deutsche Bank. Page 19

■ **Iceland's central bank** raised its key interest rate six percentage points to 18%. Page 2

■ **Boeing Machinists will vote** Saturday on a pact that would end a 52-day strike. Page 4

■ **Volkswagen shares** continued to climb after Monday's surge on investors' enthusiasm for Porsche's plans to buy three-quarters of VW's stock. Page 6

■ **Auto lender GMAC** is seeking a commercial-bank charter to access U.S. bailout monies and lower-cost loans. Page 6

■ **Higher oil prices boosted** third-quarter earnings at BP and Occidental Petroleum. Page 4

■ **Banco Santander posted** a 4.4% rise in net profit and said it had enough capital to make it through a downturn. Page 5

■ **Russia and China reached** agreement on an oil-pipeline deal under which Chinese firms will provide "considerable" loans to Russian firms. Page 10

■ **The dollar and euro** surged against the yen. Page 19

Markets 4 p.m. ET

MARKET	CLOSE	NET CHG	PCT CHG
DJIA	9065.12	+889.35	+10.88
Nasdaq	1649.47	+143.57	+9.53
DJ Stoxx 600	199.44	+4.40	+2.26
FTSE 100	3926.38	73.79	+1.92
DAX	4823.45	+488.81	+11.28
CAC 40	3114.92	+47.57	+1.55
Euro	$1.2478	+0.0023	+0.18
Nymex crude	$62.73	-0.49	-0.78

Money & Investing > Page 19

World-Wide

Sarkozy outlined measures to boost employment in France, including an additional 100,000 subsidized job contracts, and warned employers not to use the financial crisis as a cover for shedding workers. The moves came as new data showed a decline in European consumer confidence. Page 1

■ **Rebels advanced toward** Congo's eastern provincial capital of Goma, sending tens of thousands of civilians into a makeshift shelter as Congolese troops and U.N. tanks retreated.

■ **The U.S. is actively** considering talks with elements of the Taliban, in a major policy shift. Meanwhile, Pakistani and Afghan leaders vowed to seek dialogue with Taliban insurgents.

■ **A widening margin** of new and returning voters support Obama, a new poll shows. But the question of how heavily they will turn out for next week's election still lingers. Page 12

■ **Republicans appear to be** losing control of the debate over taxes in the U.S. Page 12

■ **Iraq's cabinet authorized** Maliki to reopen talks with the U.S. on a security pact. An Iraqi court sentenced to death a suspected al Qaeda militant for killing three U.S. soldiers in 2006.

■ **Syria ordered** an American school and a cultural center in Damascus closed in response to a U.S. attack on a village near the border with Iraq. Page 10

■ **A Russian court convicted** banker Alexei Frenkel of organizing the murder of central bank official Andrei Kozlov in 2006.

■ **Britain said it will** publicly list and ban entry of over 200 people whose extremist views threaten national security.

■ **The kidnappers** of Chinese oil workers in Sudan panicked when they saw a military aircraft and killed at least three hostages, Sudan said, contradicting China's claims of a botched rescue.

■ **Israel plans to hold** national elections in mid-February, a Parliament spokeswoman said.

■ **Spanish police detained** four alleged members of Basque separatist group ETA who are suspected of planning an attack.

EDITORIAL & OPINION

Orange split

Ukraine's major parties have picked an awful time to resume their long-running feud. Page 15

U.S. Fed is poised to cut key interest rate to 1%

Desires to avert recession, deflation drive latest effort

By Jon Hilsenrath

The U.S. Federal Reserve is widely expected to cut its benchmark interest rate again Wednesday, possibly to 1%, amid a darkening economic outlook.

The case for more rate cuts strengthened Tuesday, with new reports showing the U.S. economy deteriorating sharply. Consumer confidence tumbled to a record low in October as credit markets collapsed. The percentage of Americans saying jobs were hard to get—at 37.2%—is at a 15-year high and seems sure to go higher.

The housing market also took a turn for the worse. Earlier in the summer, several housing indicators suggested that home-price declines might be slowing. But the S&P/Case-Shiller home-price index for 20 large cities was down 16.6% in August from a year earlier, a record decline. Falling home prices feed a downward housing spiral, creating pressure for more foreclosures and mortgage losses among banks.

The Fed has already pushed its

Please turn to page 31

Dow leaps 11% as investors seek bargains

By Peter A. McKay

U.S. stocks roared higher in late trading after earlier being tripped up by a rock-bottom reading of U.S. consumer confidence.

The Dow Jones Industrial Average closed at 9065.12, up 889.35 points, or 11%. It was only the fifth gain this month, but the second-biggest rally in the index's history in point terms. Only the 936.42-point rally on Oct. 13 was larger.

ABREAST OF THE MARKET

Rallies in overseas shares and favorable news at two blue-chip companies, **Boeing** and **General Motors**, boosted market participants' mood early in the session.

That enthusiasm briefly wavered after the release of downbeat economic data but came back as the closing bell approached, with buyers rushing in either to rebalance beaten-down portfolios or to place speculative bets at bargain-level prices.

"People are starting to take a long-term view, and the long-term looks pretty good," said Anthony Conroy, head trader at BNY ConvergEx, a New York brokerage firm.

Alluding to the Dow's steep decline from its record about a year

Please turn to page 31

AFP

French President Nicolas Sarkozy, center, visits a new **jobs center** in Rethel, France, Tuesday, with Finance Minister Christine Lagarde, second from right.

Sarkozy unveils job plan; Europe data show slump

By Sebastian Moffett

PARIS—French President Nicolas Sarkozy unveiled a series of employment-boosting measures, including 100,000 additional subsidized job contracts, as new data showed a decline in European consumer confidence.

Mr. Sarkozy said his government will increase to 330,000 the number of subsidized job contracts it will finance in 2009. The figure is 100,000 more than originally proposed.

He also warned employers not to use the crisis as a cover for shedding workers: "I won't tolerate any cynical or opportunistic strategies," he said in a speech, pointing to "those who might use the current crisis to justify reducing production and jobs."

Mr. Sarkozy's speech came as Italian Economy Minister Giulio Tremonti met with Bank of Italy Gov. Mario Draghi and other top financial regulators to discuss challenges facing Italian banks.

Also on Tuesday, several European economies announced declines in consumer confidence for October, presaging what could be a long and sharp recession for the Continent. The fear is that, as businesses cut down their hiring plans and lay off workers, households will feel the pinch and spend less. That would further damage businesses.

In the U.K., a Confederation of British Industry survey reported that sales on U.K. high streets fell for a seventh consecutive month in October and that retailers expect lit-

Please turn to page 31

Iceland increases key rate to 18%

IMF backs effort to support krona, prevent capital flight

Iceland's central bank raised its benchmark interest rate by six percentage points to 18% in a bold attempt to support the Icelandic krona, as the island moves to reanimate a foreign-exchange market frozen since the collapse of its banking system earlier in the month.

The move makes clear how critical currency is in the hard-hit smaller countries at Europe's perimeter. Raising rates is a tool generally used to cool overheating economies and lower the risk of inflation. When the economic outlook is bleak, rates are usually cut to spur investment and growth.

By ***Charles Forelle*** *in Brussels and* ***Bob Davis*** *in Washington*

But in countries like Iceland and Hungary—which are both seeking help from the IMF—the need to defend the currency is coming first. Hungary last week raised rates three percentage points to bolster a wilting forint. Iceland, which depends heavily on imports, desperately needs a functioning foreign-exchange market so Icelanders can use their kronur to buy euros or dollars, and with them the goods they need.

The rate moves are large, but not record-setting by historic standards. In September 1992, Sweden's central bank raised rates to 75% from 16% to ward off a run on its currency. A few days later it took them all the way to 500%.

Iceland's rate increase—which more than reverses a cut of 3.5 percentage points made just two weeks ago—was a condition of the International Monetary Fund, the central bank said. The IMF last week reached a preliminary accord for a $2 billion loan to the beleaguered nation.

Amid other signs that countries are eager for currency stability, Poland's government approved a timetable that calls for the country to adopt the euro in 2012. Polish President Lech Kaczynski has resisted the move, but on Tuesday he said the "finance minister made some strong arguments in favor of fast euro adoption," including that Poland would have been better insulated from the fall in Hungary's currency. The Polish zloty has lost significant ground against the euro since midsummer, but strengthened 3.6% on Tuesday.

Iceland's prime minister was in Helsinki on Tuesday, talking with his Nordic counterparts about further assistance. He is seeking $4 billion in addition to the $2 billion IMF loan, and he told reporters in the Finnish capital that Iceland also has requested help from the U.S. Federal Reserve and the European Central Bank. An IMF lending program helps assure other nations that Iceland will make necessary changes to bolster its economy—and lessen the chances their money will be wasted.

IMF and Icelandic officials have been worried about the krona, which slid after beginning the year at 92 to the euro. It touched 156 to the euro, according to the ECB, on Oct. 3, as the crisis broke out. It has since effectively stopped trading. Investors off the island aren't much interested in holding kronur, and Iceland recently imposed restrictions on selling kronur for foreign currency.

Getting the foreign-exchange market going again comes with a big risk: Investors could use the opportunity to dump kronur and take capital out of the country. A further collapse in the krona would also kick up inflation, already running at 15.9% annually.

To provide a value for the krona, Iceland's central bank has been holding a local foreign-exchange auction; on Tuesday, the currency was set at 152.50 to the euro. But analysts say the krona could dramatically weaken, perhaps to 250, as offshore trade is restarted.

That's something the IMF wants to avoid. The "immediate objective" of the IMF's plan—which could be approved by the agency's executive board in coming days—is to "stabilize the krona," said Poul Thomsen, the head of the IMF's mission to Iceland, in an interview Monday. "There is a substantial risk of capital flight."

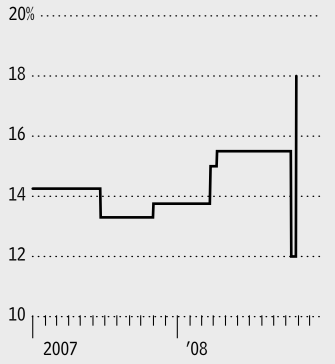
Tuesday's rate increase is designed to encourage investors to hang on to Icelandic assets and keep krona deposits in local banks. In a statement, the central bank said it believes that contracting demand in Iceland will swing the country's current-account deficit into balance or into surplus. That would boost the krona, it said, and quell inflation. "If forecasts materialize, the policy rate will be reduced," the central bank said.

What happens in coming quarters is far from clear. In the interview, Mr. Thomsen said the IMF wouldn't insist on immediate fiscal belt-tightening, but would delay such measures until perhaps 2010. That's because Iceland came into the crisis with relatively low levels of government debt. Analysts say, though, that the country will have to assume, in some fashion, a portion of the debt incurred by its now-collapsed banks. That will change the fiscal picture. The IMF may not be so relaxed with other countries seeking aid, such as Ukraine and Pakistan.

—Joel Sherwood, David McQuaid and Edith Balazs contributed to this article.

Bouncing

Iceland's policy interest rate



Source: Central Bank of Iceland

CORRECTIONS & AMPLIFICATIONS

Fund-of-hedge-funds manager **Gottex Fund Management Holdings** AG has erected a so-called gate that prevents investors from withdrawing funds, but has applied it to only one of its funds, the ABI fund. An Oct. 27 Financial News article didn't say the gate applied to a particular fund.

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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FINANCIAL CRISIS & REPAIR

Gulf funds too hit to help?

Calls by Brown, U.S. for fresh infusions face a roiled Mideast

BY CHIP CUMMINS

DUBAI—Western officials came knocking on the door of the oil-rich Middle East Tuesday, seeking funds amid today's global financial crisis. But governments here and their big investment funds are licking their own wounds from the fallout.

U.S. Deputy Treasury Secretary Robert Kimmitt started a week-long tour of the Persian Gulf on Tuesday, telling an audience in Dubai that the U.S. was eager for fresh investment from the region. And British Prime Minister Gordon Brown asked nations enjoying big budget surpluses, like those in the Persian Gulf, for more money for the International Monetary Fund, ahead of his own trip to the region this weekend.

But the calls come as the Gulf's handful of government investment funds face big paper losses amid recent global stock-market carnage. Meanwhile, U.S. benchmark crude has fallen by more than half from its July highs, robbing Mideast governments of some of the surplus cash they looked set to rake in a few months ago.

Most governments are still a long way from seeing their current budget surpluses turn into spending deficits. The IMF estimates that Gulf states, on average, will stay in the black as long as crude prices keep above $47 a barrel. But they are now a lot less flexible when it comes to foreign investments and financial commitments.

In the past two years, Mideast funds have invested heavily in the West's banking sector, and they are now holding big paper losses on those bets. Equity investments by Mideast and Asian funds in six U.S. and European banks are down between 19% and 66% so far since January 2007, according to a report released Tuesday by Deutsche Bank.

Officials at investment funds across the Middle East have stressed they are long-term investors and aren't worried about individual, paper losses. But the region's biggest funds are also heavily exposed to sharply falling global equities more broadly, just like many big U.S. pension funds and university endowments.

The **Abu Dhabi Investment Authority** has said in the past that it invests as much as 55% of its portfolio—estimated by McKinsey & Co. at above $500 billion as of two years ago—in developed-world equity markets. As much as an additional 12% is invested in emerging-market equities. The **Kuwait Investment Authority**, with assets estimated at $200 billion in 2006, has said its portfolio is about 60% invested in global equities markets.

"ADIA and KIA have significant exposure and probably have taken a big hit," said Eckart Woertz, a Dubai-based analyst at the Gulf Research Center.

KIA's investments have sparked public criticism at home, where parliament has questioned the wisdom of a $3 billion investment in **Citigroup** Inc. and a $2 billion investment in **Merrill Lynch** & Co. earlier this year. Kuwait was a relatively conservative overseas investor for decades, keeping much of its overseas holdings in ultrasafe U.S. Treasuries. That changed just a few years ago, when the fund's new head, Bader Al Sa'ad, pushed the fund to invest more aggressively.

There have been few public acknowledgements of losses. Qatari Prime Minister Sheikh Hamad bin Jassim bin Jabor al Thani told reporters earlier this week that the financial crisis wouldn't slow his country's overseas investments. The Qatar Investment Authority, which Mr. al Thani heads, earlier this month led an $8.83 billion capital infusion into **Credit Suisse Group**.

An ADIA spokesman declined Tuesday to comment. Phone and email requests for comment from KIA in recent days haven't been returned.

Eroded resources

Western governments asked for support from the Middle East Tuesday, but the region's funds are licking their own wounds.

Inception	Fund	Assets under management, in billions
1976	Abu Dhabi Investment Authority*	$875
N/a	Saudi Arabia (various funds)	350
1953	Kuwait Investment Authority	264
2006	Investment Corp. of Dubai*	82
2005	Qatar Investment Authority	60
2002	Mubadala Development Co.*	10

* United Arab Emirates
N/a = Not available

Note: Data reflect latest available figures as reported by individual entities or other authoritative sources
Sources: Various public sources, GAO, Deutsche Bank Research

Aegon secures $3.8 billion from Netherlands

BY NICOLAS PARASIE

PARIS—**Aegon** NV of the Netherlands became the first major European insurance company to seek a government capital injection, in a sign global financial rescue efforts are shifting from banks to insurers.

Aegon said the Dutch government will pump €3 billion ($3.8 billion) into the company. Aegon follows in the footsteps of banking and insurance firm ING Groep NV, which one week earlier secured €10 billion in state funding to help it weather the credit storm.

Aegon's move to secure government support comes amid growing concerns about the outlook for the insurance industry, which has so far survived the financial crisis relatively well, with the exception of American International Group Inc. and the collapsed Japanese insurer Yamato Life Insurance Co. While most insurers are financially sound and managed to avoid disastrous investments in subprime-backed bonds, their investments in corporate bonds and stocks have taken a beating amid the market turmoil. That, analysts say, could ultimately force more of them to turn to their shareholders, or to governments, for capital to shore up their finances.

CORPORATE NEWS

EUROPEAN UNION

Kroes warns states to avoid illegal subsidies

Associated Press

EUROPEAN governments must avoid giving illegal subsidies to struggling industries and instead act together to support growth and innovation, said European Competition Commissioner Neelie Kroes, left.

"There is no national route out of this crisis. It would be a disaster to start a subsidy race," Ms. Kroes warned. Spurred by fears that recent financial rescue-packages might prompt governments to extend aid to other sectors, she called for "a calm and clear Europe-wide response, not a series of divergent national responses."

European Competition rules need to remain "rigorously enforced," she said. *—Peppi Kiviniemi*

BANKING

Kazakhstan will pump $5 billion into top banks

Corbis

KAZAKHSTAN plans to buy about $5 billion of newly issued shares in the country's top four banks to stave off a renewed banking crisis, the nation's prime minister said Tuesday.

The decision to buy into the banks—**Alyans Bank** AO, **BTA Bank** AO, **Halyk Bank** AO and **Kazkommertsbank**—is in line with recommendations from the Kazakh financial-markets regulator, Premier Karim Massimov said. Kazakhstan, the largest economy in Central Asia, over the past year has seen inflows of foreign capital dry up as the global credit crunch has unfolded. The state could end up with 25% of voting shares in the lenders, Mr. Massimov said. *—Associated Press*

CONSUMER PRODUCTS

AB Foods and ADM forge packaged-oil joint venture

Inmagine

ASSOCIATED British Foods PLC said it is combining its North American unbranded packaged-oil business with that of **Archer-Daniels-Midland** Co. of the U.S. in a 50-50 joint venture.

In addition to vegetable oil, the venture—named Stratas Foods—will produce shortening, margarine and pan spray but won't include AB Foods's consumer brands such as Mazola corn oil, Argo corn starch and Karo corn syrup. The British company, 55%-owned by the founding Weston family, is contributing $38 million in assets, while ADM will provide packaging equipment at four of its facilities in the U.S. *—Michael Carolan*

Boeing pact faces a vote

After 52-day strike, machinists to decide Saturday on accord

BY J. LYNN LUNSFORD

IN REACHING a tentative deal to end a nearly two-month strike, **Boeing** Co.'s machinists proved again that at least one manufacturing work force can confront its employer over thorny issues such as job security, pensions and health care.

Officials with the International Association of Machinists and Aerospace Workers began Tuesday to lobby the union's 27,000 members—who spent 52 days on the picket line— to vote Saturday to ratify a new agreement that gives workers greater assurances of job security while still allowing Boeing to streamline its manufacturing.

Boeing officials said that despite making several concessions, company officials believe they won some key victories, including an agreement by the union to extend the contract by a year to four years. This detail alone will enable Boeing to more reliably guarantee that deliveries of its flagship 787 Dreamliner won't be interrupted in three years, just as the production lines are getting up to full speed. The 787 program is already behind schedule, and the company is under heavy pressure from airline customers to keep to the current production plan.

The strike in the midst of global economic turmoil was risky, but the machinists found leverage in the fact that Boeing has 3,725 airplane orders that need to be filled. In addition, the union's specialized work isn't easily replaced in an industry where the safety of the final product is paramount.

The agreement was hailed by union leader Tom Wroblewski, president of District 751, as a pivotal victory over what union officials believe is a push by the company to reduce its reliance on organized labor. "We're a strong unit now, but it won't always be that way if the company offloads our work and chisels away our benefits," he said. "What our members did this time was preserve their future."

News of the agreement helped Boeing shares jump 15% to $48.91 in trading on the New York Stock Exchange, amid the market's strong rally. But the company's labor issues aren't over. The deal with the machinists comes just as Boeing faces another big contract showdown with its 21,000-member engineering union, whose pact expires Dec. 1.

On the financial side, Boeing's salary offer remained largely the same as its previous offer, providing for an 11% wage increase over the first three years of the contract and an additional 4% for the newly added fourth year. The company also agreed to pay workers a lump sum equal to 10% of 2007 wages, or $5,000, whichever is greater, for the first year of the contract. During years two and three, the contract calls for lump sums of $1,500 that could also be rolled into a savings plan to bolster pension savings.

Boeing also agreed to raise the monthly pension multiplier by almost 16% to $81 for each year of service during the first three years of the contract, with a bump to $83 for the final year of the contract. It also raised the minimum hourly wage in each job category by $2.28 an hour.

For the agreement to take effect, at least 51% of the members must vote to accept it. The Union said workers would return to the factories the day after the agreement is ratified.

Like the Machinists, the engineers' union, SPEEA, has had an increasingly strained relationship with Boeing, particularly over the company's efforts to farm out increasingly large quantities of the design and fabrication of new airplanes to suppliers and contractors.

SPEEA officials have been particularly critical of the company's handling of the Dreamliner program, which is suffering from almost two years of delays as the result of design and manufacturing snafus on the part of suppliers. "Our people are extremely frustrated right now because they feel like the company doesn't value their knowledge and experience," said SPEEA Executive Director Ray Goforth.

Associated Press

Boeing officials said they won key victories in **the deal with the machinists union**, including an agreement by the union to extend the contract by a year to four years.

Boeing officials have not yet said what effect the strike will have on the Dreamliner program, but people familiar with the situation say the company will have difficulty meeting its goal of delivering the first airplanes in 2009. Boeing had hoped to fly the first 787 before the end of the year, but work on that aircraft was interrupted by the strike. After that, Boeing must still assemble several other planes and then take them through almost a year of around-the-clock flight testing.

During Boeing's earnings conference call last week, Chief Financial Officer James Bell said the company would update all of its delivery schedules after the strike. But he said it was safe to assume that most deliveries would be delayed by at least one day for every day the workers were on strike.

Profit at BP, Occidental soars with oil prices

BY BEN CASSELMAN AND JAMES HERRON

Oil-and-gas giant **BP** PLC posted an 83% rise in third-quarter profit Tuesday, due mostly to higher energy prices, and, when many smaller rivals are scrambling for cash, said it has more than $6 billion in the bank.

That could position U.K.-based BP to take advantage of falling energy prices by snapping up assets on the cheap.

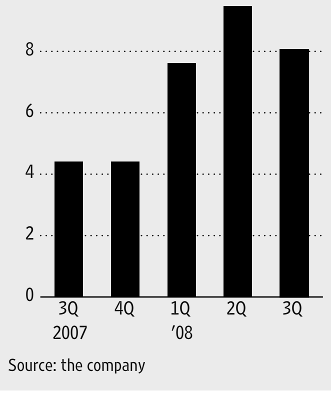
"The current turmoil may in fact create opportunities for us, and we will look at those very closely," BP Chief Executive Tony Hayward said.

Other cash-rich companies are similarly poised to benefit. **Occidental Petroleum** Corp., which also reported strong earnings Tuesday, said it has $1.45 billion in cash and expects to make deals early next year.

BP and Occidental have already been buyers this year. BP paid $3.6 billion to U.S. natural-gas producer Chesapeake Energy Corp. for assets in two separate transactions in the last three months. Occidental, based in Los Angeles, in September paid $1.25 billion for assets in Texas and Colorado. Many small producers borrowed heavily, spent aggressively when energy prices were rising, and now are looking to sell assets to raise cash.

Bouncing back

BP's net profit, in billions



Source: the company

But in a conference call with investors, Occidental President and Chief Financial Officer Steve Chazen said further deals won't happen until sellers drop their prices. "Right now the sellers are looking at six-months-ago prices, and the buyers are looking at a lot lower than that," Mr. Chazen said.

BP said third-quarter net profit came to $8.05 billion, up from $4.41 billion a year earlier.

Revenue rose 44% to $104.83 billion from $72.84 billion.

Production rose slightly, to 3.7 million barrels a day, after having been flat in the second quarter. But BP realized an average oil price of $111.47 a barrel, compared with $71.12 in the third quarter last year.

Prices have since fallen back under $65 a barrel. But Mr. Hayward said BP hasn't been hit by falling prices as hard as some of its competitors. The company hasn't committed as much money as its rivals to high-cost methods of producing oil, such as mining tar sands, he said.

BP also stands to benefit from improvements in its refining business. Refiners have been hurt this year by high oil prices and slumping demand, but profit margins have been improving recently.

"There's no denying the upstream was good and downstream is bouncing back," said Jason Kenney, an analyst at Dutch bank ING.

Occidental reported earnings of $2.27 billion, up from $1.32 billion a year earlier. Oil-and-gas production rose 3.2% to 588,000 barrels a day.

Selina Williams contributed to this article.

CORPORATE NEWS

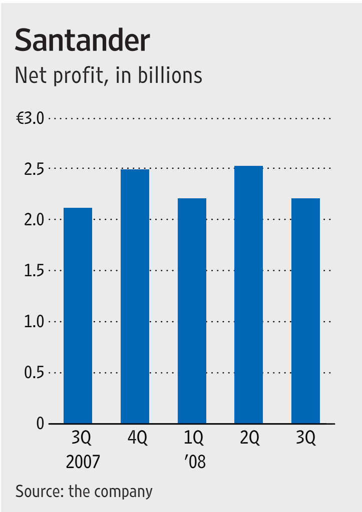
Santander ekes out growth amid crunch

Bank says it doesn't need to recapitalize; net profit rose 4.4%

BY CHRISTOPHER BJORK

MADRID — Spain's **Banco Santander** SA Tuesday reported a 4.4% rise in third-quarter net profit, boosted by higher lending profitability and by its recent takeover of Brazil's Banco Real.

Although the bank survived the early stages of the credit crunch relatively unscathed, its stock has fallen more than 25% in the past week on worries about its vast Latin



American franchise, where financial turmoil has led to plummeting commodities prices, sharply weakening currencies, and a brutal selloff in equity markets.

Analysts said the bank's results could give the company's share price some support in coming days. "We remain reasonably comfortable about Santander's ability to weather a more challenging economic outlook," said J.P. Morgan analyst Ignacio Cerezo. "That said (...) a global recession does not look like a particularly favorable scenario for the bank to outperform."

Spain's largest bank by assets said third-quarter net profit rose to €2.21 billion ($2.77 billion) from €2.11 billion a year earlier. Operating results were lifted by a 12% rise in net interest income, to €4.44 billion. Third quarter revenue was up 7% to €7.45 billion, while costs grew 1.5% to €3.13 billion.

"Despite turbulence, market difficulties and the crisis in the banking system, Santander's business model remains consistent, recurrent and with few surprises, producing strong results both in good times and bad," Chief Executive Alfredo Saenz said.

Santander has in the past three months acquired two troubled U.K. banks — Alliance & Leicester and Bradford & Bingley — and one struggling U.S. lender — Sovereign Bancorp Inc. Santander said its nonperforming loans rose to 1.63% of total loans in September from 1.3% in June. As a result, the bank boosted loan-loss provisioning to €1.54 billion in the third quarter from €898 million a year earlier.

Mr. Saenz said Tuesday the bank would focus on integrating those assets and wasn't planning further acquisitions. He also said Santander's capital ratios were sufficient and didn't need to be boosted with a recapitalization similar to the ones several of its peers have undergone recently. Santander's core Tier 1 ratio—a key measure of a bank's balance-sheet strength —stood at 6.31% at the end of September.

Later this week, Santander will lay out plans for the integration of Banco Real, which Santander acquired from Dutch bank ABN Amro. The unit has contributed €451 million to net profit so far this year, Santander said.

At Santander's core continental European division — which includes the bank's Spanish and Portuguese retail banking network and its consumer finance unit— profit inched up 0.4% in the first nine months to €3.53 billion. U.K. unit Abbey reported a 4% increase in net profit, to €943 million. Measured in pounds, Abbey's profits rose 20%. Profits at Santander's Latin American franchise rose 6% to €2.17 billion.

Fortis statements spur public probe from Belgians

A WSJ NEWS ROUNDUP

Belgian public prosecutors launched a formal investigation Tuesday into whether current or former executives at Belgian-Dutch bank **Fortis** NV misled financial markets when the bank reassured shareholders that it remained on a solid financial footing.

The investigation of unnamed people could concern current and former top executives of Fortis, the Brussels prosecutor's office said.

The investigation follows complaints from a former employee and public concern over the matter, said Josef Colpin, a spokesman for the prosecutor's office. The probe is likely to take several months.

A Fortis spokeswoman said the company hadn't been informed of the investigation.

Shareholder groups have complained that former Chairman Maurice Lippens and ex-Chief Executive Jean-Paul Votron repeatedly assured markets that the bank's balance sheet was strong and that there would be no change to the dividend policy. The bank scrapped its interim dividend and sought new capital at the end of June.

FOCUS ON AUTOMOBILES

GMAC seeks bank charter

A GM-Chrysler deal may hinge on access to Fed guarantees

BY DAMIAN PALETTA AND JOHN D. STOLL

GMAC LLC, the big lender co-owned by **General Motors** Corp. and investor group **Cerberus Capital Management** LP, is seeking to become a bank holding company under the auspices of the U.S. Federal Reserve Board, according to people familiar with the talks.

The move, a key element in the merger talks between GM and **Chrysler** LLC, is aimed at shoring up GMAC's shaky financial footing. It would allow the home-and-auto lender to qualify for billions of dollars in government aid and gain access to lower-cost funding.

Cerberus owns 80.1% of Chrysler and 51% of GMAC, and is discussing the transfer of most of its Chrysler holdings to GM in return for a bigger stake in GMAC.

GMAC's move is the latest example of the extraordinary measures companies are employing to access new bailout programs aimed at quelling the financial-market crisis. The government intervention, in the form of loan guarantees and tax dollars, has forced some companies to take unprecedented steps to ensure their survival.

Cerberus could merge GMAC and Chrysler Financial, Chrysler's auto-lending arm, into one entity controlled by the bank holding company, people familiar with the plan said. That company would be well suited to offer consumers an arsenal of financial services, ranging from auto loans to credit cards to interest-bearing bank accounts.

Becoming a bank holding company is critical because it could allow GMAC to receive equity injections from the U.S. Treasury's capital-purchase program and have its debt temporarily guaranteed by a new **Federal Deposit Insurance** Corp. program. GMAC's funding costs—currently unfavorable because of battered credit ratings—could decline dramatically if it could access the Federal Reserve's discount window.

Lower funding costs, equity injections and debt guarantees would provide a lift for GMAC, which has been incurring billions in losses because of its heavy exposure to the mortgage and auto-lending industries. However, GMAC's pursuit of the designation would require approval from multiple government agencies and it is unclear whether it will prevail, several people familiar with the matter said.

When Cerberus bought 51% of the lending company in 2006 from GM, the financial-services firm was considered a lending powerhouse, netting billions of dollars in profit on mortgage originations, insurance products and car loans. However, the collapse of the subprime-mortgage market, coupled with the softening of demand in the U.S. auto industry, has threatened to sink GMAC.

Cerberus is jockeying to get GMAC access to bailout programs.

GMAC's restructuring would be part of a complex but coordinated effort to stabilize GMAC, GM, Chrysler and Chrysler Financial. The White House and at least four government agencies are looking at different ways to help the U.S. auto manufacturing industry.

"I think what we're trying to do right now is use the tools that Congress gave us to try to help companies where we can," White House spokeswoman Dana Perino said.

Many financial-services companies avoid registering as bank holding companies because of the increased scrutiny from the Fed and bank capital-holding requirements. But since the financial crisis hit, a handful of firms have approached the central bank about registering as bank holding companies because it allows them to qualify for multiple government financing programs. **Goldman Sachs** Group and **Morgan Stanley** recently took the once-unthinkable step of becoming bank holding companies.

"You want to be a regulated entity now, because it provides confidence to the market that you've got the Fed providing oversight and you have the ability to qualify for a broader range of programs," said Gil Schwartz, a former Fed attorney who is now a partner at **Schwartz & Ballen** LLP in Washington, D.C.

The mechanics of any restructuring for GMAC are complicated, in part because GM owns 49% of the company and different Cerberus entities own the rest. GM would need to transfer at least half of its ownership in GMAC to Cerberus so that the auto maker no longer owned more than 24.9% of the voting shares. That way GM won't have a controlling interest in the firm under federal law.

If the Fed classified GMAC as a bank holding company, it would have more access to a Treasury program that is expected to purchase as much as $250 billion in preferred shares in financial institutions. Treasury spokeswoman Jennifer Zuccarelli said that this facility, called the capital-purchase program, "is only open to federally regulated banks and savings institutions."

If GMAC became a bank holding company, it also could qualify to have some of its debt guaranteed by the FDIC. Officials could try to structure such a deal before a Nov. 12 deadline for banks to notify the government if they want to be part of the program. Still, the government will consider any application after that date on a case-by-case basis.

GMAC owns an industrial bank chartered in Utah that doesn't have the full powers of a commercial bank. The industrial bank, which had $32 billion of assets and $17 billion of deposits as of June 30, could be converted into a commercial bank or a national bank. To control the new bank holding company, Cerberus might have to create several bank holding companies within its own structure.

—Jon Hilsenrath contributed to this article.

Associated Press

Weeds grow along an **empty car lot** at a Chevrolet dealership in Clarks Summit, Pa., that closed in August.

More U.S. car dealers close amid credit crunch

BY KATE LINEBAUGH

With credit drying up and new-vehicle sales slumping to a 25-year low, car dealerships from New Jersey to California are going out of business at an accelerating pace, threatening greater economic pain for communities around the U.S.

The National Automobile Dealers Association estimates 700 new-car dealerships will close this year, up from 430 last year, and take with them an estimated 37,100 jobs around the country. That is a heavy blow to a key piece of the U.S. economy. The country's 20,700 dealerships accounted for $693 billion in sales last year, or 18% of all retail sales, according to NADA.

The rapid disappearance of dealers could also complicate the challenges facing **General Motors** Corp., **Chrysler** LLC and **Ford Motor** Co. After years of market-share losses, each has been left with more dealers than they need, and have been pushing dealers to consolidate. But a sudden loss of some of the bigger players could make it harder for the Big Three to maintain sales. GM suffered a setback recently when **Bill Heard Enterprises** Inc., one of the largest sellers of Chevrolet-brand vehicles, filed for bankruptcy-court protection and closed its chain of 14 stores.

"The most serious concern for dealerships at the moment is liquidity," said Paul Melville, a partner at consulting firm **Grant Thornton** LLP.

Joseph Pfeffer, owner of **Bigelow Motors**, a Chrysler and Jeep dealer in Belleville, N.J., closed shop Oct. 4 after his bank decided to exit automotive financing. He had been in business since 1942. "I always survived," said Mr. Pfeffer, "but nobody ever cut off my line of credit before."

Mr. Pfeffer said he approached three banks about providing financing but none was interested. In September, he sold only seven vehicles, compared with 40 the previous month. When he closed, all 26 employees were terminated.

Similar scenes have been playing out around the country. According to NADA, 590 new-car dealerships this year closed through September.

The markets most vulnerable to dealer closings are California, which has the most dealers of any state, followed by Texas, Pennsylvania and New York, according to NADA.

GMAC LLC, which provides financing for most of the nation's General Motors dealers, recently notified dealers that it was revising terms of inventory credit and interest rates on revolving credit lines. Chrysler Financial took similar steps. Both raised dealership costs.

Honda sees tough times as profit tumbles 41%

BY YOSHIO TAKAHASHI

TOKYO—**Honda Motor** Co. posted a 41% drop in its fiscal second-quarter net profit and issued a profit warning for the full year, reflecting the tough times that lie ahead for Japan's second-biggest car maker.

Honda, the maker of Civic and Accord sedans, posted a net profit of 123.32 billion yen ($1.32 billion) in the three months ended Sept. 30, down from 208.48 billion yen a year earlier.

The auto maker's cost-cutting steps and solid sales in emerging markets were offset in the latest quarter by the yen's strength, declining sales of large vehicles in the U.S and higher material costs.

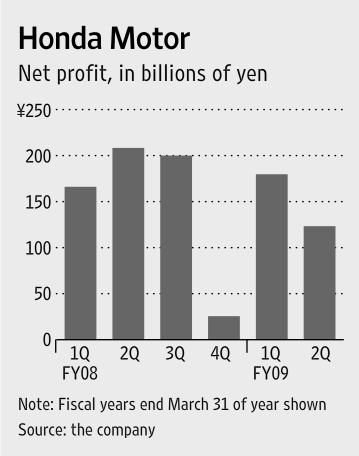
The steep profit decline underscores the increasing problems in the auto industry, as financial upheavals damp auto demand in major markets such as the U.S. and have started slowing growth even in booming markets such as China.

Carlos Ghosn, the head of Honda's rival **Nissan Motor** Co., warned Tuesday that tough business conditions in the auto industry could continue until as late as 2010.

Honda's slack results follow profit warnings issued by European car makers **Daimler** AG and **Renault** SA last week and bode ill for other Japanese car makers that will release their results this month and next month.

The auto maker's sales during the latest quarter fell 4.9% to 2.827 trillion yen from 2.971 trillion yen, while its operating profit sagged 48% to 148.85 billion yen from 286.34 billion yen.

Honda's global auto sales fell 0.2% to 935,000 vehicles during the period, with North America posting a drop of 9.9% and Europe down 13%.



For the full year ending March, the auto maker cut its net profit outlook to 485 billion yen from 490 billion yen and lowered its full-year operating profit outlook to 550 billion yen from 630 billion yen.

Honda revised downward these forecasts as it trimmed its global vehicle sales projections for the full year and said now expects the yen to get stronger in the second half. Revenue is now pegged at 11.6 trillion yen, lower than the 12.14 trillion yen in revenue it previously expected.

VW shares jump for second day as short-seller squeeze continues

A WSJ NEWS ROUNDUP

Shares of Volkswagen AG continued their climb Tuesday on the heels of a 150% surge Monday, as investors continued to show enthusiasm for Porsche's plans to buy three-quarters of VW's stock.

VW shares settled at €621.33 ($779.29), up 20% in Frankfurt trading Tuesday following a volatile session; at one point VW shares touched €1,005, making the automaker for a short time the world's largest company by market capitalization, ahead of U.S. oil giant **Exxon Mobil** Corp.

Volkswagen shares have been volatile over the past two months, leading to speculation that short sellers were desperate to cover positions. But covering activity took on renewed speed after **Porsche Automobil Holding** SE announced over the weekend that it increased its equity stake in VW to 42.6% from about 35%, and more crucially, that it had options to buy another 31.5% of VW.

The scramble for Volkswagen shares is particularly acute because its free float—the shares available on the open market—is estimated to be just over 5%, since Porsche holds VW shares either directly or indirectly that amount to 74%, and the Lower State of Saxony holds another 20%.

Porsche hasn't disclosed the strike price of the options but said that it will lock in gains between whatever the market price of VW when it exercises the option and the strike price.

Porsche said over the weekend that it was acting, in part, because it was "clear that there are by far more short positions in the market than expected."

A spokesman for Porsche rejected allegations of share price manipulation. He said this would be a confusion of cause and effect, adding that investors betting on Volkswagen's share price are responsible for the stock's extreme volatility.

CORPORATE NEWS

Biotech firms hit hard by financial crunch

Running out of cash, some cancel drugs, cut staff or merge

BY JEANNE WHALEN AND RON WINSLOW

The financial crunch is shaking the foundation of the global biotech industry, threatening to slow the development of new medicines and cut high-tech jobs in the U.S. and Europe.

Many small biotech firms are expected to file for bankruptcy, cancel drug trials, lay off workers or sell out to large companies over the coming year.

The biotech industry, largely made up of hundreds of private and public companies with just a handful of drugs in development each, has produced some of the most successful new medicines for cancer, HIV and other diseases in recent years. In the long term, a hobbled biotech industry would be bad news for big pharmaceutical companies, which increasingly rely on biotech start-ups to invent products the giants can acquire and market.

"The whole way of doing business is gone, at least temporarily. Companies that don't have a lot of cash or assets to generate cash" are in jeopardy, said George A. Scangos, chief executive of **Exelixis** Inc., a South San Francisco, Calif., biotech company.

Earlier this week, Mr. Scangos warned analysts on a conference call, "We're in an economic environment unlike anything I've seen before. ... While it's true we have an amazing pipeline of promising compounds, it's also true we don't have the resources, either financial or human, to develop them."

In the U.S., 38% of 370 small biotech companies are operating with less than a year's worth of cash, and nearly 100 publicly traded biotech companies have less than six months' cash, according to the Biotechnology Industry Organization, or BIO, in Washington, D.C.

The largest biotech companies, such as **Amgen** Inc., **Genentech** Inc., and **Gilead Sciences** Inc., have seen their stock prices fall but have robust revenue streams that should help them weather the downturn. The financial-market crunch is mostly hitting small biotech firms, public and private, with low revenue and little cash in the bank.

GlaxoSmithKline PLC said this week it may step up its acquisition of smaller drug companies now that their share prices are dropping, and **Novartis** AG said it is watching the situation carefully.

Venture capitalists are scaling back their investments in biotech companies, while opportunities for public offerings and bank loans have dried up. To obtain funding, companies are increasingly selling a drug's potential future revenue streams to investment funds. It is an expensive way to raise cash, and not one many companies would use if they had a choice, analysts say.

"We're very dependent on functioning capital markets to finance research and development," said Jim Greenwood, BIO's president and chief executive officer. "When those markets seize up there is less capital for investors to put at risk."

Oramed Pharmaceuticals Inc., based in Jerusalem needs $25 million to carry out human trials of an oral form of insulin. Instead of trying to sell stock in a public offering, it is asking large drug companies and other investors in Russia, South Africa, South Korea and India for cash in exchange for some of the drug's eventual revenues in those markets should the drug be approved for sale.

Among companies facing funding problems, **Atherogenics** Inc. of Alpharetta, Ga., filed earlier this month for chapter 11 bankruptcy protection after defaulting on debt payments due in September. The company was poised to launch a trial of a drug for diabetes before the money ran out. The company hopes to sell the medicine to another drug maker that will try to bring it to market. In September, **Cytokinetics** Inc. of South San Francisco said it was slashing its work force by 29% and jettisoning its cancer research to focus on a drug for heart failure.

In the U.K., **Ardana** PLC and **Phoqus Pharmaceuticals** PLC both went into insolvency administration this summer after running out of cash. **Lonza Group** AG, a Swiss company that makes chemical ingredients for the drug industry, said this week it will probably miss its full-year earnings targets because small start-ups are placing fewer orders.

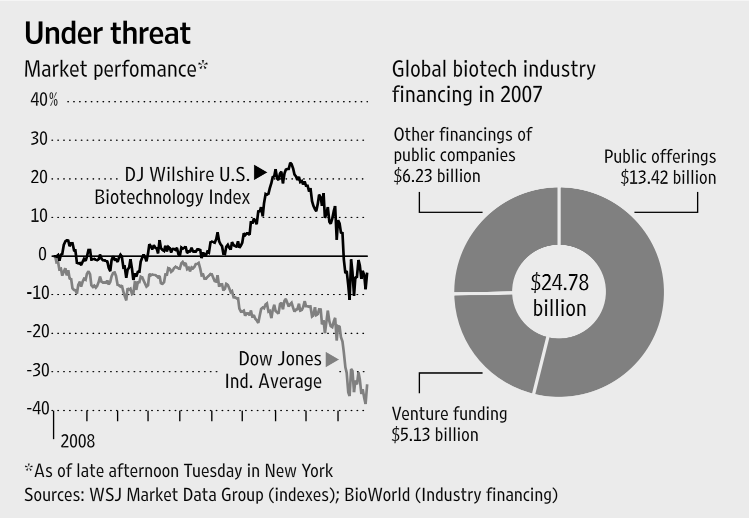
"A number of companies are going to find it very difficult to survive," said Aisling Burnand, chief executive of the BioIndustry Association in the U.K.

Arena Pharmaceuticals Inc. of San Diego has enough cash on hand—about $160 million to $175 million—to finish studies and file an application with the U.S. Food and Drug Administration on its weight-loss drug lorcaserin. But it will need more money to bring the pill, if successful, to market. "If the markets don't cooperate, we could be left with a problem," said Chief executive Jack Lief.

The Wellcome Trust, a charitable group in London that funds medical research, has seen the number of biotech companies approaching it for funding double over the last 12 months, said Richard Seabrook, head of business development and technology transfer.

Usually, the charity likes to deploy its £65 million ($101.5 million) annual budget to fund early-stage projects, before a drug goes into human studies. But it is receiving more applications from companies that need funding for human studies, funding they would normally get from equity markets or partnerships with big pharma, Dr. Seabrook said.

Another source of funds is a company with cash but lacking a promising drug. **Transcept Pharmaceuticals** Inc. of Point Richmond, Calif., faced difficulty getting its insomnia drug to market. In September it said it would merge with **Novacea** Inc., a publicly traded South San Francisco company whose lead drug failed, leaving it with nearly $100 million in the bank.



*As of late afternoon Tuesday in New York
Sources: WSJ Market Data Group (indexes); BioWorld (Industry financing)

SAP reports 5% drop in profit, scales back plans amid slowdown

BY LEILA ABBOUD AND ARCHIBALD PREUSCHAT

Business-software maker **SAP** AG reported a lower third-quarter profit and scaled back its plans for the rest of the year, saying the financial crisis is causing some customers to cut spending on software.

Net income fell 5% to €388 million ($486.6 million) from €408 million in the year-earlier quarter, Germany-based SAP said. The latest result was weighed down by an €87 million revenue write-down and charges on its January acquisition of a French company, Business Objects.

SAP and its competitors sell software to companies of all sizes to help them manage tasks such as inventory and payroll.

Quarterly revenue at SAP rose 14% to €2.76 billion from a year earlier. Revenue from software and software-related services increased 15% to €1.99 billion. "We are not in crisis mode," said Co-Chief Executive Leo Apotheker in an interview. "But we recognize that revenues will continue to be volatile, so we're taking precautionary measures to cut costs."

SAP said it would reduce costs by €200 million in the fourth quarter. A memo to staff earlier in the month declared a hiring freeze, urged them to travel in coach class when on business trips and canceled all external training courses. For now, no job cuts are planned, the company said.

In a bid to entice companies to keep buying software in tough times, SAP has retooled its product offerings. It created several software packages to help companies better manage their cash flow and liquidity, redeploy workers in changing business conditions and reduce procurement costs. "We put together these tools for our customers once we saw that the crisis was here to stay," Mr. Apotheker said.

SAP declined to provide specific revenue guidance for next quarter, given continuing volatility in the market. "Only a fool would try to predict what is going to happen," Mr. Apotheker said.

CORPORATE NEWS

Growth outlook is slashed for U.S. drug sales

Gain of 1%-2% seen; emerging markets pick up some slack

By Jeanne Whalen

Pharmaceutical sales in the U.S., the world's biggest market, will grow far less than originally forecast this year and are in for meager growth next year as economic turmoil and a lack of new products take their toll, according to a closely watched annual forecast.

U.S. drug sales this year are expected to rise just 1% to 2%, to as much as $297 billion, according to IMS Health Inc. The consulting firm forecasts U.S. sales to rise another 1% to 2% next year. IMS a year ago forecast 4% to 5% sales growth for this year.

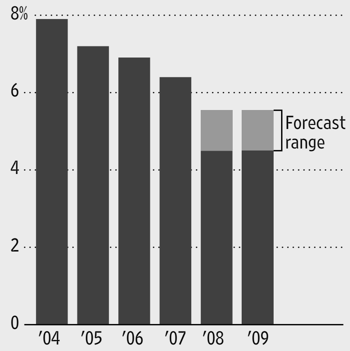
The dramatic slowdown is helping reshape the industry by propelling drug companies to devote more attention and resources to emerging markets. Early this decade, the U.S. accounted for 40% to 50% of the growth in global pharmaceutical sales each year. Next year, the U.S. will account for just 9%, IMS forecast in its report, which was scheduled for release Wednesday.

Emerging markets should help the global pharmaceutical market grow 4.5% to 5.5% to as much as $830 billion next year. But with the global economy in flux, IMS said an exact forecast is difficult. IMS includes branded and generic prescription drugs in its forecast.

With emerging markets increasingly picking up the slack, drug companies are scrambling to increase their sales forces in such countries. **GlaxoSmithKline** PLC, **Novartis** AG and **Sanofi-Aventis** SA have been among the most aggressive at introducing new products in emerging markets. "It's quite a dramatic shift," Murray Aitken, senior vice president of Healthcare Insight at IMS, said in an interview.

Flattening out

Sales growth for the global pharmaceutical market



Source: IMS Health

The top seven emerging markets will account for about 34% of global sales growth next year, up from 7% in 2000, IMS said. But sales could be hurt if economic turmoil continues in the top emerging markets, IMS said. Many consumers in countries such as Brazil, India and Russia pay out-of-pocket for drugs, so any damage to those economies could quickly affect drug sales.

In the U.S., economic uncertainty appears to be making Americans less likely to visit their doctors or to fill prescriptions, hurting drug sales, Mr. Aitken said. Also, drug companies aren't discovering as many new drugs these days, and the U.S. Food and Drug Administration is approving fewer medicines as it becomes more safety conscious.

Insurers also are hurting sales by not quickly covering new drugs and by pushing consumers and doctors toward low-cost generic drugs, Mr. Aitken said. Novartis's Tekturna for high blood pressure, for example, has been a weak starter because there are many good generic drugs for hypertension on the market.

That said, IMS also expects a slowdown in generic drug sales. Intense competition among generic-drug makers in the U.S. and Europe is driving down prices. IMS predicted the global generic market will grow by 5% to 7% next year, to more than $68 billion, down from double-digit growth in the past.

Aegis, Publicis warn ad spending is hard to predict

By Erica Herrero-Martinez And Ruth Bender

U.K.-based advertising and marketing company **Aegis Group** PLC and French ad company **Publicis Groupe** SA fueled concerns Tuesday when they warned that the economic slowdown was making it difficult to predict ad spending.

Even though organic revenue—which excludes acquisitions, disposals and currency movements—grew 7.3% in the first nine months of the year, "we have become more cautious about the outcome for the full year," Aegis said.

"We believe sterling weakness will offset fourth-quarter deterioration, and we are leaving our 2008 forecasts unchanged," analysts at investment bank Numis said in a report. "However, we are now factoring in a downturn" for 2009 and 2010, the report added.

Aegis said its financial position remains strong, and at Monday's close of business it had committed headroom of £112.1 million ($175.6 million) on its revolving-credit facility.

The cautious outlook put pressure on the company's stock, which closed down 10% at 57 pence, one of the biggest declines in London's FTSE 250 mid-cap index. Shares in Aegis have fallen more than 50% since the start of the year as the economic crisis has hit ad budgets.

In August, Aegis's media-buying division, Carat, cut its global-advertising-growth forecast for 2008 to just under 5% from 6%.

French rival Publicis, meanwhile, posted weaker third-quarter organic-revenue growth and said it expects a further slowdown in the fourth quarter. Organic revenue grew 3.9% in the third quarter, down from the 4.6% growth recorded a year earlier. Revenue fell slightly to €1.11 billion ($1.39 million) from €1.12 billion.

While it maintained its full-year targets for 2008, the Paris-based company said it expects a "marked slowdown" of the industry in 2009.

Next year "will be a tense year," warned Chief Executive Maurice Levy, adding that mature markets will pose the biggest challenge. He said that Publicis nevertheless still aims for organic-revenue growth above the 3.1% it logged last year.

CORPORATE NEWS

U.S. Steel income triples

End of boom means tougher times ahead; output curbs in place

BY ROBERT GUY MATTHEWS

U.S. Steel Corp., North America's largest steelmaker by output, reported its most profitable quarter ever, with strong demand and high prices more than tripling net income in what is likely to prove the last quarter of the commodity boom.

John Surma, the Pittsburgh steelmaker's chief executive officer, tamped down expectations for the fourth quarter, saying the volatile economy, softening automotive markets and a drop in demand and sales prices in both the U.S. and Europe would have "significant negative effects on our businesses."

Visibility into next year's performance is limited because of low order-backlogs and short production lead times, he warned. However, raw material costs are expected to decline, the company said.

Steel companies have been delivering record-breaking results this year but are now getting hit hard as nervous steel buyers limit their metal purchases because of the uncertain world economy.

This week Eurofer, Europe's steel trade and lobbying group, said the steel market is entering a period of instability and oversupply and "the downward trend is expected to accelerate during the first half of next year." Steel markets in North America, analysts say, aren't likely to recover until sometime in 2009 at the earliest.

The World Steel Association, spooked by the swift drop in steel prices and demand, declined to issue its annual world steel forecast last month, saying the financial crisis made it impossible to estimate demand with any accuracy. It expects to make a prediction sometime in early 2009.

U.S. Steel reported net income of $919 million, or $7.79 a share, for the quarter ended Sept. 30, compared with net income of $269 million, or $2.27 a share, in last year's third quarter.

Revenue soared 68% to $7.31 billion amid strong demand for the company's flat-rolled products and for tubular goods, which are used by the oil and gas industry. The average sales price for flat-rolled goods, the company's biggest product category, jumped 41% and shipments rose 25% compared with the same period a year earlier.

Wall Street analysts polled by Thomson Reuters had forecast earnings of $7.09 a share on revenue of $7.2 billion.

U.S. Steel said it saw demand for steel slow at the end of the third quarter and quickly started to reduce production at its mills in North American and Europe. The company said it will continue to operate at reduced levels, corresponding to customer order rates.

There is one bright spot for all steelmakers: lower energy and raw material costs. The costs of metallurgical coal, iron ore and fuel have started to decline as both demand and consumption in China has slowed.

At U.S. Steel, the impact won't be as great as it will be for other steelmakers. U.S. Steel is in the rare position of being able to supply most of its own iron ore and a significant amount of coke—a byproduct of coal—especially at its North American operations.

When prices for raw materials started skyrocketing last year, the company was not as affected by the increases as others. In turn, as prices for raw materials fall, its costs won't drop as dramatically.

U.S. warns Bayer over marketing

BY JARED A. FAVOLE

WASHINGTON—Pharmaceutical giant **Bayer** AG has received warnings from U.S. federal regulators for illegally marketing two unapproved over-the-counter medicines combining aspirin with dietary supplements.

Bayer's "Bayer Aspirin With Heart Advantage" and "Bayer Women's Low Dose Aspirin + Calcium" are drugs and require Food and Drug Administration approval before being marketed, the FDA said in two letters posted on its Web site Tuesday. The letters are dated Monday.

The two drugs combine Aspirin with over-the-counter dietary supplements. Bayer's Women's combines Aspirin with calcium. Bayer Aspirin with Heart Advantage combines Aspirin with phytosterols, which Bayer says help lower cholesterol.

Products that combine drugs and dietary supplements require FDA approval before they can be marketed, even if the drug, in this case Aspirin, is already approved.

Bayer has been marketing Aspirin Heart Advantage since earlier this year, while Bayer Women's Low Dose Aspirin + Calcium has been on the market since 2002. A company spokeswoman said Bayer was in the process of reviewing the FDA letters and will respond to the agency.

She said Bayer stands behind "both products and all the marketing claims that we make in their support."

Bayer has faced criticism from lawmakers over television ads for Bayer with Heart Advantage. Earlier this month, leaders of the U.S. House Energy and Commerce Committee said Bayer appeared to be ignoring FDA recommendations that companies refrain from marketing products that combine drugs and dietary supplements.

The FDA doesn't closely scrutinize dietary supplements for safety and effectiveness, and lawmakers are concerned that a product containing an FDA-approved drug and a supplement misleads people to believe the supplement has also been vetted.

The FDA says, however, it isn't aware of any significant adverse events associated with the drugs.

Lufthansa's net profit declines 65%

BY JAN HROMADKO

Deutsche Lufthansa AG said profit for the first nine months of the year fell 65% from a year earlier, when results were boosted by gains. The carrier also issued a profit warning for the full year.

The flagship German airline said Tuesday that because of higher fuel costs and an uncertain market environment, it now expects 2008 operating profit of about €1.1 billion ($1.38 billion). It previously said full-year operating profit would "follow up" on last year's €1.38 billion result.

The warning came three weeks after Lufthansa said the international financial crisis and the cooling economy have led to a noticeable decline in bookings.

Last week, Franco-Dutch carrier **Air France-KLM** SA, the world's biggest airline by revenue, already said that it will be very difficult for it to meet its operating income objective of €1 billion for this financial year. It said it had decided to limit its capacity increase for the winter 2008 and summer 2009 seasons to between 1% and 2%.

In a preliminary earnings report, Lufthansa said net profit for the first nine months fell to €551 million from €1.6 billion. The year-earlier results were boosted by gains of more than €500 million related to the sale of its stake in travel agency Thomas Cook. Revenue increased 14% to €18.6 billion.

Operating profit fell 9.3% to €984 million, hurt by "record levels in fuel costs, which could not be fully compensated in the increasingly difficult environment," Lufthansa said.

Sweden expands loan to Carnegie

A WSJ NEWS ROUNDUP

The Swedish central bank said it was ready to lend investment bank **Carnegie** AB as much as five billion kronor ($627 million) to ease a liquidity crunch.

The Riksbank said it was increasing the assistance from its previous offer of one billion kronor as a preventive measure "to make it easier for Carnegie to release its own liquidity should the need arise."

The Riksbank said it and Sweden's Financial Services Authority believed Carnegie was solvent, but the central bank didn't elaborate on why it had raised the loan from the amount announced Monday.

Riksbank deputy governor Lars Nyberg said: "Against the background of the prevailing unease in the financial system, the Riksbank has decided to grant Carnegie increased liquidity assistance in order to reduce the risk of serious disruptions to the financial system."

Carnegie said it had requested the expanded loan to enhance its "financial flexibility." It said it wouldn't necessarily use the entire credit facility.

GLOBAL BUSINESS BRIEFS

Luxottica SpA

Eyewear maker's net drops, but revenue increases 5.2%

Luxottica SpA of Italy reported a 7% drop in third-quarter net profit and issued a profit warning. The world's biggest eyewear maker by sales attributed most of the profit decline to charges after its acquisition of Oakley last year and unfavorable exchange rates. Net profit fell to €104.6 million ($131.2 million) from €112.4 million a year earlier, even though sales rose 5.2% to €1.21 billion from €1.15 billion. Luxottica owns the LensCrafters chain and the Ray-Ban brand and makes eyewear for fashion houses such as Prada and Chanel. The company also cut its 2008 earnings-per-share forecast to between 96 European cents and 98 European cents from a previous target of as much as €1.14.

Austrian Airlines AG

Austrian Airlines AG swung to a third-quarter net loss, hurt by higher jet-fuel prices, competition from low-cost carriers and losses on long-haul flights amid the financial crisis. The net loss was €16.4 million ($20.6 million), compared with a year-earlier net profit of €29.2 million. Sales rose 1.4% to €697.2 million from €687.6 million, helped by an upswing in passengers in the short- and medium-haul segment. The airline said it still expects a full-year net loss between €100 million and €125 million, excluding special items. Austria's government is trying to sell its roughly 42% stake in the national carrier. On Monday it extended the deadline for offers until Dec. 31, after at least one bidder, Deutsche Lufthansa AG, demanded that the government take on part of the airline's €900 million debt.

Continental AG

German auto-parts maker **Continental** AG said it will cut production at its Regensburg plant. As of November, the Regensburg plant will produce only four days instead of six every week, and production will close down completely between the Christmas holidays and year-end, a company spokeswoman said. Around 1,500 of the 6,500 staff members in Regensburg will be affected, and they will reduce their overtime during the production cuts, she said. The auto-parts maker is looking at similar measures for its approximately 30 other plants in Germany, she added. German auto maker **Daimler** AG is halting production for four weeks over the Christmas holidays at all of its 14 plants, while **BMW** AG plans to cut production by between 20,000 and 25,000 cars in 2008.

TeliaSonera AB

Telecommunications operator **TeliaSonera** AB of Sweden on Tuesday posted a 12% drop in third-quarter net profit, mainly because of higher costs and lower income from associated companies. Net profit fell to 4.77 billion Swedish kronor ($598.2 million) from 5.4 billion kronor a year earlier, while sales rose 4.1% to 25.82 billion kronor. The company said it still expects full-year net profit to be "somewhat higher" than last year, excluding gains of two billion kronor in 2007. The company also said its Spanish start-up, Yoigo, is likely to post a loss of more than one billion kronor in full-year earnings before interest, taxes, depreciation and amortization. TeliaSonera said it is considering its options for the business.

Mediobanca SpA

Milan-based **Mediobanca** SpA posted a 20% decline in first-quarter net profit, as higher net-interest income failed to offset lower trading-profit and fees. Net profit dropped to €310 million ($389 million) from €390 million a year earlier, as net fees and commissions fell 7% to €111 million. Net interest income meanwhile rose 7% to €223 million, thanks to a strong performance at the bank's consumer-credit operations. Chief Executive Alberto Nagel has been expanding the Mediobanca's operations outside Italy and boosted existing businesses such as consumer credit and wealth management in a move to modernize what was until then considered a traditional merchant bank.

Aviva PLC

U.K. insurer **Aviva** PLC posted a 12% rise in new-business sales for the first three quarters of 2008 thanks to better performances in Asia and the U.S., but said it sees a slowdown for the rest of the year. Sales of life insurance and pensions rose to £25.67 billion ($40.21 billion) from £22.94 billion a year earlier, even though investment sales were down 37% to £3.37 billion, partly because of a weaker U.K. commercial-property market. "These are unprecedented times," said Chief Executive Andrew Moss, noting that in spite of a drop in the company's share price, "people around the world are still saving and buying insurance." Since the start of the year, shares in Aviva have lost 64% of their value. Tuesday, the company's stock rose 5.6%.

TomTom NV

TomTom NV said third-quarter net profit dropped 41% because of plummeting prices for its navigation devices and warned that it won't reach its full-year sales target. Net profits fell to €58 million ($73 million) from €99 million a year earlier, as higher costs for research and development, administration and the acquisition of map maker Tele Atlas paired up with a drop in prices for TomTom's products. Sales came in at €429 million, flat from last year, but down 5% from the second quarter. Expecting a slowdown in consumer spending, the Dutch company lowered its full-year revenue outlook to between €1.75 billion and €1.85 billion, down from its previous target of up to €2.15 billion.

Panasonic Corp.

Panasonic Corp. of Japan said net profit for its fiscal second quarter slid 16% as the electronics company absorbed the impact of a stronger yen, higher raw-materials costs and anemic consumer spending. Panasonic hasn't cut its profit forecast for the fiscal year ending in March, but the company waved a caution flag. The outlook for the economy "is increasingly becoming uncertain," said Makoto Uenoyama, Panasonic's chief financial officer. Net profit for the three months ended in September fell to 55.5 billion yen ($593 million), from 65.8 billion yen a year earlier.

—Compiled from staff and wire service reports.

ECONOMY & POLITICS

TURKEY

In a policy shift, EBRD plans investment program

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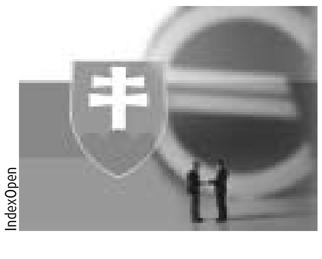
THE European Bank for Reconstruction and Development will start investing in Turkey, after its government shareholders approved the move. The bank, which was set up to help former Soviet nations become market economies, is likely to invest around €150 million in Turkey next year, and roughly €300 million in 2010, President Thomas Mirow said.

The bank plans to focus its lending on three areas in Turkey: providing loans to small cities to help improve their infrastructure; investing in small- and midsize companies based outside the big cities; and agribusiness, particularly improving the supply chain. *—By Paul Hannon*

SLOVAKIA

Central bank lowers rate before joining euro zone



IndexOpen

SLOVAKIA'S central bank cut its key interest rate by half a percentage point to bring its monetary policy in line with the European Central Bank ahead of Slovakia's adoption of the euro in January.

The central bank lowered its key two-week repurchase agreement rate to 3.75%. While the change was expected before year end, the timing of Tuesday's move surprised markets. Because of Slovakia's relatively high inflation rate compared with that of the euro zone, analysts had largely expected the central bank to wait until year end before adjusting its monetary policy. The board voted unanimously in favor of the change, the bank said. *—Sean Carney*

SYRIA

American school, center are ordered to close

Associated Press

THE SYRIAN government ordered an American school and a U.S. cultural center in Damascus closed in response to a deadly U.S. attack on a village near the Iraq border, the state-run news agency said.

U.S. officials said the raid killed a top operative of al Qaeda in Iraq who—according to intelligence—was about to conduct an attack in Iraq. Syria and the Iraqi government criticized the raid, and Syria denied Tuesday the attack had targeted an al Qaeda operative.

"What they [the U.S.] are saying is just unjustified. I deny it totally," Syrian Foreign Minister Walid al-Moallem said.

Overlooked measures hold clues on recovery

Economists watch South Korean index, weekly jobless claims

BY JUSTIN LAHART AND KELLY EVANS

AMID THE GLOBAL financial tumult, economists are struggling to gauge how deep the U.S. downturn will be. While standard measures such as gross domestic product and monthly payroll figures give snapshots of what has happened, those indicators say less about what will happen next. Economists are turning to other, less-obvious measures such as home-vacancy rates and foreign stock markets for clues to when the economy will turn the corner.

The current downturn is shaping up to be worse than the recessions of 1990-91 and 2001. Banks are cutting back on lending, consumers are spending less, companies are shedding jobs amid sinking profits, and the housing bust that triggered the slide persists. Here is a look at five areas that economists are watching and what indicators they are tracking.

Banks

The U.S. government's plan to inject $250 billion into financial institutions as well as its guarantees on loans between banks eased some of the stress ripping through credit markets.

In a sign that banks have become less wary of lending to one another, the London interbank offered rate, a benchmark interest rate for many dollar loans, has fallen over the past two weeks. It still is historically high relative to the U.S. Federal Reserve's target rate, however. Continued declines in Libor will be an important sign that the credit crunch is easing.

While lower interbank rates are an important precondition for a recovery in lending markets, they won't automatically lead to a lending revival. "It doesn't matter whether a bank will lend to a bank," said Northern Trust economist Paul Kasriel. "It's whether a bank will lend to Joe the plumber."

Associated Press

A nearly two-decade spurt of **consumer-spending growth** in the U.S. likely ended during the period from July to September, economists say.

Banks are cautious about lending, in part because they have been hurt badly in the housing downturn and financial-market turmoil, but also because lending is riskier during a downturn. In the Fed's July quarterly survey of senior loan officers, a large percentage of banks reported that they had tightened lending standards. One early sign the economy is on the road to recovery, according to Mr. Kasriel, will be when more banks are easing lending standards than tightening them.

Homes

The housing market will play a major role in any easing of lending standards. As long as home prices continue to fall, more homeowners will find themselves owing more on their mortgages than their homes are worth. That sets the stage for more mortgages going sour and continued caution among lenders. Through this year's second quarter, the S&P Case-Shiller national index of home prices was 18% below its 2006 peak.

The key to how much further home prices fall, Goldman economist Jan Hatzius said, is how fast the glut of empty homes is absorbed.

At the beginning of 2005, 1.8% of nonrental homes were empty and waiting to be sold. The Census Bureau reported Tuesday a 2008 third-quarter vacancy rate of 2.8%—even with the second quarter and just shy of the first quarter's 2.9%. With many homes on the market, sellers are lowering prices to attract buyers.

"If you see excess supply coming down, Economics 101 says that house prices will eventually stabilize," Mr. Hatzius said.

Consumers

Worries about the economy have skittish consumers tightening their purse strings. Consumer spending drives more than two-thirds of U.S. growth and hasn't declined on a quarterly basis since late 1991. That nearly two-decade spurt of spending growth likely ended during the July-through-September period, economists predict, dragging economic growth down with it.

A widely followed index of consumer expectations, part of the monthly consumer-sentiment report from Reuters and the University of Michigan, could offer clues to where spending is headed. After hitting its lowest level in nearly 30 years in June, the gauge had begun to improve as oil and gas prices fell from their record highs. But that improvement was wiped out this month as financial and economic conditions worsened.

One sign of improving attitudes among consumers will be their willingness to buy big-ticket items such as cars, furniture, appliances and electronics.

Jobs

Americans probably won't be inclined to make such commitments until they see improvement in the labor market. The payroll figures and unemployment rate from the monthly employment report are lagging indicators, showing changes in the jobs environment long after the fact.

Many economists more closely monitor the Labor Department's weekly report on initial unemployment insurance claims, which measures the number of people filing for new unemployment benefits. A rule of thumb says that when claims stay above 400,000, the economy is slipping into recession. That started happening in July. The latest weekly claims figure is 478,000.

Stocks

Companies play the major role in the jobs outlook: If they are worried about losses, they are more likely to pare the work force than hire. The stock market, for all its imperfections, is one of the best indicators of corporate health. Millions of investors are devoted to figuring out where profits are headed, and their opinions get reflected in prices.

But at a time when companies' health is highly dependent on the global economic environment, watching the Dow Jones Industrial Average may not give the best reading. Instead, Merrill Lynch strategist Richard Bernstein tracks the Korea Composite Stock Price index, better known as the Kospi. South Korean companies are export-oriented, which makes them highly sensitive to global profit growth. The Kospi topped out a year ago. Tuesday, it was 52% below that level.

Russia and China reach oil deal

BY ANDREW OSBORN

MOSCOW—A top Russian energy official said China will provide Russian oil firms with "considerable" loans in return for increased oil supplies as Moscow and Beijing agreed on details of a new pipeline linking the two countries.

Deputy Prime Minister Igor Sechin didn't say how much money China would be willing to lend, adding that the amount would depend on future oil supply contracts between Russian oil and pipeline companies OAO **Rosneft** and OAO **Transneft**, and Chinese energy giant **CNPC Sinopec.**

Such a loan would be timely for oil-major Rosneft, which finds itself heavily indebted at a time when the global credit markets are all but shut. It has already faced at least one margin call from creditors.

Any oil-for-credit deal would also help Russia further diversify its customer base for oil exports. Speaking during a visit to Moscow by Chinese Premier Wen Jiabao, Mr. Sechin told reporters that Russia was looking for new markets. "We need to seek a replacement for those markets which have stabilized or where consumption has fallen off," Russian news agency Interfax quoted him as saying.

Some media have reported that the loans could be as high as $25 billion. Spokesmen for both Rosneft and Transneft declined to comment on that figure.

Tuesday also saw a deal signed between Transneft and CNPC to build a pipeline spur that would link the two countries' trunk pipelines. A Transneft spokesman said the two sides had agreed on "who would build which section" but that construction and entry-into-service deadlines remained unsettled.

The pipeline is expected to be completed by the end of 2009 at the earliest. It will carry around 300,000 barrels of Siberian oil a day to China.