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THE WALL STREET JOURNAL.

Plowmen vie for gold on Austrian field of dreams

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ECB plots to clamp down on lending standards

LEADING THE NEWS | PAGE 3

Commerzbank to acquire German rival Dresdner

Allianz to keep stake following completion of $14.4 billion deal

Commerzbank AG has agreed to acquire Dresdner Bank AG in a €9.8 billion ($14.4 billion) deal that will combine Germany's No. 2 and No. 3 banks by assets, creating a bulkier domestic rival to compete with **Deutsche Bank** AG in Europe's largest economy.

Allianz SE, Dresdner's owner, said Sunday it will hold nearly a 30% stake in the combined entity at the end of a two-step, cash-and-stock transaction to be concluded next year. It marks the biggest transaction in Germany's highly fragmented banking sector in nearly a decade, and could trigger further consolidation in a country blanketed with more than 2,000 financial institutions, or about five times as many as in the U.K. or Spain.

By **Mike Esterl** *in Frankfurt and* **Dana Cimilluca** *in London*

The sale represents a major retreat from banking by German insurance giant Allianz, which bought Dresdner in 2001 for about €24 billion to form a multi-armed financial-services behemoth. Allianz's share

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U.S. Republican Convention kicks off

John McCain and Sarah Palin, at a hurricane command center in Mississippi Sunday

Reuters

What's News—

Business & Finance

Commerzbank agreed to acquire Dresdner Bank in a $14.4 billion deal that will combine Germany's No. 2 and No. 3 banks by assets, creating a bulkier rival to compete with Deutsche Bank. Page 1

■ **The U.K. Treasury chief** offered a gloomy economic assessment, saying the U.K. could be facing the worst economic conditions in 60 years. Page 9

■ **A surveyors group called on** the British government to let investors swap newer mortgage-backed securities. Page 9

■ **A study casts doubt** on the accuracy of a key index that banks use to gauge their subprime-related losses. Page 9

■ **British Airways is weighing** a partnership with Alitalia, as Italian investors are ready to make an offer for assets. Page 2

■ **The euro zone's inflation** rate eased in August while other data suggested economic growth would continue to slow. Page 2

■ **The Dow industrials shed** 1.5% to 11543.55, ending a strong month for stocks on a sour note, as Dell's weak profit battered tech issues. Page 20

■ **Lehman will try** to shore up its balance sheet by creating a structure to allow it to sell billions of dollars in real-estate loans. Page 19

■ **France's PPR** said first-half net profit more than doubled, helped by the integration of its stake in Germany's Puma. Page 5

■ **Microsoft's deal** to buy Greenfield for $486 million aims to help the software firm win users for Web services and compete with Google. Page 7

■ **Russian companies** may delay issuing bonds because the conflict in Georgia has made borrowing too costly. Page 19

■ **Carrefour posted** a 3.1% rise in first-half net profit on strong emerging-markets growth. Page 4

■ **Rosneft and Lukoil** benefited from record crude prices and higher refining volumes as they reported earnings. Page 5

Markets

MARKET	CLOSE	NET CHG	PCT CHG
DJIA	11543.55	-171.63	-1.47
Nasdaq	2367.52	-44.12	-1.83
DJ Stoxx 600	288.18	+0.97	+0.34
FTSE 100	5636.6	+35.4	+0.63
DAX	6422.30	+1.76	+0.03
CAC 40	4482.60	+21.11	+0.47
Euro	$1.4716	-0.0007	-0.05
Nymex crude	$115.46	-0.13	-0.11

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World-Wide

Hurricane Gustav bore down on the U.S. Gulf Coast, threatening to cut across offshore oil and natural-gas infrastructure and to flood at least parts of New Orleans, under evacuation orders just three years after Hurricane Katrina. Bush and Cheney canceled appearances at the Republican convention. Pages 1, 10, 32

■ **EU leaders aren't expected** to impose sanctions on Russia at a summit Monday over Moscow's invasion of Georgia. Page 1

■ **Russian police arrested** and shot to death the head of a Web site who had criticized authorities in the volatile Caucasus province of Ingushetia. Page 12

■ **Republican McCain chose** Alaska Gov. Sarah Palin as his vice-presidential running mate, a move aimed at attracting Hillary Clinton supporters. Pages 16, 17

■ **Obama's acceptance** of the Democratic presidential nomination came before 80,000 people, with a vow to cut taxes for working-class families. Page 11

■ **Palestinian President Abbas** rejected Israel's idea of an interim peace agreement at a summit Sunday with Olmert.

■ **Thailand's prime minister** said he won't resign as protests spread beyond Bangkok, amid disruption of rail and air services.

■ **Chinese rescuers rushed** to reach survivors of a 6.1-magnitude earthquake that struck Sichuan province Saturday, killing at least 27 people in the region.

■ **Authorities took** control of all private boats amid hijackings of rescue vessels and severe flooding affecting an estimated three million people in northern India.

■ **Pakistan said** it will halt a major operation against insurgents in the northwest because of the Muslim holy month of Ramadan.

■ **An Afghan commander told** a government panel that U.S. and Afghan troops were fired on first from the village where some officials say 90 civilians were killed.

■ **Bosnian Serb former leader** Karadzic refused to enter a plea before a war-crimes tribunal in The Hague, calling it an illegitimate arm of NATO. Page 12

■ **Over 100,000 people marched** across Mexico Saturday to demand government action against crime, killings and kidnappings.

EDITORIAL & OPINION

The other change ticket

With new running mate Sarah Palin, John McCain shows he's out to reform the GOP. Page 13

Gustav leading to evacuations on U.S. coast

Evacuations were in high gear Sunday as Hurricane Gustav bore down on the U.S. Gulf Coast, threatening to cut a devastating swathe across the Gulf of Mexico's oil and gas infrastructure and to flood at least parts of New Orleans just days after the third anniversary of Hurricane Katrina.

Gustav's untimely arrival also disrupted plans for the Republican National Convention, scheduled to begin Monday in Minnesota. President George W. Bush and Vice President Dick Cheney both canceled appearances scheduled for Monday because of the hurricane, as convention planners scrambled to cope with political and practical implications of the mammoth storm.

By **Leslie Eaton** *in New Orleans and* **Ben Casselman** *in Lake Charles, La.*

Republican candidate John McCain traveled to a hurricane command center in Jackson, Miss., Sunday morning, along with his new running mate, Alaska Gov. Sarah Palin, to get briefed on storm preparations. Meanwhile, his top

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U.S. ties with Georgian ally prove volatile amid dispute

Russia's claim that the U.S. orchestrated the conflict in Georgia has sharpened the dispute between the two superpowers. But despite close links between the U.S. and Georgia, their relationship in recent years has been marked more by frustration than coordination.

By **Marc Champion** *in Tbilisi, Georgia, and* **Jay Solomon** *and* **Mary Jacoby** *in Washington*

According to interviews with current and former U.S. officials, as well as with Georgian officials in Tbilisi, the U.S. for years has found the relationship with Georgian President Mikheil Saakashvili difficult to manage.

From Mr. Saakashvili's ascent to power in the 2003 "rose revolution" to his assault last month on Tskhinvali, capital of separatist South Ossetia, his risky moves have often caught Washington unprepared and left it exposed diplomatically, U.S. officials say.

American frustrations have been matched by those in Tbilisi. At a crucial moment earlier this year, a lame-duck administration in Washington was unable to deliver European support to kick-start Georgia's membership in the North Atlantic Treaty Organization.

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LEADING THE NEWS

Alitalia's appeal grows

British Airways sees possible partnership; Italian offer is set

BY STACY MEICHTRY AND DANIEL MICHAELS

British Airways PLC is considering a partnership with **Alitalia** SpA, people familiar with the matter said, becoming the latest European carrier to jockey for a piece of the insolvent Italian airline as it embarks on a major restructuring.

A group of Italian investors will launch on Monday a formal offer for Alitalia's potentially profitable assets—including its newer planes and airports slots—with the aim of then merging them with smaller Italian carrier **Air One** SpA.

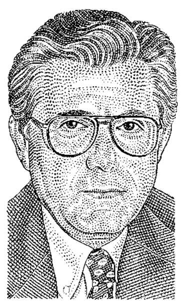
The complex deal, which was brokered by the Italian government and would create a new Italian airline, is the latest in a string of rescue plans over the past two years for Alitalia. According to the airline itself, it has been losing between €1 million and €2 million a day ($1.5 million and $2.9 million).

As the rescue effort has taken shape, Italian bank **Intesa Sanpaolo** SpA—an architect of the plan—has lured other European carriers to take part.

Franco-Dutch airline **Air France-KLM** SA has already said it might take a minority stake in the new Italian carrier. Germany's **Deutsche Lufthansa** AG, which already has an alliance with Air One, is also considering a partnership with the new airline, according to a person familiar with the matter.

Over the past week, British Airways has also joined the fray, people familiar with the matter said. The idea would be for BA to forge an industrial partnership, though it is unclear whether the U.K. airline would eventually also take a stake, these people said. A spokesman for British Airways declined to comment.

The interest of three rivals in Alitalia, long considered the albatross of European air travel, reflects the gathering pace of consolidation in Europe's fragmented airline industry. BA, Air-France and Lufthansa are all trying to snap up second-tier airlines that are seeking investors, even considering potential partnerships with carriers they have shunned in the past.


Roberto Colaninno

Lufthansa said Thursday it is in talks to buy a 45% stake in the parent of Brussels Airlines for €65 million. BA and Spain's **Iberia Lineas Aereas de España** SA announced plans last month to merge.

Lufthansa has said it is also interested in buying a minority stake in **Austrian Airlines** AG that the Austrian government is selling. Air France-KLM and BA have also expressed interest in the sale, according to people familiar with the talks. The airlines haven't commented officially.

Alitalia's sudden appeal is also the result of a new shield erected around the airline by the Italian government. Last week Prime Minister Silvio Berlusconi issued a decree revising Italy's bankruptcy-protection law to protect the group of Italian investors from Alitalia's creditors. The new law allows the investors—led by Roberto Colaninno, head of motorcycle maker **Piaggio** SpA—to swiftly buy Alitalia's potentially profitable parts, while the airline's aging fleet and most of its €1.2 billion in debt are liquidated.

The European Union is currently reviewing Alitalia's rescue plan to determine whether Italy, by changing its bankruptcy law, is providing the carrier with illegal state aid.

Mr. Colaninno, along with Intesa and Italy's Benetton family, has created a new company with €1 billion in capital, **Cia. Aerea Italiana**, that will purchase Alitalia's newer planes and slots at Rome and Milan airports from Alitalia and merge them with Air One.

"We are working under the umbrella of the new law," said Mr. Colaninno in an interview.

A crucial step in Mr. Colaninno's plans is forging an alliance with one of Europe's major airlines. Mr. Colaninno said the new Italian airline can't survive in Europe's competitive aviation market without a larger partner providing scale and logistical help. "Technically speaking it is very complicated to manage," Mr. Colaninno said, referring to all aspects of the airline business.

Mr. Colaninno also faces a battle in renegotiating the contracts of Alitalia's staff with Italy's restive unions, which have used strikes to cripple past efforts to sell the airline.

The rescue plan calls for between 5,000 and 7,000 job cuts to Alitalia and Air One's combined staff. The staff of both airlines numbers about 20,000.

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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Euro-zone inflation falls; oil's drop eases concerns

BY PAUL HANNON

LONDON—The euro zone's annual rate of inflation fell to 3.8% in August from 4% in July, adding to signs that price pressures are easing in the 15-country bloc, even as data suggest economic growth will continue to slow.

The decline in the inflation rate was the first since March, although it remains above the European Central Bank's target of just below 2%. However, economists expect the inflation rate to fall further, with some forecasting that it will slip below 3% by the end of the year.

The decline in food and oil prices since June has had an immediate impact on inflation expectations, a key concern for the central bank.

According to a monthly survey carried out by the European Commission, the measure of inflation expectations in the euro zone fell to 22 from 30 in July. It was the second-largest monthly drop in the measure's 18-year history, and brought the survey down to its lowest level since July 2007 and below its long-term average.

The ECB's fear since rising oil and food prices first pushed the inflation rate above its target in September 2007 has been that consumers will expect prices to rise at the same rapid pace over the medium term. High inflation expectations could lead to high wage demands and set off a so-called second round of price increases as businesses cover increased wage bills.

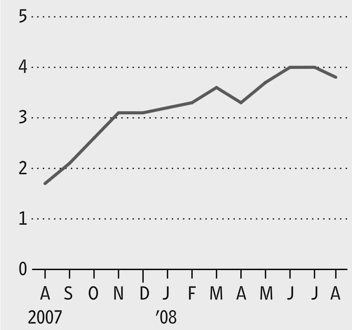
The fact that inflation expectations have responded so quickly to the fall in oil prices should lessen that fear but won't remove it.

"The latest round of survey data will not extinguish the ECB's concerns over pipeline inflation pressures and inflation expectations, but the good news is that the decline in oil prices is having a positive effect," said Ken Wattret, an economist at BNP Paribas.

The commission's survey also recorded a slight pickup in consumer confidence, although it remains low. However, the Economic Sentiment Index that measures both business and consumer confidence fell again, to 88.8 from 89.5, its lowest level since March 2003.

Inflation slows

Euro zone's consumer-price index, year-to-year percentage change



Source: Eurostat

"This is...consistent with [gross domestic product] growth momentum hovering just above zero," said Marco Valli, an economist at UniCredit in Milan.

The slight improvement in consumer confidence was due to the drop in inflation expectations and is unlikely to lead to a revival in flagging spending. Indeed, the commission's survey found that workers have become more fearful of losing their jobs and less willing to make major purchases. Eurostat, the European Union's statistics agency, said the unemployment rate remained at 7.3% for the fourth straight month in July, but most economists expect it to begin to rise soon.

To investors, the decline in the inflation rate and signs that the economy is weakening point to lower interest rates in the future. Immediately following the release of the inflation figures Friday, the euro weakened to $1.472 from $1.474. Late Friday in New York, the euro was trading at $1.4671.

In a concerted effort to subdue expectations of a rate cut, several ECB governing council members asserted that inflation may take off 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

ECB plots a lending-standard clampdown

Collateral on loans propping up banks appears to be dicey

By Carrick Mollenkamp
And Sara Schaefer Muñoz

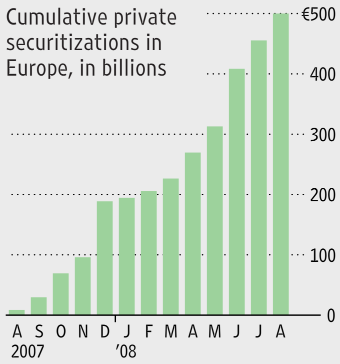
LONDON—The European Central Bank is considering tightening lending standards amid concerns it has become a dumping ground for troubled securities, a move that could squeeze some struggling banks.

As soon as Thursday, when its governing council meets, the ECB could announce plans to toughen rules on the collateral it will accept in exchange for billions of euros in loans that have kept much of the banking sector afloat.

Policy makers are worried that banks have been taking advantage of the ECB's lending facilities, in part by packaging risky mortgages into securities specifically designed to be parked as collateral with the central bank. There are also signs that lenders are setting up shop in the euro zone to obtain funding from the ECB, which offers banks easier lending terms than its U.K. counterpart.

Repackaged

Cumulative private securitizations in Europe, in billions



Source: Citigroup

Central banks are in a precarious position, because banks, now in the second year of a credit crunch, remain dependent on central-bank loans to finance portfolios of hard-to-sell securities. In providing banks with a longer-term home for the securities, central bankers could be aggravating the crisis by preventing the market from finding a proper price for the securities.

But pulling back support would put added strains on banks and increase borrowing costs at a difficult time for both the financial system and the broader economy.

Changes to the ECB's lending rules would likely bring them more in line with those of other central banks, though they aren't likely to take effect for a few months. The ECB, for example, accepts as collateral securities with credit ratings as low as single-A-minus, as opposed to the Bank of England, which accepts only triple-A assets. The Bank of England also requires borrowers to put up more excess collateral.

An ECB spokesman declined to comment. A few weeks ago, ECB President Jean-Claude Trichet said bank officials will "see what we have to do, if it proves necessary, to refine elements of our scheme."

In a conversation with bankers, at least one ECB official expressed concern that the central bank has become the only game in town for financing mortgage securities, according to a person familiar with the conversation. The bankers also learned the ECB had received complaints that its lending practices are creating an artificial price for the securities and could be stalling any market recovery, the person said.

Since the onset of the credit crunch last year, banks' demand for central-bank cash injections has surged. While overall ECB lending hasn't changed much, the central bank is lending more for longer periods: As of Aug. 1, it had some $300 billion in three-month loans to banks outstanding—an amount that was doubled in late 2007 as a result of turmoil in the credit markets.

The ECB has also extended some loans as long as six months. The ECB's relatively easy lending terms have encouraged foreign banks to set up shop in the euro area, specifically with the aim of tapping ECB funds. England's **Nationwide Building Society**, for example, recently announced plans to open a small deposit-taking operation in Ireland, in part to get access to the ECB funding, said spokesman Steve Cowdry.

Data released Friday by the Irish Central Bank suggest Nationwide isn't alone: Total lending to credit institutions at the end of July stood at €44.1 billion ($64.7 billion), up from €21.8 billion a year earlier, with most of it going to foreign-based banks with operations in Ireland, according to a central-bank spokeswoman.

At the same time, the nature of the collateral that banks put up for the loans has changed markedly. Faced with a dearth of demand in the public "securitization" markets that traditionally allowed them to package and sell loans to investors, banks have been putting loans and other assets into "private" securities that have little use other than as ECB collateral—a practice that effectively puts the central bank in the position of funding the banks' continuing operations.

While the practice doesn't violate any ECB rules, "it is very questionable whether such deals are consistent with the spirit" of the central bank's lending policies, says Ganesh Rajendra, head of European securitization research at Deutsche Bank AG in London. Various indicators suggest the private securities could contain a lot of problematic assets, particularly mortgages.

In one ominous sign, a large share of the securities are coming from banks in Spain and the U.K., which both face sharp economic downturns and deepening housing busts. Birgit Specht, an analyst at Citigroup Inc., estimates that from the time the credit crunch took hold in August 2007 though July 2008, Spanish and U.K. banks created a total of €91 billion and €152 billion in private securities, respectively.

Spanish banks have also increased their use of ECB lending programs: According to data from the Bank of Spain, net lending to credit institutions was €49 billion in July, nearly triple the level of a year earlier. The data on Spanish borrowing include foreign-based banks with operations in Spain.

—Joellen Perry contributed to this article.

CORPORATE NEWS

AIRLINES

EU looks into cooperation between BA, Iberia, AMR

Associated Press

THE EUROPEAN Commission launched an antitrust investigation into the planned cooperation between **British Airways** PLC, **AMR** Corp.'s American Airlines and **Iberia Líneas Aéreas de España.**

A spokesman for the European Union's executive branch said the commission opened the probe on its own accord and will concentrate on whether a deal would violate European cartel rules.

The three airlines plan to cooperate commercially on flights between the U.S., Mexico and Canada, as well as the EU, Switzerland and Norway, while continuing to operate as separate legal entities.

—Peppi Kiviniemi

VIDEOGAMES

Nintendo shares jump on stronger profit outlook


Nintendo

NINTENDO Co. raised its net-profit outlook, citing Wii and DS console sales and more favorable foreign-exchange rates.

The Kyoto-based game-machine maker said it now expects net profit to climb to 410 billion yen ($3.77 billion) for the year ending in March, 26% higher than the 325 billion yen it previously forecast, and nearly 60% higher than its net profit for the last fiscal year. Nintendo shares rose 8.4% on the news.

The guidance upgrade shows Nintendo is growing more confident it can pull further away from its rivals Sony Corp. and Microsoft Corp.

—Yuzo Yamaguchi and Hiroyuki Kachi

STEEL

ArcelorMittal and union reach four-year contract


Shutterstock

THE United Steelworkers and **ArcelorMittal**, the world's largest steel producer, agreed Saturday to a tentative four-year contract.

The union has been negotiating since April on a contract for more than 14,000 workers and tens of thousands of retirees. The current contract expires Monday, and rank-and-file workers had given union leaders the authority to launch a U.S. strike if negotiations failed.

While both sides declined to publicly discuss details, the agreement provides a lump-sum payment of $6,000 following ratification, plus a $1 hourly increase in the first year and 4% increases in each of the following three years.

—Associated Press

Carrefour profit rises on emerging markets

Weakness in France hurts performance for giant retailer

BY MIMOSA SPENCER
Paris

CARREFOUR SA, the world's second-largest retailer after Wal-Mart Stores Inc., posted a 3.1% rise in first-half net profit as strong growth in emerging markets helped the French company offset weakness at home.

Net profit for the first six months of the year rose to €751.8 million ($1.1 billion) from €729.1 million a year earlier. The company previously reported an 8% rise in first-half sales to €41.95 billion.

The retailer reiterated its full-year targets, reassuring investors who had been concerned it would announce a disappointing outlook or a management change. The company, which had lowered its outlook in June, said it is sticking to its current full-year forecast of 7% sales growth at constant exchange rates.

Carrefour shares closed up 7.2%, or €2.43, at €36.13, outperforming a 0.5% rise in the CAC-40 Paris index.

The earnings were "totally in line with our expectations," said Cedric Lecasble, analyst with Landsbanki Kepler, noting that "no spectacular announcements" such as a profit warning or management changes were made.

Carrefour has been dogged by recurring talk in the market of management changes, prompted in part by the influence of shareholders Colony Capital and Bernard Arnault, who hold three seats on its board.

Asked Friday whether the board supports Carrefour's current plans, Chief Executive José-Luis Duran said, "I wouldn't be here presenting the results" without the board's support.

The French retailer's solid results were a bright spot amid otherwise lackluster retail earnings in Europe. Supermarket operators Ahold NV of the Netherlands and Casino Guichard-Perrachon SA of France on Thursday posted sharp declines in net profit from a year earlier, when earnings were boosted by gains from asset sales.

Reuters

Carrefour repeated its full-year forecast after solid first-half earnings.

Looking ahead, Carrefour outlined plans to accelerate its Champion store conversions, boost promotions in its French hypermarkets and reduce operating costs. The company said it seeks to save €100 million in operating costs by year end to help offset the impact of new tax rules in France. Measures will include a hiring freeze at the company's headquarters, Mr. Duran said.

The retailer will redirect €200 million in capital to investments that it expects to generate high returns, such as investing in growth markets and increasing the proportion of its new store openings in countries like Brazil and China.

Carrefour said that by year end it expects to convert 150 Champion stores to the Carrefour format, up from its previous goal of 100 stores. The company hopes to gain market share through the program, which will entail streamlining information-technology systems and selling more Carrefour-brand products.

Carrefour's stock has fallen more than 30% since the beginning of the year, compared with a drop of about 20% in the Paris CAC-40 index. Investors have been spooked by the drop in sales from the company's largest stores in France as rising prices of goods and gasoline drove customers away.

How to make a name for drugs without using their names

BY ALICIA MUNDY

Pfizer Inc. has found a way to encourage the use of its antismoking drug Chantix without detailing serious potential side effects through a commercial that doesn't mention Chantix at all.

During NBC's coverage of the Beijing Olympics this month, Pfizer aired a commercial in which a middle-age woman tells the camera, "At 6:30 in the morning, I have a cigarette. And then another on my way to work." During the 60-second commercial, a voice discusses ways to break the habit and directs viewers to Mytimetoquit.com. Visitors to the site find a link to a Chantix site that contains information on the antismoking drug, including the negative side effects.

Such "unbranded product advertising" like the mytimetoquit.com spot is gaining popularity among drugmakers, which in recent months have come under renewed fire from lawmakers for the ways in which they promote drugs directly to consumers.

Under Food and Drug Administration rules, if an ad doesn't directly name the drug, it doesn't have to include the reading of possible side effects that can chew up expensive television time. An **Eli Lilly** & Co. ad for its osteoporosis drug Evista, for example, spent 25 of its 60 seconds listing risks such as blood clots and "dying from stroke."

The unbranded efforts include 15-second ads created by **Sanofi-Aventis** SA to promote a Web site called silenceyourrooster.com. Visitors to the site discover that it promotes the anti-insomnia pill Ambien.

The rooster Web site got 400,000 hits in the first seven days on the air last month.

Direct-to-consumer drug advertising dropped nearly 30% in the first quarter, experts say, but such TV ads surged temporarily during the Olympics. One night during the Games, NBC host Bob Costas noted that the 3 a.m. rerun of the prime-time broadcast was sponsored by the maker of Ambien. "No lie," he said. "There's irony there somewhere."

This unbranded approach has been used in the past to promote disease awareness and build markets for treatments for those disease.

Bob Ehrlich of DTC Perspectives, which monitors direct to consumer advertising by drug makers, says the Ambien and Chantix promotions may be clever, but "There's a risk they could rouse congressional ire over cute commercials that don't emphasize medicine."

Pfizer says it isn't pushing Chantix in its ads, or trying to circumvent FDA rules. "The goal of the My Time to Quit campaign is to encourage people to quit smoking," said company spokeswoman Sally Beatty.

"My Time to Quit is designed to encourage people who are thinking about quitting to speak to their healthcare provider about the benefits of quitting smoking and available treatment options," she said.

Chantix had sales last year of $883 million. But recently, it has been losing ground following reports linking the drug to suicides and suicidal behavior. That led to an FDA alert in February. A study this spring linked Chantix to drowsiness and more than 100 accidents. That led federal aviation regulators to ban it for use by pilots. Pfizer has said that it stands by the safety of Chantix.

The mytimetoquit.com commercial first aired in December 2006 a few months after the drug came to market. As Chantix' popularity boomed, Pfizer ran a different ad that mentioned the drug.

But in June, in the wake of the study on accidents and Chantix, Pfizer relaunched My Time to Quit.

"With unbranded ads, you don't have the 'fair balance' requirement," said Rich Gagnon of the ad agency DraftFCB, part of Interpublic Group of Companies Inc., in New York. "Imagine paying millions to run that ad campaign, and having to use up 30 seconds to list all the problems," said Mr. Gagnon, who has several pharmaceutical clients.

Ruth Day of Duke University, a frequent critic of direct to consumer ads, gave the commercial and website high marks for useful information. An expert in how medical ads work on consumers, Dr. Day said mytimetoquit.com is relatively easy and gets to lists of side effects quickly.

Pfizer had originally been skeptical of unbranded "help-seeking" and "disease-awareness ads." In late 2005, an executive said that such ads "do not drive patients to the doctor" as well as ads that offer a solution.

CORPORATE NEWS

Holding in Puma helps drive net for France's PPR

By Mimosa Spencer
And A.H. Mooradian

PARIS—French luxury-goods and retail company **PPR** SA said first-half net profit more than doubled, lifted by gains and the integration of its stake in German sportswear company **Puma** AG.

The company, home to high-end fashion brands Gucci, Bottega Veneta and Balenciaga, confirmed its full-year outlook and said it has a program under way to cut structural costs and improve efficiency to boost sales and profitability amid the recent deterioration of consumer demand.

Chief Executive François-Henri Pinault said in an interview that PPR is accelerating its plans to boost efficiency, even though the company doesn't expect a further decline in the retail environment and is confident of meeting full-year targets.

"It's true we don't see a pickup yet, but we don't see the situation worsening, either," Mr. Pinault said, adding that the company's mass-market retail activities in the U.S., which have suffered from a decrease in mall traffic, even saw a slight improvement in the first half.

Net profit for the first six months rose to €779.2 million ($1.14 billion) from €323.4 million a year earlier, though the results were bolstered by capital gains of €418 million, mostly related to the sale of YSL Beauté to French cosmetics company L'Oréal SA.

The integration of PPR's 68.5% stake in Puma and the United Retail unit in the first half was a significant boost. PPR said that if these two businesses had been included in the year-earlier period, recurring operating profit would have edged up just 1%. Instead, reported recurring operating profit was up 24% to €742 million.

First-half revenue rose 12% to €9.58 billion.

PPR shares climbed 4.3% to €79.72 in a moderately higher French market Friday.

Through its efficiency plan, Mr. Pinault said the company aims to lower the break-even point of its operations with measures such as improving logistics and supply-chain management, as well as reducing administrative costs by pooling resources of different activities. He declined to provide figures on the financial impact of these measures.

The efforts will concern all areas of business, with emphasis on catalog division Redcats and furniture retail chain Conforama.

Mr. Pinault said he expects benefits from the streamlining program in the second half. He said the program is also aimed at improving cash flow, which he called unsatisfactory. Chief Financial Officer Jean-François Palus said cash flow had been hurt in the first half by a range of factors, including seasonal and calendar-related effects, as well as longer payment lags by customers. PPR plans to aggressively cut inventories to address the problem, and Mr. Palus predicted that PPR's cash flow will return to normal by year's end.

PPR's share price has shed more than 30% since the beginning of the year, a steeper drop than that of the Paris CAC-40 index, which has declined more than 20% over the period. The stock has been hit by concerns that consumer spending will remain weak in the U.S. and Western Europe.

—Nathalie Boschat contributed to this article.

Areva's profit more than doubles

REpower stake sale, greater contributions from units boost net

By Adam Mitchell

PARIS—French nuclear group **Areva** SA said its first-half net profit more than doubled, helped by one-time gains and greater payouts from its stakes in other companies.

The state-controlled nuclear group, which is promoting its European pressurized-water reactor in the U.K. along with **Électricité de France** SA, said net profit rose to €760 million ($1.12 billion) from €295 million in the same period a year earlier.

Areva said net profit was helped by a €95 million increase in net financial income, including a gain from the sale of a stake in wind-turbine manufacturer **REpower Systems** AG.

The contribution to profit from Areva's stakes in other companies rose to €121 million from €34 million a year earlier, helped by strong income growth at mining and metals company **Eramet** SA.

"As usual, there are a lot of one-offs," said Alex Barnett, a Paris-based analyst at Jefferies. There are so many items, he said, that it is "hard to read anything in the numbers."

Operating income more than doubled to €539 million. Areva said it booked an additional provision on its reactor-building contract in Finland but didn't specify the size of the provision.

Last month, Areva reported first-half revenue rose 15% to €6.17 billion, as sales in its reactors and services division surged.

Areva's share price has fallen more than 15% in the past three months to close at €688.36 Friday as oil prices slipped, taking the edge off investors' enthusiasm for all things nuclear.

There has also been speculation that the French government might push for a tie-up between Areva and French heavy-engineering company **Alstom** SA, in which French conglomerate **Bouygues** SA holds a 30% stake.

Friday, Bouygues's chairman and chief executive, Martin Bouygues, said there has been no movement on this, and the issue doesn't seem to be a priority for the French government.

—David Pearson contributed to this report.

Tata stops work on new auto factory in India

By Eric Bellman

Tata Motors Ltd. stopped work on the site of its new factory, saying that continuing public protests against the plant threatened the company's workers.

The auto maker, based in Mumbai, India, is slated to start making the $2,500 Nano minicar, which has been called the world's least-expensive mass-produced car, in October at Singur, in India's eastern state of West Bengal. Tata, which already has invested more than $350 million in the project, said demonstrations have disrupted efforts to get the plant ready to begin production.

"Our employees and workers are not attending work today," said Debasis Ray, a spokesman for Tata, on Friday. "We are reviewing the situation."

Employees were asked to stay home on Saturday as well, and Sunday is a regular holiday. Mr. Ray said late Sunday that Tata had yet to decide whether it would restart work on Monday.

Tata Motors has become one of India's best-known companies. Earlier this year, it acquired the Jaguar and Land Rover luxury-car brands from **Ford Motor** Co. for $2.3 billion. Tata Motors produces trucks as well as passenger vehicles and sport-utility vehicles for Indian consumers.

Ratan Tata, chairman of the Tata Group conglomerate, on Aug. 22 threatened to relocate the Tata Motors factory because of violent demonstrations. Political opposition to the plant in West Bengal has continued for almost two years, both in support of local farmers who say they were forced off the land and to protest the use of agricultural land for industry.

Associated Press

Thousands of farmers protest outside a Tata factory in Singur, India, Sunday. They say they were forced off the land and they object to the use of agricultural land for industry.

The increasingly ugly battle between small farmers and big business shows that India still needs to learn how to reconcile rapid economic expansion with the needs of ordinary citizens, who often are displaced or disadvantaged by new industrial, mining or other projects from which they derive little or no direct benefit.

"We clearly don't yet have a foolproof, transparent, fair policy that allows for a relatively peaceful transfer of land," said Subir Gokarn, chief economist at Standard & Poor's Asia Pacific in New Delhi. "Wherever large tracts of land are being proposed for transfer, this issue flares up."

India needs to build its industries to create jobs for its population of 1.1 billion, and industrial operations need large tracts of land. But acquiring land is difficult in a crowded country with many competing political groups and powerful networks of social activists.

Across India, conflicts have erupted over proposed special economic zones, mines and chemical plants. In the impoverished eastern state of Orissa last year, steel company **Posco** of South Korea dealt with violent protests and even kidnapping of its employees over its plans to take over thousands of acres for a plant.

London-listed metals-and-mining company **Vedanta Resources**PLC has had to fight for the right to mine bauxite in Orissa. Local tribal groups and environmental activists tried to block its expansion in the courts, arguing the mining project will do serious harm to the flora and fauna of the area, which is sacred to some tribes.

The resistance is a problem not just for corporations, but also for India's government, which has embraced a strategy of industrial growth to create jobs. "The Tatas pulling out of West Bengal would be unfortunate for India. Nano is seen as a world car and has drawn international acclaim. Immediate political dialogue to find a solution toward keeping the project in West Bengal is imperative," said Sunil Bharti Mittal, chairman of telecommunications company **Bharti Airtel** Ltd., in a statement. "If the House of Tatas, known for its values and care for the society, can face such resistance, the much-needed fresh wave of industrialization in the country could suffer."

Although the Indian economy's growth rate has averaged more than 8.5% a year over the past five years, annual expansion in the agricultural sector is usually closer to 2%. Two-thirds of India's population still lives in rural areas, with most rural dwellers earning less than $2 a day. Officials would like to see more of them in industrial jobs, but the transition is often painful.

—Tariq Engineer and Santanu Choudhury contributed to this article.

Oil prices, added refining boost Lukoil, Rosneft

By Andrew Langley

Russia's biggest oil producers, OAO **Rosneft** and OAO **Lukoil**, benefited from record crude prices and higher refining volumes as they reported second-quarter earnings.

Lukoil, Russia's second-biggest oil producer after state-run Rosneft, said net profit jumped 64% to $4.13 billion from $2.52 billion a year earlier, while revenue rose 59% to $32.09 billion.

The company, which is 20%-owned by Houston-based **ConocoPhillips**, said soaring oil prices more than offset a 3.1% drop in production to 1.9 million barrels a day and higher government export duties.

Total throughput of higher-margin refined products, such as gasoline, also rose 7.1%. This increase helped push up earnings before interest, taxes, depreciation and amortization, or Ebitda, 59% to $6.24 billion from $3.92 billion despite a $800 million hit from asset-impairments and hedging costs.

However, analysts at investment bank Troika Dialog in Moscow warned that growing export duties, which the government recalculates every two months, and falling oil prices could herald a tighter third quarter.

The unprecedented increase in oil-price rises relative to lagging export tariffs accounted for 20% to 25% of Russian oil companies' Ebitda, they estimated in a research note. "With the recent drop in oil prices, the sector now faces a squeeze almost equal to that profitability spike, making the quarter's financials almost a backward-looking indicator," they said.

After a peak in mid-May, when the authorities agreed to cut oil-sector taxes, Lukoil shares have lost around 40% of their value, in line with a drop in oil prices and a wider exodus from Russian equities.

Tax cuts due to come into force next year have made investing in domestic output more attractive and could save Lukoil as much as $27 billion by 2017, said Deputy Chief Executive Leonid Fedun.

"We now have a strong appetite for production projects within Russia," he said, adding that developments further afield had previously been more lucrative.

State-controlled Rosneft saw its net profit drop 44% to $4.31 billion from $7.66 billion a year earlier. However, stripping out the $7.9 billion pretax gain booked last year from the bankruptcy proceedings of OAO Yukos, net profit more than doubled from $1.7 billion in the second quarter of 2007.

Revenue soared to $21.13 billion from $10.79 billion, as an 8.2% surge in crude output to 2.1 million barrels a day drove the benefits from oil prices higher.

CORPORATE NEWS

Vodacom Group expands in Africa

Telecom to buy bulk of Gateway's assets in $575 million deal

By Robb M. Stewart

JOHANNESBURG—Vodacom Group Ltd., South Africa's largest mobile-phone operator by subscribers, Friday said it agreed to buy most of **Gateway Telecommunications** SA in a deal valued at about $575 million, bolstering its presence in fast-expanding African markets.

Vodacom, jointly owned by **Telkom** SA of South Africa and **Vodafone Group** PLC of the U.K., said it will buy most of the closely held satellite and terrestrial-network-services provider, excluding its broadcasting arm.

"This sets us up for growth going forward and access to a much bigger market," Vodacom Chief Executive Officer-designate Pieter Uys said. The deal would boost Vodacom's presence in Nigeria, Africa's biggest mobile-phone market, and other countries.

Mr. Uys, who is to succeed CEO Alan Knott-Craig in October, said that as part of the deal, Vodacom will also take on about $100 million in Gateway's debt and will pay $25 million to buy back Gateway's high-yield bond. He added that the deal will be funded through loans, which would be raised locally and internationally.

Gateway, which provides interconnection services via satellite and ground networks to telecommunications companies, has offices in 17 countries and last year recorded sales of $257 million.

The acquisition will further Vodacom's ambition to offer converged communications services, diversifying away from being a pure mobile-phone service company, Mr. Uys said.

Mr. Uys said Gateway, which will be operated at arm's length and retain its brand, will act as a springboard for Vodacom's growth ambitions. "Once in a country, once we have a foot in the door, we can obviously look around," he said.

Africa, where penetration rates for mobile-phone use are among the lowest in the world, has increasingly attracted companies looking for customer growth. South Africa's **MTN Group** Ltd., the continent's biggest operator overall, has led the charge on the continent in recent years and this year attracted merger interest from two Indian operators.

Vodacom offers mobile-phone services in South Africa, the Democratic Republic of Congo, Lesotho, Mozambique and Tanzania. However, it has been held back from aggressively chasing MTN across Africa and the Middle East by a pact between its owners, which limited expansion.

South African fixed-line operator Telkom, however, has said it remains in discussions to shed its stake in Vodacom, selling a portion to partner Vodafone and handing the rest to its shareholders.

Mr. Uys said Vodacom's owners have agreed to the purchase of Gateway's businesses, which remains subject to regulatory and central-bank approval.

Besides aiming to cement its control of Vodacom by buying part of Telkom's stake, Vodafone is seeking to expand elsewhere in Africa. In July it bought a 70% stake in Ghana Telecommunications in a deal valued at $900 million.

U.S. firm disputes liability for bassinet recall

By Melanie Trottman

In a conflict that threatens to leave tens of thousands of potentially hazardous bassinets on the market or in consumers' homes, a company that acquired the assets of the Simplicity bassinet brand says it isn't liable for recalling products that U.S. federal regulators have linked to two deaths.

Seven big retailers agreed as of Friday afternoon to stop selling and take back the Simplicity bassinets that the U.S. Consumer Product Safety Commission says could be hazardous to babies. The retailers are **Wal-Mart Stores** Inc., **Toys "R" Us** Inc., **Kmart** Corp., **Big Lots** Inc., **Target** Corp., **J.C. Penney** Co. and **Amazon.com** Inc.

Toys "R" Us was selling as many as eight of the 66 models affected by the warning but halted sales Thursday morning, a spokeswoman said Friday. Target was selling affected models only on its Web site, a spokesman said.

The big retailers also agreed to bear the expense of providing a refund or store credit to consumers who return a product to the store where it was bought, said the CPSC. While the agency estimates these retailers account for a majority of the products already sold or still on shelves, it needs many more to cooperate. "We believe many more will come on board," said CPSC spokeswoman Julie Vallese.

The dispute over who ultimately should bear the costs of a recall affecting nearly 900,000 convertible bassinets is continuing between the agency and the company, **SFCA** Inc., which bought the assets of Simplicity Inc. in April after Simplicity went out of business. The products have been on the market for about seven years.

Wednesday, the CPSC warned parents and caregivers to stop using certain Simplicity brand bassinets following two infant deaths from strangulation. But the agency stopped short of a product recall, citing SFCA's lack of cooperation and claims that it isn't responsible for products previously made by Simplicity.

Seven retailers agreed to stop selling and take back Simplicity bassinets deemed potentially hazardous to babies. They also will provide a product refund or store credit.

The CPSC is now seeking access to all of SFCA's financial records, said Ms. Vallese. That should help it determine the terms of the asset purchase and what SFCA is liable for, she added.

SFCA is standing by its assertion that it has no legal liability for any products distributed previously by Simplicity.

Rick Locker, counsel to SFCA, said he disagrees. "There's no difference between general U.S. civil and liability law and federal law. The issue is: Is SFCA a successor to Simplicity Inc.? And they're clearly not," he said.

Pamela Gilbert, a lawyer with Washington's Cuneo Gilbert & LaDuca LLP and former CPSC executive director, said that "just because they're excluded from legal liability doesn't mean they're shielded from responsibility under federal regulatory laws." She added that looking at their corporate structure should help clarify the situation.

The circumstances of these events are unusual. Typically, the CPSC works with the product manufacturer or importer to get them to voluntarily recall a hazardous product. Forced product recalls are rare because they can require lengthy legal action, the CPSC says, but the agency has been criticized many times for waiting too long. The first of the two infant deaths linked to Simplicity bassinets occurred a year ago. The second happened last week.

The CPSC's Ms. Vallese said the agency began investigating the product after learning about the first death, but "taking action was complicated" because of difficulty getting data. The agency had "new authority" when the second death occurred that made action easier, she said. That authority comes from recently passed legislation to toughen product-safety regulation.

Ms. Vallese said the CPSC doesn't see the need to take legal action against SFCA because retailers have started to cooperate.

The CPSC said the 66 dangerous models of convertible "close-sleeper/bedside sleeper" bassinets are hazardous in part because of metal bars spaced too far apart to prevent infants from slipping through and becoming strangled. The metal bars are covered by an adjustable fabric flap that is attached by Velcro, and the fabric is folded down when the bassinet is converted into a bedside co-sleeping position. If the Velcro isn't properly resecured when the flap is adjusted, it can expose the dangerous gap.

The bassinets that SFCA has been making post-acquisition aren't cited as dangerous. They have an added panel of fabric for protection, Mr. Locker said.

Convertible bassinets are popular in part because they are considered a safe alternative to "co-sleeping," when infants sleeping beside an adult in a bed can become crushed or entrapped.

Donald Mays, senior director of product safety at the Consumers Union, said there is no mandatory standard for bassinets, and the voluntary guidelines don't cover convertible bassinets. His group lobbied one of the main standards-setting organizations to develop such a standard, and it is writing one now, he said.

Cara Smith, deputy chief of staff for the Illinois state attorney general, said her office is likewise seeking access to SFCA's records to get a scope of the products affected in Illinois. She is concerned that the nature of this recall will limit costly efforts to inform consumers.

Pernod to control U.S. sales of Absolut

By David Kesmodel

Fortune Brands Inc. agreed to end a joint venture to distribute Absolut vodka in the U.S. in exchange for a $230 million payment from **Pernod Ricard** SA, which recently bought Absolut's parent company. Fortune Brands also agreed to buy Cruzan rum from Pernod Ricard for $100 million.

The accord allows Pernod Ricard to take full control of the distribution of Absolut in a key market, in the wake of the French company's $8.3 billion purchase of Sweden's Vin & Sprit AB last month. And it gives Fortune Brands a premium rum brand to help the maker of Jim Beam bourbon and Sauza tequila bolster its spirits roster.

Fortune Brands and Vin & Sprit's joint distribution venture in the U.S. will end Oct. 1. The agreement had been scheduled to run through February 2012.

Fortune Brands, of Deerfield, Ill., had been among the bidders for Absolut's parent earlier this year, but Pernod Ricard, which makes Chivas Regal scotch and Beefeater gin, was willing to pay more.

Cruzan, which was part of Vin & Sprit, is the fifth-largest rum brand in the U.S., where sales rose at a double-digit clip last year. Fortune Brands already distributes Cruzan, produced in the U.S. Virgin Islands, through the joint venture with Vin & Sprit.

"Rum is one of the most attractive spirits categories, and the addition of Cruzan fills a portfolio gap in premium rum with the category's fastest growing brand in the U.S.," Bruce Carbonari, chief executive of Fortune Brands, said in a statement.

By ending the distribution joint-venture, Fortune Brands will create a sales force focused only on its brands, which will "simplify our route to market in the U.S.," Mr. Carbonari said.

Fortune Brands, a conglomerate that owns Moen faucets, Titleist golf balls and other products, expects to book a net again of $180 million, after taxes, in its third-quarter results, reflecting the cash payment from Pernod Ricard, among other gains and charges.

Allco Finance posts year loss on write-downs

By Rebecca Thurlow

SYDNEY—**Allco Finance Group** Ltd. said Friday that it had a full-year net loss of 1.73 billion Australian dollars (US$1.49 billion) on asset write-downs, and announced plans to further trim its operations as it battles to pay down debt.

The asset manager is one of a handful of Australian companies with complicated structures that have been hurt by repercussions of the U.S. subprime-mortgage crisis.

Allco has been selling assets and winding back some operations to pay down debt after a loss of investor confidence resulted in a share-price slide and triggered talks with the company's bankers.

Allco's loss for the year ended June 30 compared with a profit of A$211.7 million a year earlier. Revenue fell to A$939 million from A$1 billion a year earlier. It won't pay a final dividend.

"The reconstruction of the group is progressing; however the business remains in a fragile position, and the continued market weakness is making the task difficult," said Chief Executive David Clarke in a statement.

The company warned in May that it might record a loss of more than A$1.5 billion for the 2008 financial year because of write-downs, impairment charges, and the potential sale of assets at less than carrying values.

Like larger asset-management peer Babcock & Brown Ltd., Allco was forced into talks with its bankers this year after a big fall in its market capitalization allowed its bankers to review its debt.

Last month, the firm signed a new debt agreement with its banks for a A$702 million senior debt facility. It is required to reduce its senior debt to A$400 million by June 30, 2009, under terms of the new facility, but the facility isn't tied to market capitalization, leverage or other financial ratios.

Allco booked noncash impairment charges of A$1.43 billion during the year, on tangible assets in all its business segments as well as goodwill and management rights.

The firm puts its net asset value at A$545 million, down 77% from A$2.41 billion a year earlier.

Allco is focusing its business on what it sees as its core capabilities—aviation, shipping and private equity. The firm plans to cease its principal investment activities, becoming a fiduciary manager of investments and only using its balance sheet to co-invest in its managed funds.

Mr. Clarke said the firm will cut jobs up to 50% by the end of June in a bid to slash costs and plans to sell more than A$300 million of assets during the same period. Allco, which had a staff of 620 in January, now employs about 370 people. Mr. Clarke expects the firm will have around 150 employees in the long term.

Allco plans to exit its rail-equipment leasing and real-estate businesses, as well as the previously announced areas of financial assets and infrastructure, he said.

Mr. Clarke said Allco's acquisition of Rubicon Holdings Ltd. in December was a mistake. In February, the trusts that Rubicon manages said that the collapse of the commercial real-estate collateralized debt obligation market had left them unable to refinance their warehouse debt facilities.

CORPORATE NEWS

Microsoft retools for fight against Google

Greenfield purchase aims to attract users for Internet services

By Aaron O. Patrick
And Robert A. Guth

Microsoft Corp.'s agreement to buy **Greenfield Online** Inc. for $486 million is a small step by the software maker toward meeting its main challenge in competing with **Google** Inc.: attracting more people to Microsoft's online services.

The companies Friday announced the deal for Microsoft to buy Greenfield, a Connecticut company that operates a service in Europe called Ciao that lets people compare prices of merchandise and write reviews of products and merchants. Microsoft said it will sell a second Greenfield business, which runs online consumer surveys, to an unidentified buyer.

The acquisition reflects Microsoft's strategy to retool its online business following a failed attempt this year to buy **Yahoo** Inc. Hoping to better compete with Google, Microsoft has spent years building the technical underpinnings of Internet search and online advertising services. But the software maker has failed to attract a large mass of consumers. Google, meanwhile, has used its Internet search service to build a big audience that attracts lots of advertisers.

Greenfield has access to both. The Ciao service has signed up 2,200 merchants and gets 26.5 million visitors a month, Microsoft said. Ciao operates in the U.K., Germany, France, Italy, Spain, the Netherlands and Sweden.

Microsoft executives said they plan to incorporate Ciao into Microsoft's Web sites, including its Live Search service. Under the plan, a person looking at Microsoft's MSN Travel site who searches for "camping gear" would be directed to Ciao, which would display a list of camping products ranked by price, a Microsoft spokesman said.


Ciao.com

Greenfield's Ciao Web site lets consumers compare products and merchants.

Greenfield is paid a commission from the merchants when people use the site to buy products. In the quarter ended June 30, Greenfield reported net income of $2.1 million on sales of $36 million.

Eventually, Microsoft plans to pass on part of the commissions it gets from merchants to consumers, figuring the rebates will increase the number of people using the site and revenue overall. The plan is in line with a "cash-back" service Microsoft rolled out in May that pays consumers when they use Microsoft's Internet search to purchase products.

"We think there is too much money for the middle man" from each transaction, said John Mangelaars, vice president of consumer and online for Microsoft in Europe, the Middle East and Africa.

Microsoft will pay $17.50 a share in cash for Greenfield, which is traded on the Nasdaq Stock Market. The deal and Microsoft's sale of the survey business are both expected to close in the fourth quarter, Microsoft said.

The sale scuttles a previous agreement Greenfield reached with **Quadrangle Group** LLC, a private-equity firm. Quadrangle in June agreed to buy Greenfield for $15.50 a share, or about $426 million at the time. But Greenfield in early August said that it was considering a new proposal from a "strategic buyer" of $17.50 a share.

On Aug. 26, Greenfield said that its board of directors determined the new offer was superior to that from Quadrangle. It said it had informed Quadrangle that it intended to terminate the earlier agreement. Quadrangle is entitled to a $5 million breakup fee.

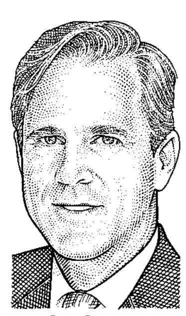
The company in August lowered its revenue forecast for the calendar year, to a range of between $143 million and $150 million, due to a gloomier outlook for its survey business. It previously had set the high end of the range at $153 million.

Delphi exit from bankruptcy at risk as U.S. car sales skid

By Jeffrey McCracken
And John D. Stoll

Giant U.S. auto-parts maker **Delphi** Corp. is sliding deeper into trouble, raising doubts about its ability to survive as a stand-alone company.

It is laboring to put together a plan to emerge from federal bankruptcy-court protection. But odds are increasing that the U.S.'s largest auto-parts maker instead will be liquidated, with some U.S. plants being taken over by its former parent company, **General Motors** Corp., according to people involved in the bankruptcy process. Even if that doesn't happen, GM's financial obligation could grow by billions of dollars, these people say.


Charles E.F. Millard

Several financial hurdles loom in coming months: Delphi's bankruptcy financing expires at year end, and there are indications that its current lenders may balk at renewing it. Its pension plan will need a large cash infusion or GM to take over some of it. The government's pension-insurance agency has expressed concern about the growing possibility of liquidation.

Delphi's woes underscore just how abysmal this year has been for the U.S. auto industry. As gasoline prices rose and consumer confidence fell, auto makers have watched sales of cars and light trucks drop about 20% so far this year, to levels not seen since the recession of the early 1990s. A slew of parts makers have sought bankruptcy protection, including two that recently filed for a second time. The mess has imperiled the jobs and retirement benefits of hundreds of thousands of workers and former workers.

Michigan-based Delphi blames its difficulties on circumstances beyond its control, such as the credit crunch and collapsing light-truck sales at General Motors. It says it doesn't intend to liquidate.

"We've not thrown that word around," says Delphi spokesman Lindsey Williams. "If that were our intent, we would not be working as feverishly as we are. We've been going down a lot of avenues to emerge from bankruptcy."

Delphi, formerly GM's in-house parts maker, produces auto electronics, safety equipment and steering systems, among other things. It filed for Chapter 11 bankruptcy protection in October 2005, citing the rising cost of labor and raw materials and the difficulty of passing along the increases to auto makers. Many of Delphi's U.S. competitors found themselves facing similar problems, and a number of them also wound up in bankruptcy court.

A liquidation of Delphi, which employs 159,000 and had $22 billion in revenue last year, would be costly to many, especially to GM. The struggling auto maker would have to decide whether to continue running money-losing Delphi plants to keep parts flowing to GM's assembly lines. Thus far, GM has had trouble finding other suppliers to build the parts at similar prices.

When GM spun off the company in 1999, it retained an obligation to fund pension and health-care benefits for former GM workers who moved to Delphi. Delphi's problems have already cost GM about $11 billion in cash and write-downs.

Delphi's pension plan, which covers about 85,000, had obligations of $14.05 billion at year end, but was underfunded by $3.3 billion, according to Securities and Exchange Commission filings.

In an Aug. 15 letter to GM and Delphi, the government's pension-insurance agency, the Pension Benefit Guaranty Corp., pressed GM to take over $1.5 billion of Delphi pension obligations next month. If Delphi were to be liquidated and its pension fund terminated, the federal agency would be on the hook for unfunded portions. The agency says it has an $8 billion claim in court should the pension plan fail, and has liens against all of Delphi's foreign assets.

"In our view, if Delphi has a proper business plan in place, it has the necessary cash flow to be a viable business," said Charles E.F. Millard, the agency's director, in an interview. "But the clock is ticking and time is getting short. If this becomes a liquidation, then our $8 billion claim would swamp any claim the creditors have. We are trying to get everyone's attention." He said time is running out "if there's going to be an emergence from bankruptcy."

Exit trouble

The falling value of Delphi's bonds and stock suggests investors have lost confidence in its ability to emerge from bankruptcy.

Sources: CapIQ (bonds); FactSet Research Systems (stock)

Ray Young, the chief financial officer of General Motors, said this month that the auto maker was having a "constructive dialogue" with Delphi, but "they have to understand there is only so much that we can do. They're going to have to do their own form of self help here."

A liquidation could also prove costly to hedge fund **Appaloosa Management** LP, which was Delphi's largest shareholder, with 9.3% of its shares, according to Appaloosa's most recent filing, in April. Delphi had struck a deal with Appaloosa's founder, veteran "vulture" investor David Tepper, and several other investors that was supposed to bring Delphi out of bankruptcy last year. But that deal fell apart this spring. Appaloosa didn't return calls seeking comment.

"It is not at all clear a stand-alone reorganization is feasible for this company given the challenges in the financing markets and the U.S. auto market," said Durc Savini, head of the auto-supplier practice for Miller Buckfire & Co., a New York turnaround firm that advised on the bankruptcy proceedings of Dana Corp. and Dura Automotive, auto-parts makers that emerged from protection earlier this year.

Delphi currently has $4.3 billion in bankruptcy loans, called debtor-in-possession, or DIP, financing. It expires at the end of the year, so Delphi will have to line up new financing amid tight credit markets and tumbling U.S. auto sales.

Because DIP lenders are paid back before any other creditors, such financing is ordinarily considered quite safe. But Delphi's current DIP financing trades in the secondary market at about 82 cents on the dollar, a discount that indicates doubts about Delphi's solvency.

"For DIP to trade at 80 cents says people have no confidence it will come out of bankruptcy," says Judith Elkin, a bankruptcy lawyer at the law firm of Haynes & Boone, which worked on the Delphi case for outside investors until earlier this year. "It has no stand-alone plan or an exit financing, so it's going on a hope and a prayer."

Delphi's current DIP lenders, led by **J.P. Morgan Chase** & Co., have hired turnaround firm **Alvarez & Marsal** as a financial adviser to study the situation, an unusual step, according to several people familiar with the financing. The banks also have retained **Blackstone Group** LP to gauge the interest of other lenders in taking a piece of any new bankruptcy loan, these people say.

There are signs that J.P. Morgan and other lenders will be reluctant to extend the current financing, or will exact a steep price from Delphi and GM to get it done. "DIP lenders are probably going to demand GM put in a lot of money, maybe cover the DIP themselves or pay down first lien, or demand some sort of preferred equity in Delphi. It will be very difficult," says one person involved in the effort. A J.P. Morgan spokeswoman declined to comment.

After Delphi sought bankruptcy protection, Chairman Robert S. "Steve" Miller, a turnaround specialist who also served as chief executive officer, negotiated new agreements with the United Auto Workers and GM that shed thousands of jobs and got Delphi out of unprofitable business lines such as chassis and brake hoses. It closed 21 of 29 U.S. factories, cut its hourly work force nearly in half, and let go 40% of its salaried staff.

Delphi lost $1.14 billion on sales of $10.48 billion during the first half of this year, compared with a loss of $1.35 billion on sales of $11.68 billion in the year-ago period.

In a successful bankruptcy reorganization, holders of company bonds often recover a substantial portion of the bonds' face value, frequently in the form of new stock. A year ago, Delphi bonds that mature in 2009 were trading at near face value, a sign that investors were expecting a successful reorganization. Now they trade at about 11 cents on the dollar, according to Robert W. Baird & Co., signaling a loss of confidence in Delphi's ability to reorganize. Stock in Delphi, which traded around $2 a share for much of last summer, now hovers around seven cents.

Delphi's struggles threaten to further complicate GM's effort to turn around its own North American operations. GM has been buying out workers and closing plants, and is rushing to implement a $15 billion liquidity plan intended to keep it afloat through 2009.

GM needs Delphi, its largest parts supplier. Without Delphi, it would have to buy parts from other suppliers, who likely would be unwilling to absorb the kind of losses Delphi swallows on the auto maker's behalf.

GM could take the wheel in the event of a Delphi liquidation. It could take back U.S. plants it once owned, which today mostly produce GM parts. GM also could help Delphi sell off other assets.

CORPORATE NEWS

Oxygen bottle blamed for Qantas midair blast

Equipment in hold exploded to cause tear in 747's fuselage

By Bruce Stanley

HONG KONG—Investigators blamed an exploding oxygen bottle for tearing a two-meter-long hole in the fuselage of a **Qantas Airways** Boeing 747 in July and shifted attention to other airlines around the world that may have similar equipment.

The Australian Transport Safety Bureau, which is leading the investigation, advised other airlines equipped with similar steel bottles to inspect them and ensure they are being maintained properly. The bureau is working with **Boeing** Co., other airlines and the bottle's manufacturer—which it declined to identify—to recover other bottles from the same manufacturing batch as the one that failed.

Australian air-safety officials also are continuing a high-level review of Qantas safety, said a spokesman for another agency, the Australian Civil Aviation Safety Authority. The review follows several other minor incidents at the airline; in the latest such event, a Qantas flight Sunday from Singapore to London diverted to Frankfurt after its crew shut down an engine because of a vibration. Qantas said it is working closely with the regulators, and results are expected this week.

The Qantas 747-400 involved in the oxygen-bottle explosion was carrying 346 passengers and 19 crew members to Melbourne from Hong Kong on July 25 when passengers reported hearing a loud bang and experienced a sudden loss of air pressure. The plane diverted safely to Manila with no fatalities.

The bottle contained oxygen for passengers to breathe in an emergency and was one of 13 such bottles in the 747's cargo hold. The bottle itself was missing after the incident, and investigators believe it was sucked out of the hole it tore in the right side of the plane's fuselage, the ATSB said in a preliminary report of its findings.

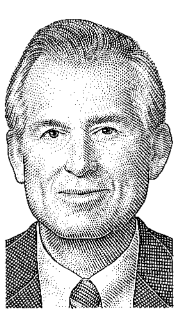
The bureau issued two "safety advisory notices" Friday. One of them encouraged other airlines fitted with pressurized oxygen bottles "to note the circumstances detailed in this preliminary report, with a view to ensuring that all oxygen cylinders, and cylinder installations, are maintained in full accordance with the relevant manufacturer's requirements."

The ATSB also urged all organizations that inspect, test, maintain and repair aviation oxygen bottles to study the report and ensure that their procedures and employees meet "the applicable regulatory requirements and established engineering best practices." Qantas said it welcomed the ATSB's report.

Boeing labor union calls for strike that would further delay the 787

By J. Lynn Lunsford

Boeing Co.'s largest labor union called for a strike, setting up a battle that has the potential to derail the company's core commercial-airplanes unit at a time when customers are clamoring for fuel-efficient airplanes.



Jim McNerney

"The company had an opportunity to come to its employees with an offer that rewarded them for their hard work by offering a top-of-the-industry contract and some real job security, and it failed on all counts," said Mark Blondin, aerospace coordinator for the International Association of Machinists and Aerospace Workers.

Two-thirds of the members must vote against the proposal Wednesday for a strike to occur. In 2005, the union struck for 28 days. In 2002, the union rejected the contract but failed to gain enough votes to strike.

The union leadership's condemnation of the proposed three-year contract, which would boost union members' wages by $34,000 on average over the period, came as a surprise to Boeing officials. They said they had hoped this year to deliver a contract that would avoid stirring up some of the tensions that had bedeviled previous negotiations.

A strike would be a severe blow to Boeing, which is running at full capacity to meet an unprecedented demand for more-fuel-efficient jetliners. A strike would also further delay development and deliveries of the 787 Dreamliner, which is already running roughly two years behind schedule with nearly 900 orders already on the books.

When Boeing officials delivered their so-called best and final offer Thursday, they said that the offer had been personally approved by Boeing Chairman and Chief Executive Jim McNerney, as well as the board of directors and Boeing Commercial Airplanes President Scott Carson.

Boeing officials have repeatedly said they want to avoid a strike, but they also insist that they won't do so at the expense of agreeing to a labor contract that hampers the company's ability to compete in what is increasingly a cutthroat sales environment.

Boeing spokesman Jim Proulx said the company was "extremely disappointed" with the union's recommendation. He said Boeing believes the company's offer "rewards employees for the company's success and allows us to remain competitive."

Under the contract that will expire Wednesday, the average Boeing machinists earned about $27 an hour, or $56,000 a year before overtime.

Mr. Blondin said union members were expecting a raise of at least 13%, rather than the 11% the company offered.

GLOBAL BUSINESS BRIEFS

Evraz Group SA

Price gains, acquisitions boost first-half profit

Russian steelmaker **Evraz Group** SA said first-half net profit jumped 82%, lifted by acquisitions and higher steel prices. London-listed Evraz, part-owned by billionaire Roman Abramovich, said net profit rose to $2.04 billion from $1.12 billion a year earlier. Revenue rose 78% to $10.73 billion, topping the company's April forecast as Evraz lifted crude steel and semifinished product output and prices rose amid strong domestic and international demand. The company expects full-year revenue of $23.2 billion to $24.6 billion. Evraz has recently consolidated an array of acquisitions including U.S.-based Oregon Steel Mills Inc. and Claymont Steel Holdings Inc., South Africa's Highveld Steel & Vanadium Corp. and the steel and pipe business of Ipsco Canada.

Hermès SA

Hermès SA said first-half profit rose 5.3%, bolstered by strong sales in Europe, the U.S. and China. The maker of Kelly and Birkin bags said net profit rose to €134.9 million ($197.9 million) from €128.1 million. Hermès recently reported that first-half sales grew 13% to €813.2 million. Operating margin rose to 25% in the first half on a 14% jump in operating profit. Hermès poured €90 million into development in the period, including buying a building in Geneva to enlarge its store there. During the second half, Hermès will open or renovate about 15 boutiques, focusing on Europe and Asia. Hermès increased its stake in French fashion house Jean-Paul Gaultier to 45%; Mr. Gaultier designs Hermès's women's clothing collections.

Bradford & Bingley PLC

British buy-to-let lender **Bradford & Bingley** PLC said write-downs and increasing impairments on mortgages pushed it to a net loss in the first half. The bank, which has lost 86% of its value in the past year, had a loss of £17.2 million ($31.4 million) after a profit of £129 million a year ago. Profit was hurt by £155 million in write-downs, fair-value changes, and losses realized after the sale of credit investments. It also recorded impairment charges on bad loans of £74.6 million, up 93% from £5.3 million. Net interest income dropped 9% to £246.7 million from £271.2 million, and the net interest margin fell to 0.98% from 1.1% at the end of December. Last month, holders supported less than one third of B&B's £400 million rights issue.

Natixis SA

Shareholders of **Natixis** SA overwhelmingly approved the French investment bank's plan to raise €3.7 billion ($5.4 billion) through a rights issue to beef up its balance sheet. Although two hedge funds—Greenlight Capital and Royal Capital Management—had called for a smaller rights offer and additional capital-raising steps, the outcome of the vote was never seriously in doubt since the proposal had the support of Natixis's two founders and main shareholders. At a meeting in Paris, 94.2% of votes from almost a billion shareholders represented at the meeting favored the resolution. Natixis now needs regulatory approval from the French stock-market regulator AMF before it can launch its rights issue.

Dexia SA

Belgian-French bank **Dexia** SA warned the continuing economic slowdown will hit results in the second half despite strong underlying growth in its core public-finance business in the second quarter. Its public-finance division reported an underlying net profit, meant to reflect operating performance by stripping out the impact of the bank's lower valuation of some of its securities, was €71 million ($104.2 million), down from €338 million a year ago. Excluding losses at its troubled bond insurer FSA, however, the result rose 50% to €398 million, Dexia said. The bank had reported preliminary results for the quarter earlier this month, and confirmed Friday group net profit for the quarter fell 32% to €532 million.

Imperial Energy Corp.

London-listed oil company **Imperial Energy Corp.**—the object of a takeover bid by India's state-run **Oil & Natural Gas Corp.**—Friday posted a smaller first-half net loss thanks to soaring oil prices and increased production. Imperial's net loss narrowed to $18.9 million from $20.7 million a year earlier, while revenue jumped sharply to $67.5 million from $4.2 million. Average oil production for the first six months was roughly 6,200 barrels a day, while the current rate of production exceeds 11,000 barrels a day, said Imperial. The company, which has assets in Siberia and Kazakhstan, said it remains on track to achieve production of 25,000 barrels a day by the end of the year and 35,000 barrels a day by the end of 2009.

Novartis AG

Switzerland-based drug maker **Novartis** AG said Friday it will take a $235 million charge after it halted development of its Aurograb treatment for bacterial infections because it showed a lack of efficacy in midstage trials. Novartis acquired the compound two years ago as part of its takeover of U.K. drug maker NeuTec Pharma, a specialist in fighting hospital superbugs. The drug maker said the charge, reflecting the full amount allocated to the project, would be taken in its third-quarter results. J.P. Morgan analysts said the move would have "no significant impact on Novartis," although it would be "a small negative for sentiment." The company said late-stage testing is continuing for Mycograb, another experimental compound acquired through the NeuTec purchase.

Benetton Group SpA

Apparel retailer **Benetton Group** SpA posted a 2.5% rise in first-half net profit and warned it now expects full-year like-for-like revenue growth to be at the lower end of its forecast. Net profit rose to €72 million ($106 million) from €70 million a year earlier as revenue inched up to €996 million from €990 million. The retailer, based in Ponzano in northeast Italy, said growth was hindered by administrative costs and expenses made to improve its supply chain, as well as the strong euro. Benetton expects full-year capital expenditures to total €250 million as it continues to open new stores in strategic markets and enhance its production plant in Tunisia. The retailer said it still anticipates full year profit to grow at least 7%, but warned that like-for-like revenue growth will likely be around 6%.

Banco Popolare SpA

Italian mutual bank **Banco Popolare** SpA said Friday its first-half net profit grew 43% to €391 million ($573.7 million), and it confirmed its 2008 targets. In a statement, the Verona-based bank said it is able now "to reach the results indicated for 2008 in the three-year plan." The bank has a 30.7% stake in Banca Italease SpA, which returned to profit for the first quarter after heavy losses in 2007 as derivatives contracts weighed. Banco Popolare itself is changing strategy to focus on retail and on credit to small and midsize companies. Previous-year figures are pro forma as it was created in July 2007 from the merger of regional lenders Banco Popolare di Verona e Novara and Banca Popolare Italiana. Banco Popolare said its Tier 1 ratio was 5.6% and it said this should reach 7.4% by year end.

WPP Group PLC

U.K advertising company **WPP Group** PLC, which has made a hostile bid for **Taylor Nelson Sofres** PLC, said Friday it has received acceptances for 8.61%, or 35.9 million, of TNS shares and extended its offer until Sept. 12. Friday was the original close date for WPP's cash-and-share bid for the U.K.-listed market-research firm. Based on WPP's closing share price on Friday of 537.5 pence, the value of its bid was about £1.203 billion ($2.19 billion). Wednesday, the only other potential suitor, German peer GfK AG, abandoned talks with TNS amid funding difficulties. Before GfK's withdrawal, shares in TNS were trading above the level of WPP's cash-and-shares bid but have fallen since.

BP PLC

Enbridge Inc. and **BP** PLC have agreed to spend as much as $2 billion to transport heavy Canadian crude from Illinois in the U.S. Midwest to the Gulf Coast with a combination of existing and new pipelines. The effort follows BP's announcement in December that it was taking its first plunge into Canada's booming oil sands, agreeing to an asset swap and investment plan with Husky Energy Inc. that calls for spending $5.5 billion over the next seven years. A BP affiliate is expected to be a major user of the envisioned pipeline system, but other shippers would be able to use the network through arrangements expected to be set this fall. The system will be able to carry as much as 250,000 barrels a day to the Gulf Coast.

Origin Energy Ltd.

Origin Energy Ltd. beat expectations by posting a 20% rise in full-year earnings as the Australian energy company tries to ward off a hostile takeover bid from **BG Group** PLC. Origin said net profit in the year ended June 30 rose 13% to 516.7 million Australian dollars ($443.5 million). Underlying net profit, a figure more widely watched by analysts, rose 20% to A$443 million. Group revenue rose 29% to A$8.27 billion. Last week, Origin formally recommended shareholders reject BG's sweetened offer on grounds it undervalues the company's businesses and growth prospects. Despite the current bid being pitched at a 48% premium to Origin's near record price in April, Origin believes it can offer shareholders better value.

—Compiled from staff and wire service reports.

ECONOMY & POLITICS

BELGIUM

'Serious' nuclear incident occurs near lab in Fleurus

Belga

BELGIAN authorities have restricted consumption of vegetables and milk produced near a nuclear-medicine institute after a leakage of radioactive iodine, the European Commission said.

The institute in Fleurus produces radioisotopes used to treat cancer. The measures were taken after samples of local grass showed higher-than-expected contamination. A commission spokesman said he was unaware of anyone being contaminated.

Belgium's nuclear-control agency said Thursday that the incident, which took place the previous weekend, was "serious" and rated it three out of seven on the International Nuclear Incident Scale. —*Reuters*

MOROCCO

Al Qaeda terror cell found; police arrest 15 suspects


Associated Press

MOROCCAN police have dismantled a new al Qaeda-linked terror cell, arresting 15 suspects in various towns across the country, the official MAP news agency reported.

The "dangerous terrorist network" was planning attacks in Morocco and was found in possession of chemicals and electronic devices to make bombs, the report said, citing security officials. An official from Morocco's Interior Ministry wasn't immediately available to comment. The group, known as Fath al-Andalus, had "operational links with foreign extremists belonging to al Qaeda," the MAP agency quoted police as saying. —*The Associated Press*

IRAN

Uranium enrichment goes beyond experimental level


Reuters

IRAN IS operating nearly 4,000 centrifuges at its uranium enrichment plant, lifting its nuclear program further out of the experimental stage and to an industrial level.

Deputy Foreign Minister Ali Reza Sheikh Attar told the official IRNA news agency that Iran was preparing to install 3,000 more centrifuges at the plant in Natanz. Iran says it aims to provide fuel for power plants, but the process can produce fuel for nuclear weapons.

The U.S. and its allies have sought a halt to Iran's uranium enrichment. A total of 3,000 centrifuges is the commonly accepted figure for a program that is past the experimental stage. —*Associated Press*

U.K. housing aid is urged

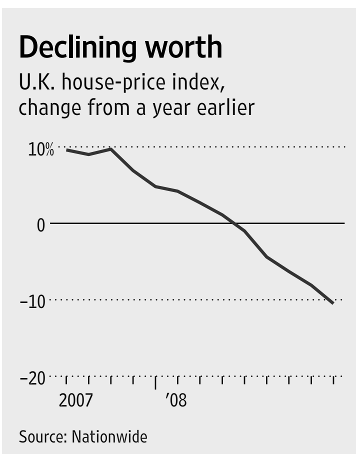
Surveyors seek steps to boost availability of mortgage funding

By PAUL HANNON
London

THE ROYAL INSTITUTION of Chartered Surveyors called on the British government to take "significant and decisive action" to support the housing market, which has seen a collapse in sales since the credit crunch began in August of last year.

Among a number of proposals, the group urged the government to boost the availability of mortgages by allowing investors to swap mortgage-backed securities and covered bonds with the Bank of England in exchange for Treasury bills.

Mortgage-backed securities were a significant source of funding for U.K. mortgage lenders before the onset of the credit crunch. U.K. lenders issued €96.2 billion ($141.14 billion) of such bonds in the first half of 2007.



But issuance ground to a halt as the credit crunch bit and has yet to recover, with investors shunning complex securities.

In April, the central bank launched a special lending facility allowing banks to swap mortgage-backed securities for Treasury bills. However, the program prohibited the Bank from accepting securities backed by mortgages made after December 2007.

Under the proposal, loans made after that date would be eligible. But mortgage-backed securities and covered bonds would first have to be sold in a public offering to investors before being swapped.

However, Bank of England Gov. Mervyn King has made it clear that he is opposed to extending the existing swap facility to new mortgages.

"Funding is not something that a central bank can provide," Mr. King said in an Aug. 13 news conference.

With the central bank strongly opposed, the proposal for reopening the mortgage-backed securities market may not make much headway.

The group also said the government should temporarily suspend a transactions tax on house purchases, which is known as stamp duty.

The surveyors predicted that home repossessions will rise 50% in 2008, to total more than 45,000.

Darling is downbeat on economy

By LAURENCE NORMAN
AND ALISTAIR MACDONALD

LONDON—Chancellor of the Exchequer Alistair Darling said the U.K. could be facing the worst economic conditions in 60 years.

In an interview with the Guardian newspaper Saturday, Mr. Darling said the economic difficulties the U.K. is facing "are arguably the worst they've been in 60 years. ... And I think it's going to be more profound and long-lasting than people thought."

The U.K. Treasury chief's gloomy assessment of the economy appeared—not for the first time—at odds with that of Prime Minister Gordon Brown, who often talks of the U.K. economy's "resilience." During the weekend, opposition politicians interpreted the comments as a sign there was a split at the top of government over the economy. Spokesmen for the Treasury and the prime minister's office said there was no difference of views and that Messrs. Darling and Brown both say the U.K. is well-positioned to weather the economic storm.

In an interview later with the British Broadcasting Corp., Mr. Darling defended his assessment of the economy and signaled the government is ready to take action to cushion people from the downturn.


Alistair Darling

"We have a credit crunch the like of which we haven't seen in generations. We have it at the same time as oil and food prices are going up. But I also am clear that the fundamentals of our economy are strong," he said. "We will do whatever is necessary to help people and to help the economy through what are undoubtedly unique circumstances."

The government is expected to announce a package of measures to help the economy when ministers return from summer vacation. Expected measures include steps to boost the housing market, which has seen prices sink in recent months.

The U.K. economy stagnated during the second quarter and the Bank of England predicts zero growth for the next year. Many economists expect the economy to fall into recession. Meanwhile, accelerating inflation has curtailed the bank's ability to ease monetary policy. Consumer-price inflation stands at a 4.4% rate, more than double the Monetary Policy Committee's 2% target.

In the Guardian interview, Mr. Darling said he didn't expect that there would be a leadership challenge against Mr. Brown this fall, despite the governing Labour Party's troubles in the polls. He acknowledged, however, that people were angry with the government over the economic situation.

Key index may overstate mortgage-debt problems

By JOELLEN PERRY

FRANKFURT—The prices of a key index that banks use to gauge their subprime-related losses have been damped partly by factors that have little to do with the risk that borrowers could default on mortgages, according to a Bank for International Settlements report that could add to growing concern about how markets measure the severity of mortgage-debt problems.

The BIS report released Sunday also says global banks have been funneling more funds out of the U.S. than into it since market turmoil erupted in the summer of 2007. BIS data suggest that foreign banks hungry for dollars could be sending funds from U.S. branches to their offices abroad, while global lending to U.S. nonfinancial firms has begun flattening after years of growth.

The Switzerland-based BIS, often called the central bankers' central bank, has few formal banking duties but is a hub for economic research and global policy makers. Its quarterly report studies a widely used measure of the subprime mortgage market called the ABX. Run by **Markit Group** Ltd., the ABX is an index that tracks the value of securities backed by subprime loans. Because such securities barely trade, the ABX gets direction from actively traded instruments that insure against default on the securities, called credit-default swaps. The ABX often is used as a proxy for the value of mortgage-backed securities. Swiss bank UBS AG used the ABX in 2007 to help estimate an additional $10 billion write-down on its subprime-mortgage investments.

Housing-market factors including the likelihood that borrowers could default on mortgages have contributed to sharp declines in the ABX since last summer. But the BIS report also says that "declining risk appetite and rising concerns about market illiquidity have provided a sizable contribution to the observed collapse in ABX prices."

Other market observers have said ABX prices have been driven down largely by bearish traders. The BIS found that ABX indexes tracking highly rated securities, such as those with triple-A ratings, were particularly sensitive to investor fears that had little to do with default risk. That could suggest investors are using the indices "as a macro hedge or to express negative trading views on the U.S. housing market," according to the BIS.

A BIS study in June suggested estimates of triple-A subprime-security losses that rely on the ABX could be overstated by more than 60%, because the index only covers part of the capital structure of relevant deals.

The BIS said some investors may be using the indices as a 'macro hedge.'

Separately, the BIS report said that, from 2000 though the middle of 2007, global banks funneled over $1 trillion more into the U.S. across their balance sheets than they withdrew. But since mid-2007, banks have sent about $321 billion more out of the U.S. than they sent in. One potential cause: "a broader shift in bank balance sheets away from the U.S. nonbank private sector."

European banks, which have boosted dollar-denominated investments in recent years, may also be raising more dollars stateside to send to their overseas affiliates.

Amid growing concern that central banks could become storehouses for hard-to-sell securities, the BIS report says banks boosted their issuance of mortgage-backed bonds to $188 billion during the second quarter of 2008 compared with the first quarter's $52 billion. The biggest increase came from U.K. banks. But in June, a Belgian institution also issued mortgage-backed bonds totaling more than $23 billion.

Gustav scrambles plans for week

Bush, Cheney cancel appearances as party treads delicately

U.S. President George W. Bush and Vice President Dick Cheney both canceled appearances at the Republican National Convention Monday because of Hurricane Gustav, as convention planners scrambled to cope with political and practical implications of the mammoth storm.

Republican candidate Sen. John McCain traveled to a hurricane command center in Jackson, Miss., Sunday morning to get briefed on storm preparations. Meanwhile, his top aides considered curtailing parts of the four-day convention. They have discussed possibilities such as shortening or canceling a day's events to avoid being seen as celebrating just as the storm slams into the U.S. Gulf Coast, potentially wreaking massive devastation.

By **Elizabeth Holmes** *in St. Louis,* **Laura Meckler** *in Minneapolis and* **Corey Dade** *in Dublin, Ohio*

Gustav is expected to roar into the Gulf Coast Monday as a Category 3 or 4 storm, the same day the convention is scheduled to begin. Politically, the timing couldn't be worse. The third anniversary of Hurricane Katrina has already dredged up painful reminders for the Republicans of the Bush administration's botched handling of one of the biggest natural disasters in U.S. history—a debacle that continues to dog the Republican Party.

The decisions of Messrs. Bush and Cheney to stay away may not have been entirely unwelcome for Sen. McCain, who has repeatedly tried to distance himself from the administration. At the same time, Sen. McCain is eager for a chance to upstage his rival, Democratic nominee Sen. Barack Obama.

Sen. Lindsey Graham of South Carolina, one of Sen. McCain's closest friends and advisers, said Sunday on ABC's "This Week" that "it might" make sense to cancel the convention's early days and concentrate the entire event into the final night on Thursday, when Sen. McCain is scheduled to deliver his acceptance speech.

"The goal is to make sure that you take the conservative approach," he said. "That you're not seen to be out of touch with people who could have everything they've worked for lost. And no one here, no one in Sen. McCain's inner circle, wants to do anything to be insensitive to what is coming."

He also said Republicans have to be very conscious about how their actions appear this week.

"The goal is to make sure we get it right, that we let the country know, the people on the Gulf Coast know that we're not going to do anything here inappropriate. To use this convention to raise money, to help people who are going to be affected by the hurricane, and to make sure we send the right signal to people in harm's way."

Sen. McCain and his running mate, Alaska Gov. Sarah Palin, were en route to Mississippi for a few hours on Sunday but were expected to return in time for a long-planned rally in Missouri.

Sen. Obama, on the other hand, dodged a question about whether he would travel to storm-damaged areas. Instead, he expressed concern about whether it would be disruptive. "Sometimes we can be a distraction in those kinds of situations," he said following a campaign stop in Dublin, Ohio. "So we want to make sure that we're monitoring the situation, and we're being useful. I will do whatever is required to be useful."

Reuters

Sen. John McCain pauses while speaking as his running mate, Alaska Gov. Sarah Palin, looks on at the Mississippi Emergency Management Agency command center Sunday.

Among the options Sen. McCain's campaign is considering for the convention: canceling one day of activities; transforming the gathering into a giant hurricane-relief telethon; asking party sponsors to cancel the outside events planned for the week; and altering the tone of the speeches to better reflect the storm. "The reality is we're likely going to have a national disaster going on," said a senior McCain adviser involved in the decision making. "We don't know exactly what this thing is going to do or when."

Asked by Fox News Sunday's Chris Wallace whether there were any circumstances in which he would consider suspending the convention, Sen. McCain said: "I'm afraid, Chris, that we may have to look at that situation and we'll try to monitor it." He said he had been in touch with the governors of Louisiana, Alabama, Texas, and Florida. "I've been talking to all of them, but you know it just wouldn't be appropriate to have a festive occasion while a near tragedy or a terrible challenge is presented in the form of a natural disaster, so we're monitoring it from day to day and I'm saying a few prayers too."

Senior adviser Mark Salter said Saturday that the campaign was still waiting to see how the storm would develop and where it would make landfall before making any decisions.

The convention will unavoidably feature some sort of ceremony because law requires the party to officially nominate a candidate, and that candidate must accept. The senior adviser said it was almost certain that Sen. McCain will still deliver a prime-time address, a politically important moment to speak to many voters who don't normally hear his words.

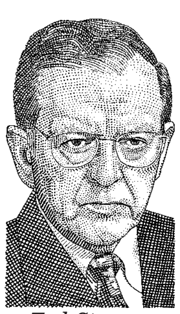
—John D. McKinnon contributed to this article.

Some fighting for seats will skip convention

By Sarah Lueck

WASHINGTON—As Republicans gear up for their party's convention in Minnesota, some of the party's members of Congress are taking a pass.

Out of seven Republican senators facing the most competitive challenges, five will stay in their home states, saying their time is better spent campaigning. Sen. John Sununu "will continue his town-to-town, person-to-person campaign throughout New Hampshire," said spokeswoman Stefani Zimmerman. For Sen. Gordon Smith of Oregon "it's far more valuable for him to spend his time campaigning," said spokeswoman Lindsay Gilbride.



Ted Stevens

Of 19 House Republican incumbents in competitive races, at least six plan to skip the event. Four of the members staying away, including Rep. Randy Kuhl of Michigan, are those with the toughest challenges, in the judgment of the nonpartisan Cook Political Report. "There's a lot to do here in the district," said Mr. Kuhl's spokesman Justin Stokes.

The absences underscore the rough election year facing congressional Republicans. Some Republicans are predicting significant losses in the House and Senate, even if Sen. John McCain keeps the White House in Republican hands. A big reason: the negative views many voters have of President George W. Bush and the Republican Party. For some incumbents, appearing at the convention could undercut their attempts to show independence from Washington.

Things were different in 2000, when Republicans were revved up about the chance to take the White House back from Democrats. That year, all five of the Republican senators who ended up losing their seats to Democrats attended the convention in Philadelphia. Of five Republican House members who ultimately lost, four showed up.

Republicans who are skipping the convention this year say the issue is primarily timing. The event is scheduled to begin at the beginning of the most intensive campaigning in congressional races.

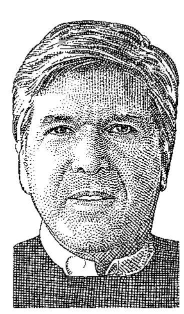
Mark Kirk

Sen. Elizabeth Dole, who spoke at the 2004 Republican convention, is facing a tough challenge this year for her North Carolina seat. On Monday, when some other Republican senators are speaking in Minnesota, she is scheduled to be at a parade in Hendersonville, N.C., celebrating the town's Apple Festival.

"I think it says she's up for re-election," said spokesman Hogan Gidley. "She's just going around the state reminding people what she's been able to accomplish."

Sen. Ted Stevens of Alaska, who was recently indicted in a corruption scandal, will also not attend. Staying home to campaign "has been the senator's plan all along," said spokesman Aaron Saunders. Mr. Stevens has said he is not guilty of the charges.

Other Republicans skipping the convention have a list of reasons explaining why their decision isn't an effort to distance themselves from the national party. Rep. Joe Knollenberg of Michigan is holding a series of town-hall meetings focusing on small businesses, hospitals and economic troubles in the district, says spokesman Nate Bailey. Rep. Phil English (R., Pa.) gave up his spot as a convention delegate so that someone from outside his county would have a chance to go, said spokesman Adam Beebe.



Gordon Smith

John Kennedy, a Republican trying to oust Democratic Sen. Mary Landrieu in Louisiana, won't attend the convention. "There's no down time anymore," said Lenny Alcivar, Mr. Kennedy's spokesman.

The campaign organizations for House and Senate Republicans didn't pressure incumbents in tight races to go to the convention. "There are more votes back home than there are in Minnesota," said Ken Spain, press secretary for the National Republican Congressional Committee.

Rebecca Fisher, communications director for the National Republican Senatorial Committee, said: "Our candidates in tight races are exactly where they need to be—on the ground speaking directly to their voters."

Some Democratic incumbents facing tough races, particularly those running in heavily Republican areas, also skipped their party's convention. They cited the same reason as Republicans, a desire to focus on campaigning.

Some Republicans are scheduled to attend, and even speak, during the convention, including Reps. Mark Kirk of Illinois and Lincoln Diaz-Balart of Florida.

Platform carries few references to candidate

By Nick Timiraos

Republicans are set to ratify a party platform this week that includes sharp reversals from 2004 on hot-button issues like immigration, and makes scant reference to Sen. John McCain.

This year's platform doesn't embody the philosophy of the presumptive Republican nominee as closely as past platforms have, although some measures like government reform bear Sen. McCain's stamp.

The past two platforms bore the strong imprint of George W. Bush, with the 2004 document mentioning him more than 250 times, and the 2000 one more than 40 times.

The party platform is written primarily for the party base and often represents an expression of the party's stances on a range of policy issues. Before the party had settled on Sen. McCain as its flag bearer, party leaders opted for a "smaller, more principled, more forward-looking" platform this year that didn't emphasize its nominee, said Rep. Kevin McCarthy (R., Calif.), who chaired the platform's drafting committee.

Besides one reference in the one-page preamble, the platform makes no other mention of Sen. McCain, who has had a sometimes-strained relationship with other Republicans over his tendency to break with party orthodoxy.

Despite some big policy disagreements, a floor fight over the platform, like one that erupted over abortion in 1996, remains unlikely because conventions these days are tightly scripted to display party unity.

The legislative advocacy arm of the Family Rights Council, a political advocacy group for social conservatives, hailed the document as the most "conservative, pro-life and pro-family platform in Republican party history."

The sharpest policy shift from the 2004 platform concerns immigration, which makes up one of the first and lengthiest topics in this year's platform. It rejects "amnesty," calls for stronger border security and defines immigration as a "national security issue." It also calls for the English language to be "recognized and promoted" by the federal government.

Four years ago, moderate Republicans prevailed in calling for an immigration overhaul that was "legal, safe, orderly and humane" and pushing for a temporary, legal guest-worker program in a short section at the end of the platform. Sen. McCain supported the Bush administration's immigration bill, which collapsed after a revolt by the conservative wing of the party. The senator's support of the bill angered many would-be backers of his presidential bid.

On global warming, moderates this year succeeded in adding language acknowledging that man-made carbon emissions have "a warming effect on the earth" and that the U.S. should take "measured and reasonable steps today"—a position that is similar to Sen. McCain's.

The 2008 platform strongly opposes gay marriage and abortion, and supports a constitutional amendment to ban both. Sen. McCain opposes such a ban.