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U.S. seizes control of Fannie, Freddie

Government steps in as the housing slump threatens economy

By James R. Hagerty And Ruth Simon

The U.S. government, increasingly alarmed by a housing slump that threatens to pull down the whole economy, is taking over the business of ensuring that funding is available for home mortgages.

The U.S. Treasury announced a plan Sunday that provides as much as $200 billion of new capital plus new credit lines for the country's main suppliers of funds for home loans, **Fannie Mae** and **Freddie Mac**, and puts the two companies under management control of their regulator, the Federal Housing Finance Agency, or FHFA. Treasury Secretary Henry Paulson said the moves will increase the availability of credit for home buyers.

The Treasury also plans to buy an unspecified amount of mortgage-backed securities issued by Fannie and Freddie in an effort to bring down borrowing costs for home buyers. Despite steep interest-rate cuts by the Federal Reserve, the cost of a typical 30-year fixed-rate mortgage has remained well above 6% for most of the past year.

The moves are likely to nudge down interest rates for consumers and help prevent a worsening of what is already the worst housing bust since the 1930s. At least in the short run, the actions also further entrench the government in a mortgage industry, leaving taxpayers exposed to default-related losses that could run into the scores of billions. In the longer run, Mr. Paulson aims to drastically shrink the amount of mortgages and related securities held by the companies, but he noted it will be up to Congress and future administrations to decide what shape Fannie and Freddie ultimately take.

Mr. Paulson said the government had no choice other than to prop up Fannie and Freddie, companies created by Congress to support the housing market but owned by private shareholders. The more than $5 trillion of debt and mortgage-backed securities issued by the companies is owned by central banks and other investors world-wide. "A failure of either of them would cause great turmoil in our financial markets here at

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Associated Press

U.S. Treasury Secretary **Henry Paulson Jr.** speaks during a Sunday news conference in Washington on the bailout of mortgage giants Fannie Mae and Freddie Mac.

What's News—

Business & Finance

The U.S. government is taking over Fannie Mae and Freddie Mac, the nation's main suppliers of funds for home loans, amid its concern the housing slump threatens the entire economy. The move was welcomed by some banks and market watchers outside the U.S. Pages 1, 30

■ **OPEC members** face a dilemma on whether to cut oil production with the world economy still on the ropes. Page 1

■ **Ford CEO Mulally is hoping** to revive the auto maker by bringing European small cars to the U.S. market. Page 4

■ **BMG and Daimler posted** strong sales for their compact brands in August as core larger cars drew less demand. Page 4

■ **Boeing's machinists** walked out on strike after their union was unable to reach an agreement with company officials on a new contract. Page 6

■ **U.S. output is rising** while jobs and wages are under strain, suggesting the business cycle itself is changing. Page 3

■ **GDF Suez** is in exclusive talks with the Dutch firm NAM over buying gas assets valued at about $1.54 billion. Page 6

■ **Analysts question** if the bailout of Fannie Mae and Freddie Mac will be more than a temporary fix for the ailing economy and financial markets. Page 17

Markets

MARKET	CLOSE	NET CHG	PCT CHG
DJIA	11220.96	+32.73	+0.29
Nasdaq	2255.88	-3.16	-0.14
DJ Stoxx 600	272.24	-5.94	-2.14
FTSE 100	5240.7	-121.4	-2.26
DAX	6127.44	-152.13	-2.42
CAC 40	4196.66	-107.35	-2.49
Euro	$1.4265	-0.0120	-0.83
Nymex crude	$106.23	-1.66	-1.54

Money & Investing > Page 17

World-Wide

Germany's Social Democrats nominated Foreign Minister Steinmeier to lead the party into national elections next September against Merkel's conservatives, as their party is faced with crumbling support and a growing challenge from the far left. Page 3

■ **Ike roared** over the southern Bahamas as a Category 4 hurricane, killing at least 10 in Haiti flooding. Cuba braced for a hit. Florida Keys began evacuating.

■ **Sarkozy visits** Moscow Monday in a bid to convince Russia to fully implement a cease-fire pact with Georgia. Cheney bluntly criticized Russia. Page 10

■ **Zardari won election** as Pakistan's president for a five-year term and will be sworn in Tuesday. A car bomb Saturday in Peshawar killed at least 35. Page 10

■ **The Bush administration** will push Congress to pass legislation this month needed to secure a nuclear-cooperation deal with India before Bush's term ends. Page 9

■ **A rockslide outside Cairo** crushed a shantytown, killing at least 31 people and spurring anger at the government. Page 10

■ **Angolan officials said** the ruling party had a big lead in early results of parliamentary voting. A final tally is expected Monday.

■ **Canadian Premier Harper** dissolved Parliament and called an early election for next month.

■ **Iraq's cabinet approved** an initial deal between the Oil Ministry and Royal Dutch Shell to tap natural gas in southern Iraq.

■ **Two suicide bombers struck** police headquarters in Kandahar, Afghanistan, killing two officers.

Editorial & Opinion

Schröder II

Frank-Walter Steinmeier's nomination has an air of desperation. Review & Outlook. Page 11

OPEC choice: to cut output or not to cut

By Neil King Jr. And Spencer Swartz

Meeting for the first time since March, OPEC ministers on Tuesday face a quandary: With the world economy still on the ropes, do they really want to be seen slashing oil production in an effort to keep prices above $100 a barrel?

To cut or not to cut—and if so, when—will dominate debate when the cartel's 13 ministers huddle in Vienna. After pleading helplessness for months as crude prices soared, officials from Venezuela, Iran and Libya say they would like the group to start trimming production to halt the steep fall in prices since late July. Big producers such as Saudi Arabia, Iraq and Nigeria have been either mute or in favor of maintaining the status quo.

Few doubt that the Organization of Petroleum Exporting Countries has the clout to prop prices up. While often feeble when called upon to boost supplies, the group has largely succeeded over the past decade in protecting its interests when prices slide. The question is whether it would be wise to act now, with the U.S. and some European nations still hovering near

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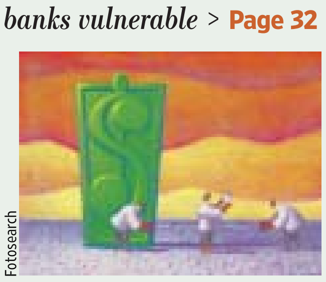
Heard on the Street

Broader strain

The takeover of Freddie and Fannie still leaves banks vulnerable > Page 32



Fotosearch

Presidential candidates embrace Treasury move

By Nick Timiraos

With the long-term future of **Fannie Mae** and **Freddie Mac** likely in the hands of the next president, Sen. John McCain appears more eager than his Democratic rival to support an aggressive revamping of the mortgage-finance giants.

Over the weekend, both presidential candidates embraced Treasury's short-term measures to rescue the companies as a necessary step, but they criticized the need for government intervention.

"We need to keep people in their homes, but we can't allow this to turn into a bailout of Wall Street speculators," Sen. McCain said Saturday at a rally in Albuquerque, N.M. The Republican nominee has told voters anxious over job losses and foreclosures that he wouldn't allow the companies to fail.

Sen. Barack Obama said in an interview aired Sunday that intervention was necessary to "prevent a long-term, much bigger crisis."

Republicans have long pushed for a structural overhaul of Fannie and Freddie. By contrast, Democrats have warned against making major changes until they are stabilized. The two companies have traditionally had stronger backing from Democrats, who support their mission of bolstering affordable housing and for years have fended off calls for greater oversight.

Democrats received 56% of some

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Hazy forecast

LEADING THE NEWS

OPEC debate: to cut or not to cut

Continued from first page

recession.

As always, the spotlight falls on Saudi Arabia, OPEC's dominant member and the world's single largest oil exporter. Saudi oil minister Ali Naimi and his boss, King Abdullah, wrung their hands for months as prices soared to records and criticism poured down from Western capitals that they weren't doing enough to ease the pain.

But their decision in June to ramp up production by an additional 250,000 barrels a day may have helped drive prices down from an all-time high of $147 a barrel in mid-July. Crude prices are now off nearly 30% from that peak, closing last week at $106.83 on the New York Mercantile Exchange. But crude is still up 11% from the start of the year and is about 50% higher than a year ago.

The king has since said he would like to see prices fall below $100 a barrel, while others suggest that the kingdom wouldn't object if crude edged into the mid-$80s range—about where it was for the earlier part of this year. Saudi officials declined to talk about their thinking ahead of the Vienna summit.

Others within OPEC, though, will surely gripe if prices tumble that far. Traditional price hawks Iran and Venezuela have been vocal in saying they want the cartel to begin slashing production now, arguing that the world is oversupplied and that the once-outlandish price of $100 a barrel should become the new benchmark. Plummeting prices could cause distress within months in Venezuela and Iran, whose leaders rely heavily on windfall oil profits to maintain their political positions.

But Saudi Arabia and most of its Persian Gulf allies appear reluctant to do anything rash.

Demand for oil this year is off sharply in the U.S. and Europe. There are signs steep demand growth may be slowing in China. Yet the thirst for fuel continues to grow at a healthy clip elsewhere, particularly within the big oil producers themselves. Energy demand is up sharply in Saudi Arabia, Iran, the United Arab Emirates and Russia, meaning that more oil stays at home and less enters the export market.

Just as Saudi Arabia has quietly added barrels this summer, most analysts expect it will quietly begin lowering its output in the coming months. The kingdom pumped around 9.6 million barrels a day in July but has already begun to trim back. OPEC as a whole supplies around 40% of the 86.5 million barrels a day the world now consumes.

With the lion's share of the world's spare pumping capacity, Saudi Arabia has led every substantial shift in production within OPEC over the past decade, whether by putting extra barrels on the market or taking them off. Between November 2006 and January 2007, OPEC slashed its output by more than 1.5 million barrels a day and kept a clamp on production for nearly a year. The Saudis accounted for more than half of that cut.

OPEC then began to add extra barrels in the fall of 2007, seeing that supplies were tight and prices were beginning to soar. By this July the cartel had put on an extra 2.2 million barrels a day—nearly half of it, again, from Saudi Arabia.

The cartel has moved to cut its formal quotas 12 times in the past 15 years, according to research by Adam Sieminski at Deutsche Bank. OPEC succeeded in 80% of those cuts to either stabilize prices or push them up within three months, Mr. Sieminski found. Its last round of cuts, in early 2007, set the stage for the historic price surge seen over the last year.

That doesn't mean OPEC states don't have their bouts of bickering and failure to abide by production cuts over time—as members try to protect oil revenue. This source of contention could become more pronounced today because a number of OPEC states, such as Venezuela and Iran, need higher oil prices to compensate for increased financial strains, like high inflation.

Talk of cutting OPEC output will revive the long-running debate over whether there should be an optimal price that the group will seek to defend. Mr. Naimi said earlier this year that the $65 or so it costs to produce a barrel of oil from the Canadian tar sands had become the new price floor within the industry. Others argue that the soaring expense of developing new offshore fields means that oil will never again linger below $70 a barrel.

But there are risks for OPEC pursuing such a high oil-price policy. Prices of more than $100 a barrel keeps consumers firmly on the prowl for ways to cut oil consumption. It also helps pay for the pursuit of alternative energy sources, like crop-based biofuels and hard-to-extract heavy oil in places such as Canada, that compete head-to-head with OPEC oil.

Crude-oil price

NYMEX-traded, light, sweet crude on the continuous front-month contract, in dollars per barrel

Source: Reuters via WSJ Market Data Group

Consumers in wealthy nations are employing a variety of tools to escape high oil prices, from abandoning gas-guzzling sport-utility vehicles in the U.S. to using more public transport in Japan, and the impact keeps adding up.

Crude demand in the Organization for Economic Cooperation and Development nations like the U.S.—which account for 56% of total consumption globally—is on course to fall a fourth straight year in 2008.

"The damage of today's high oil price is to demand. Consumers and governments are looking for solutions wherever they can and the more some OPEC states talk about wanting oil above $100, the more consumers search," said Leo Drollas, chief economist at the London-based Centre for Global Energy Studies.

Georgian leader weighs launching a political party

By Brittany Hite

Nino Burjanadze, the former speaker of Georgia's parliament who served as acting president of the country during two interim periods, said she couldn't rule out the possibility of creating a new political party in Georgia but stopped short of openly breaking with President Mikheil Saakashvili.

Some analysts believe that Ms. Burjanadze could emerge as a key opposition figure to Mr. Saakashvili, who has drawn criticism outside the country for his handling of hostilities with neighboring Russia. Russian troops invaded Georgian territory last month amid escalating tensions over two breakaway Georgian regions.

"If it will be helpful, I will do it," Ms. Burjanadze said while speaking at Columbia University in New York on Friday, referring to the possibility of forming a new political party.

Lincoln Mitchell, a professor at Columbia who specializes in Georgian politics, said the establishment of a new party in the country would be a positive step toward furthering democracy. "Georgia is effectively a one-and-a-half party system," he said, noting the government is dominated by a single party, the United National Movement. Opposition political parties are legal and do compete, but the "line between party and government or party and state is very gray, and in a democracy, that needs to be very clear."

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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

LEADING THE NEWS

Steinmeier will run against Merkel in poll

Social Democrats tap the foreign minister as challenges grow

By Marcus Walker

BERLIN—Faced with crumbling support and a growing challenge from the far left, Germany's Social Democrat party nominated foreign minister Frank-Walter Steinmeier to lead the party into national elections next year.

Sunday's nomination effectively launches Germany's election campaign with a year to go until the Sept. 2009 poll, pitting Mr. Steinmeier against Chancellor Angela Merkel. That rivalry, say analysts, could add to the paralysis in Germany's already-fractious coalition government, where the Social Democrats are junior partners to Ms. Merkel's conservatives.

Like center-left parties in Britain and France, Germany's Social Democrats are in deep trouble as they compete with conservatives for the center ground on economic policy while at the same time trying to hold on to voters who feel Europe's mainstream leftist parties have abandoned their roots.

Wooing those voters back could prove difficult for the 52-year-old Mr. Steinmeier, who until 2005 was chief of staff to then-chancellor Gerhard Schröder. Many voters and party rank and file haven't forgiven Mr. Schröder's Social Democrat government for cutting back Germany's generous welfare state while in office and want to roll at least some of the changes back. Mr. Steinmeier helped design Mr. Schröder's policy.

A meeting of Social Democrat leaders on Sunday also replaced party chairman Kurt Beck, who has moved the party to the left in the past two years but was unable to unite it. The new party chairman will be Franz Müntefering, another Schröder-era veteran and leading moderate.

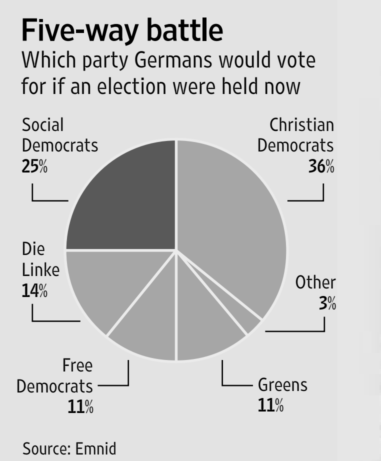
Mr. Steinmeier told reporters Sunday his party had to end its internal faction fighting. "We need to stand together now," he said.

German voters give Mr. Steinmeier high personal approval ratings. But he has mostly kept out of the rough and tumble of domestic-policy arguments and has never before run for public office. Although an experienced technocrat, he lacks the charisma of past Social Democrat election winners such as Mr. Schröder and Willy Brandt.

Mr. Brandt was the closest thing the Social Democrats ever had to a John F. Kennedy. He managed to unite the West German left in the early 1970s, when it was as divided as today amid generational conflict and a protest movement fueled by the U.S. war in Vietnam. But Mr. Steinmeier is no Willy Brandt, says German historian Manfred Görtemaker.

"Steinmeier has no chance" of reuniting the German left and little chance of winning next year's election, Mr. Görtemaker said. "He is a competent, pragmatic man, but he has no charisma and he isn't popular with left-wingers."

Germany's Social Democrats face a particularly strong challenge from the hardline leftist party Die Linke (German for 'The Left'), an alliance of former East German Communists, discontented West German trade unionists and ex-Social Democrats. Die Linke has eaten into the Social Democrats' voter base with a populist promise of pacifism abroad and anticapitalism at home. Opinion polls say about 14% of the German electorate would now vote for Die Linke, up from 9% at the last elections in 2005. Many of their supporters are former Social Democrat voters.



Frank-Walter Steinmeier, designated chancellor candidate and deputy chairman of the German Social Democratic Party

Ms. Merkel has added to the Social Democrats' woes by shifting to the left herself on economic policy, dropping her former free-market zeal after it proved a vote loser. After campaigning in opposition to deepen Mr. Schröder's economic reforms, she has even watered parts of them down in office.

Mr. Steinmeier is expected to lead a centrist campaign with themes including investing in education and renewable energy and challenging Ms. Merkel for the middle ground. But Social Democrats also are likely to push for more redistribution, via minimum wages, heavier taxes on the rich and lower social-security levies for average households.

Germany's economy, the biggest in Europe, is teetering on the brink of recession, threatening to add to voters' discontent with rising food and energy prices, stagnant incomes and years of welfare cutbacks. That is eroding support for both of Germany's traditionally dominant parties, Mr. Steinmeier's Social Democrats and Ms. Merkel's Christian Democrats.

The two parties together used to enjoy the support of over 80% of German voters. Opinion polls currently put the Christian Democrats on about 36% and the Social Democrats on only 25%. Ms. Merkel has strong personal-approval ratings, but her party is short of the roughly 40% voter support she would need to govern without the Social Democrats.

The question of whether to support American military interventions around the world has also tested the unity of Europe's left. Though Mr. Steinmeier, like Mr. Schröder, opposed the U.S.-led invasion of Iraq, he supports Germany's continued involvement in NATO operations in Afghanistan. That mission is widely unpopular with German voters.

Die Linke's figurehead, firebrand ex-Social Democrat Oskar Lafontaine, wants to pull German troops out of Afghanistan and reverse the free-market changes Germany made under Mr. Schröder. An opinion poll last week put Die Linke ahead of the Social Democrats in a Western German state for the first time—albeit in Mr. Lafontaine's home state of Saarland. Die Linke is already more popular than the Social Democrats in Germany's former Communist East.

"Die Linke under Lafontaine is telling some of our voters everything they want to hear," said Johannes Kahrs, a leading member of the Social Democrats' moderate wing, which defends the party's pragmatic policies of recent years. "We need to convince voters that Die Linke might make them feel warm and fuzzy inside, but we appeal to their brains." Messrs. Steinmeier and Müntefering will make a good team, he said.

According to economists, Mr. Schroder's welfare cutbacks worked: Unemployment is down to 7.6% from its peak of over 12% in 2005, and economic growth picked up strongly until the global economic downturn reached Germany this spring. But the strategy, which included deep cuts to unemployment benefits, split the Social Democrats. Defectors including Mr. Lafontaine accused the party of betraying its principles.

The Social Democrats' left wing wants to return to traditional policies of boosting workers' rights and state welfare support to win back voters. Many party traditionalists also want to ally with Die Linke, fearing that otherwise the Social Democrats will be condemned to remain, at best, junior partners in governments led by Ms. Merkel.

Mixed U.S. economic data show a changing business cycle

By Jon Hilsenrath
And Kelly Evans

The U.S. economy looks like it is traveling along two tracks.

If you look at output—the amount of goods and services Americans produce— the economy has been rising at a decent clip. But people aren't feeling it in their wallets because the factors driving their own incomes—such as jobs and wages—are under strain.

THE OUTLOOK

The point has been underscored by a slew of economic reports released in the past few weeks. The government's measure of inflation-adjusted gross domestic product expanded at a surprisingly robust 3.3% annual rate in the second quarter. Exports were a big driver, in particular exports of industrial supplies and capital goods.

Yet employment has fallen for eight straight months by a cumulative 605,000 jobs. Some 45% of the losses have been in manufacturing. You might expect manufacturing employment to hold up better during an export boom. But it isn't.

With job losses mounting, companies are cutting back on hours and getting tough on wages. Year-to-year personal income growth has slowed from more than 7% a couple of years ago to a little more than 4% in July, not enough to keep up with inflation.

In theory, output and income should go up and down together. If the economy is still expanding, why are so many households being squeezed?

One answer is that the business cycle itself is changing. Recessions in the past used to follow a predictable script. Business would slow or inventories would go up too much and catch companies flat-footed. As their own productivity dropped, they would belatedly respond by cutting back on workers. Then, as the process fed on itself, everything would go down together—output, employment, income and productivity.

The 2001 recession changed the script—productivity held up surprisingly well throughout. Companies cut back ahead of the business slowdown and kept doing it even after demand started rising again. The productivity they managed to squeeze out of existing workers bolstered output, even as it strained households.

The same thing seems to be happening again: To the surprise of many economists, worker productivity is rising, not falling.

"There seems to be a change in how businesses operate," says Dean Maki, economist for Barclays Capital. With better technology, businesses get ahead of inventory buildups or demand slowdowns more quickly. The declining influence of unions is also putting management in a position to fire workers more quickly.

The result: While incomes are getting squeezed, the output per hour of workers was up at an annual rate of more than 3% in the first half of the year—the best performance since early 2004.

More than ever, it seems, this puts the brunt of a downturn on workers. But there are important upsides to the shift. Better productivity helps bolster corporate profits, so while the stock market is weak it hasn't collapsed as have stock markets elsewhere in the world this year. It also helps restrain inflation and give the Federal Reserve leeway to keep interest rates low and help the economy heal.

It also makes it harder to read a business cycle. The collection of economists at the National Bureau of Economic Research who date recessions debated for months about the beginning and end of the last downturn because of the striking disconnect between output and income.

"If you dated it based on the labor market you'd have it be one of the longest recessions in history, and that didn't feel right," says Christina Romer, an economics professor at the University of California, Berkeley. The group finally decided November 2001—when output growth restarted—was the point at which the recession ended, making the eight-month slowdown one of the shortest on record.

But the debate hasn't gone away. "What matters to individuals more than anything else is the behavior of the labor market," says John Lonski, chief economist at Moody's Investor Service. "If I were the NBER I would simplify the entire process and focus on the labor market. From the perspective of the economy and social welfare it's labor-market behavior that matters the most."

There are other factors at play now, including confusion about how statisticians measure all of these trends. Some economists are skeptical of the 3.3% annualized increase in gross-domestic-product growth registered in the second quarter. The figure, produced by the government's Bureau of Economic Analysis, is out of line with another BEA figure called gross domestic income—a measure of the income earned by businesses and households.

In theory, the two figures should go up and down together. But gross domestic income expanded at a much smaller 1.9% annual rate in the second quarter, after contracting the two previous quarters. The income number might have been skewed as government statisticians try to make sense of the massive write-offs being recorded by banks. The output number might also have been skewed, for instance by big shifts in the trade environment and the price of oil. Data revisions could ultimately show output wasn't as strong as it now appears.

Statistics aside, it is also possible output won't hold up under the pressures building against the U.S. economy, even with better productivity. Exports have been the bright light in the growth picture. But the global economy is slowing.

Neil Soss, a Credit Suisse economist, notes that three quarters of the economy's growth in the past year came from an improved trade position. "How much can I count on that for the future?" he asks.

Meantime, the strain on incomes might finally be catching up to households. They will clearly be helped by the drop in gasoline prices, but tax rebates have run their course and the housing and credit squeezes run unabated.

Adjusted for inflation, consumer spending—the biggest driving force of growth—contracted in June and July. It hasn't contracted for an entire quarter since late 1991. That 17-year run is now being put to the test. If consumers crack, output and income might finally meet up again—in recession.

CORPORATE NEWS

TELECOMMUNICATIONS

Grameen suit of Telenor is a 'remote possibility'


Associated Press

NOBEL PEACE laureate Muhammad Yunus of Bangladesh said Friday that it was only a "remote possibility" that his **Grameen Telecom** would need to take legal action against Norwegian telecom operator **Telenor** ASA.

The remarks from Mr. Yunus followed his warning late Thursday that Grameen Telecom might file suit against Telenor in a dispute over their co-owned Bangladesh mobile-phone operator Grameenphone. "This is not an outcome that we think is necessary," Mr. Yunus said. "It is a possibility, a remote possibility." Telenor controls Grameenphone, Bangladesh's biggest mobile operator, with a 62% stake. Grameen Telecom owns the rest.

RUSSIA

AiRUnion to be rescued through holding company

RUSSIA said Friday it will create a state-controlled airline holding company as big as leader **Aeroflot** OAO in order to rescue the cash-strapped **AiRUnion** OOO airlines alliance.

The new holding will be controlled by **Russian Technologies**, a state-owned conglomerate crafted under former President Vladimir Putin. AiRUnion last month fell behind on payments for jet fuel, grounding aircraft and stranding thousands at airports across Russia. Russian Technologies said it would take at least nine months to create the holding company. Russia has been supplying the air alliance with state-owned fuel to help it fly passengers home. *—Reuters*

AUTOS

Honda may fail to reach lower Europe sales target


Honda

HONDA Motor Co. Senior Managing Director Shigeru Takagi cast doubt on the company's ability to reach its recently revised European sales target for this fiscal year.

Its warning comes a month after Honda cut its sales outlook for Europe to 455,000 vehicles from its initial 470,000 for the year through March. For Japanese car makers, Europe is becoming a growing headache as slumping auto demand there, on top of already flagging sales in the U.S. and Japan, makes global sales targets increasingly difficult to achieve. Europe accounts for about 10% of Honda's sales.

—Yoshio Takahashi

Ford seeks U.S. fit for Europe cars

Smaller-auto push is about 'survival'; bumper-design woes

BY MATTHEW DOLAN
Lommel, Belgium

CHIEF EXECUTIVE Alan Mulally is hoping to revive **Ford Motor** Co. by bringing European small cars to the U.S. market, and success may hinge on a rather mundane component: the front bumper.

The Dearborn, Mich., auto maker posted a loss of $8.7 billion in the second quarter and is scrambling to react to this year's rise in gasoline prices and the consumer shift to small cars and away from trucks and sport-utility vehicles—which together generate most of the company's revenue in North America.

In July, Mr. Mulally announced an effort to retool three North American truck plants so they can make at least six vehicles Ford now builds and sells in Europe.

To make European cars comply with U.S. safety regulations and insurance standards, Ford will have to add some potentially costly parts and steel reinforcements. If the work isn't done carefully, the vehicles could become too expensive for Ford to make money on them in the U.S., or too heavy to deliver the kind of gas mileage Americans crave.

Ford's rush to tailor its European cars for the U.S. market "is about our survival," said Jim Farley, Ford's global sales and marketing vice president, who was in Europe late last week for the launch of the Ford Fiesta, a new subcompact. Originally designed for Europe and Asia, it has been reworked for North America and will arrive in U.S. showrooms in the first half of 2010.

Mr. Farley believes selling the car in all markets will help Ford's bottom line. "The key is that we'll be able to sell these cars in great volume on a global scale," he said.

Mr. Mulally's bid to bring to the U.S. market cars that Ford originally designed for Europe is a risk. Ford, like its Detroit rivals **General Motors** Corp. and **Chrysler** LLC, has a strong name among truck buyers but it faces an uphill battle in passenger cars against the likes of **Toyota Motor** Corp. and **Honda Motor** Co.


Ford

Ford late last week unveiled the **Ford Fiesta**, a new subcompact originally designed for Europe and Asia. It will arrive in U.S. showrooms in the first half of 2010.

If gas prices continue to fall, demand for small cars could ease, making it harder for Ford to hit the sufficient sales volumes.

And even if Ford's European models take off in the U.S., it is unclear how much profit they will generate. A car maker's profit margin on cars can be a few hundred dollars, and often the Big Three lose money on each small car they sell. Any profit they make probably won't offset declining truck sales. Each full-size pickup and SUV Detroit sells generally generates about $8,000 in pretax profit.

Mr. Farley said he believes that U.S. customers who are used to buying larger vehicles are willing to pay extra to get good-looking small cars loaded with optional features. If that is the case, it could make it easier for Ford to earn a profit on passenger cars—a segment where Detroit has often lost money in the past.

Ford plans to spend $3 billion to overhaul three truck plants so they can make small cars, including the Fiesta for the North American market, and a new version of the Focus compact, its smallest model.

Ford has tried to bring European cars to the U.S., and had limited success, often because the vehicles had been stripped down to save costs. In the 1980s, the Mercury Merkur, a sports car Ford made in Germany, failed to take off. Years later, Ford spent billions to introduce the Ford Contour and Mercury Mystique, both based on European designs. They were beset by early recalls, competition from its own Taurus sedan and tepid reviews.

"We didn't spend any time to find out the unique needs of the

Rising gas prices have left few options but to modify European models for the U.S.

American market," said Andreas Ostendorf, Ford's chief vehicle engineer in Europe who worked on the Contour program.

Ford is beginning to develop new cars from the ground up to be built and sold anywhere in the world. Rising gas prices have left Ford few other options but to modify European models for the U.S. market. With Americans flocking to cars, Ford's U.S. vehicle sales are down 15% this year, and sales of its F-150 pickup truck, its franchise product, are off 20%.

Bumpers present one of the biggest challenges on the safety front. European regulations require auto makers to design bumpers that cause minimal injury to pedestrians. U.S. bumpers are much heavier to withstand direct impacts and front-end collisions against a solid barrier or a large vehicle, like a truck or SUV.

Steve Kozak, one of Ford's top safety engineers, said the company is designing new U.S. bumpers for the European compacts and midsize models Ford aims to start assembling in North American plants next year. It is the single most-expensive adaptation, he said.

"There is far more emphasis, especially with insurance companies, on low-speed damage from a frontal collision," said Mr. Kozak, who dispatched a team of safety engineers to Germany from the U.S. 20 months ago to modify European designs to meet U.S. requirements. "You can't find an F-150 [truck] in Europe so the requirements there don't have those collisions in mind."

At Ford's test track in Lommel, Belgium, Gunnar Herrmann, executive director of Ford's next-generation Focus car programs, pointed to the front end of the company's new Fiesta to show the placement of a prominent bar across the grille designed to protect pedestrians.

That crossbar would be removed when the Fiesta arrives in the U.S. market in 2010, he said, replaced by a new structure hidden behind the grille and designed to withstand a high-speed, full-frontal impact with another car or truck.

Other safety modifications include larger, dual-stage air bags because federal safety standards demand vehicles also protect unbelted passengers. Mr. Herrmann said the safety belts will also be different because the U.S. versions need to account for higher-speed crashes.

Ford engineers and designers also need to make modifications to appeal to U.S. consumer tastes. They plan on outfitting the U.S. cars with a spare tire—European use an inflatable one—and a more powerful air-conditioning system because U.S. occupants expect their cars to cool down more rapidly than Europeans, according to Marin Burela, who help leads Fiesta's global product development.

Compacts drive monthly sales at BMW, Daimler

BY CHRISTOPH RAUWALD

FRANKFURT—**BMW** AG and **Daimler** AG's Mercedes-Benz Cars unit both posted rising sales for their compact brands in August, though their core larger cars experienced lackluster demand.

The consumer shift toward smaller cars, which are usually less profitable than large vehicles, comes amid sluggish demand in major markets such as the U.S. and Western Europe and a gloomy economic outlook, which are increasingly clouding the perspectives for global car makers.

Total sales at Mercedes-Benz fell 12% in August from a year earlier to 84,400 vehicles as improved sales of the Smart two-seater failed to offset a 16% decrease at the core Mercedes-Benz brand to 75,200 cars. Sales of the Smart minicar rose 29% to 9,200 vehicles.

BMW eked out a 2% sales rise to 101,673 cars, driven by strong demand for the compact Mini brand as well as growth in Asia and Eastern Europe. Sales of the Mini rose 11% to 16,257 vehicles, but sales at the core BMW brand were virtually flat at 85,315 cars.

In the U.S., BMW's biggest market, sales of the core BMW brand fell 4% to 25,462 cars.

The decline came "in stark contrast" to BMW's customer incentives, which increased sharply in August and in the first eight months of the year, Citigroup analyst Kristina Church wrote in a note to clients. BMW's incentive level is almost twice as high as the one at German rival Mercedes-Benz, she said.

Last month, BMW said it is adjusting its U.S. strategy to focus on profitability rather than sales volume, after its first-half earnings were hit by higher risk provisions and allowances for residual-value risks and bad debts relating to its financial-services business. These factors shaved €695 million ($989 million) off earnings in the first six months of the year.

"The difficult economic conditions on the global automobile markets remain a major challenge," BMW executive-board member Ian Robertson said Friday.

CORPORATE NEWS

DAILY SHARE PRICE

Nokia

On the Helsinki Stock Exchange
Friday's close: **€14.20, down 9.6%**
Year-to-date change: **down 46%**

Source: Thomson Reuters Datastream

Alitalia gets turnaround experts

Piaggio executives to run firm created to overhaul airline

By Luca Di Leo And Liam Moloney

MILAN—The overhaul of Italian airline **Alitalia** SpA gathered momentum Friday as the company created to take over the airline's viable assets named two turnaround experts to run it.

The two executives come from Italian scooter maker **Piaggio** SpA. Chairman and Chief Executive Roberto Colaninno will become chairman of Cia. Aerea Italiana, or CAI. His right-hand man, Rocco Sabelli, will become chief executive of the company, formed last month by 16 Italian investors.

CAI investors, which count the Benetton family and **Intesa Sanpaolo** SpA, one of Italy's largest banks, as the largest shareholders, will hope the pair can repeat their track record at Piaggio. There, under Mr. Colaninno's guidance, Mr. Sabelli cut costs, weeded out unprofitable scooter models and worked with labor unions to restructure the company.

Analysts caution that managing a group of 16 investors will prove difficult and that both businessmen lack experience in running an airline.

"It takes an understanding of networks, of the airport business, of marketing," said Carlo Scarpa, professor of Industrial Economy at the University of Brescia.

Last week CAI offered to buy a large part of Alitalia's viable assets after the airline filed for bankruptcy. As part of the government-sponsored rescue plan, Alitalia's €1.2 billion ($1.7 billion) debt and its liabilities will be split off.

CAI's investors Friday also approved the acquisition of AP Holding, which owns Air One SpA, Italy's No. 2 airline by passengers.

Augusto Fantozzi, the government-appointed commissioner overseeing Alitalia's bankruptcy, said an international partner would be identified by the end of the month. **Air France-KLM** and **Deutsche Lufthansa** AG are seen as the leading contenders to buy a stake in Alitalia.

Nokia trims back previous outlook on market share

By Adam Ewing

Nokia Corp., the world's largest mobile-phone maker, reduced its market-share outlook, causing investors already skittish about a lackluster global economy to send the company's shares sharply lower.

The Finland-based cellphone maker blamed the gloomy news on a weaker economy world-wide and a decision to stay out of a handset price war. It said it now expects its third-quarter market share to be lower than initially signaled in July, when it predicted market share of 40%, unchanged from the previous quarter. It still targets an increase in its 2008 market share.

Friday's warning is the latest sign of the combined impact of spreading economic gloom and fierce price competition between mobile companies.

Nokia rival Sony Ericsson, a joint venture between Japan's **Sony** Corp. and Sweden's **Telefon AB L.M. Ericsson**, barely broke even in the second quarter as average selling prices fell sharply. It has issued two profit warnings this year.

Meanwhile, Europe's largest mobile operator, **Vodafone Group** PLC, spooked the market in July with poor quarterly results and a wavering full-year outlook that sent its shares sharply lower. At the time, Vodafone cited difficult conditions in important markets including Spain and Turkey, as well as rising costs.

Nokia shares fell 9.6% in Helsinki trading Friday to end at €14.20 ($20.21) each, a near three-year low.

Nokia said the overall mobile-phone sector is being hit by weaker consumer confidence in several markets. Still, Nokia said it expects total unit sales of mobile devices to rise by 10% or more this year, lifted by sales in emerging markets.

Research firm Gartner Inc. said late last month that it expects 11% unit growth in handset sales in 2008, but revenue growth of just 9% as competition and the economic slowdown weigh down average selling prices.

Gartner's research director for mobile devices, Carolina Milanesi, said both South Korea's **Samsung Electronics** and Sony Ericsson made price cuts in Asia during the past month, and Samsung is also aggressively going after the European market.

Samsung's cellphone division had an operating-profit margin of 13% in the second quarter, up from 7.8% a year earlier, but below the first quarter's 16% margin. Samsung executives said the company boosted marketing expenses sharply in the period.

—Ian Edmondson contributed to this article.

CORPORATE NEWS

Boeing machinists strike

Last-minute talks fail to reach pact; more 787 troubles?

By J. Lynn Lunsford

Boeing machinists marched from the company's Renton, Wash., factory to their union hall to vote on Boeing's final contract offer Sept. 3.

SEATTLE—**Boeing** Co.'s machinists walked out on strike Saturday after their union was unable to reach an agreement with company officials during last-minute negotiations on a new contract.

Members of the 26,800-member Seattle-area International Machinists and Aerospace Workers voted overwhelmingly to strike, unhappy with proposed pay raises, health-care costs and what it calls a lack of guaranteed job security. But the machinists union delayed a walkout for 48 hours after a U.S. mediator asked the two sides to continue talking. The continued negotiations failed, however, setting the stage for the union's second walkout since 2005.

In an email to employees, Boeing Commercial Airplanes President Scott Carson said the company was "deeply disappointed" that the two sides had been unable to reach an agreement during talks that were held at a Walt Disney Co. resort in Florida following the strike vote Wednesday.

With Boeing's factories running at peak capacity to keep up with strong demand for new jetliners from airlines seeking fuel-efficient planes, a strike is expected to cost the company roughly $100 million a day in lost revenue.

Boeing's 787 Dreamliner, which is already running nearly two years behind schedule, will likely slip even further, putting the company in even hotter water with customers who have ordered nearly 900 of the ground-breaking jetliners as replacements for aging long-haul planes.

Depending on its length, a strike could also affect Boeing's suppliers world-wide, particularly those who rely on it for a large part of their business. In some cases, suppliers will be able to take advantage of the down-time to build up inventory or catch up with what has been a hectic few months in the jet-making industry.

The company's final contract proposal included a pay raise of 11% over the life of the contract, as well as a boosting of pensions by 14% to $80 a month for each year of service. Under the proposed contract, the average union member would earn roughly $65,000 a year before overtime that averages $10,000 a year or more.

The union said it wanted pay raises of at least 13% and a larger pension amount. It also wants Boeing to abandon plans to have workers take on a greater share of health-care costs.

Europe's budget airlines post gains but face woes

By Kaveri Niththyananthan

Thrifty consumers lifted European budget airlines like **easyJet** in August.

European budget airlines prevailed in an unusually quiet August booking period as travelers turned to less-expensive carriers for their summer getaways.

Waning consumer spending has taken its toll on European airlines, which saw their profits battered by rising oil prices and declining demand for air travel. Even benefits from the recent drops in oil prices are now being wiped out by the strengthening dollar, as fuel is priced mainly in dollars.

Consumers pinched by the weakening economy who aren't willing to give up travel altogether are choosing less-expensive short-haul destinations over long-distance flights. On Friday, **easyJet** PLC said it carried about 24% more passengers last month than a year earlier, bringing its August passenger number to 4.6 million from 3.7 million. Its load factor—a measure of how full an airline's planes are—rose to 91.3% from 87.4%.

Aer Lingus PLC meanwhile posted an 8.8% rise in passenger numbers to one million. The Irish flag carrier saw an 11% increase in passengers on its short-haul flights to 900,000 as capacity was up 15.4%. However, more expensive long-haul flights fell 2.3% to 120,000.

On Thursday, Europe's largest budget carrier, **Ryanair Holding** PLC, had already reported a 19% increase in passenger numbers, although its load factor edged down to 90% from 91% in August because of increased capacity.

Yet, analysts doubt the growth is sustainable. As the typically weaker winter period approaches, demand is set to decline. Many airlines, including **British Airways** PLC and Ryanair, have already announced capacity cuts for the winter to help prop up profits.

Unlike other European budget carriers, the Scandinavian carrier **SAS** AB said its traffic had fallen 0.7% and that passenger numbers were down 4.7% to 3.3 million. However, it said fuel surcharges will help offset the decline.

Another victim of consumers tightening their belts was British Airways, which last week highlighted that currency movements had eliminated the benefits from lower oil prices. Oil prices have dropped from the $147-a-barrel peaks seen in July to about $106.

BA also said the outlook for its lucrative premium business, where it makes most of its profit, was uncertain as it reported a 1.6% decline in total traffic for August and a 3.2% fall in passenger numbers.

GDF Suez chases gas assets in talks with Dutch company

By Adam Mitchell

French utility **GDF Suez** SA said Friday that it was in exclusive talks to buy a package of gas assets in the Netherlands for €1.08 billion ($1.54 billion)—a step toward achieving its medium-term objective of having 1.5 billion barrels of oil equivalent of proven and probable reserves.

The assets, owned by Nederlandse Aardolie Maatschappij BV, include working interests of between 30% and 60% in five producing fields, as well as potential for exploring and boosting volumes, said both GDF Suez and NAM. The interests produce about 3.3 million barrels of oil equivalent a year, they said.

A stake in the Dutch section of the A6-F3 pipeline, which transports gas from the German North Sea to the Nogat pipeline system, and a 30% stake in **Nogat** BV—the operator of the pipeline—are also part of the package.

NAM is the largest exploration and production company in the Netherlands and is owned by **Royal Dutch Shell** PLC and **Exxon Mobil** Corp.

"With this acquisition, GDF Suez reinforces its strong position in the Netherlands and becomes the largest exploration and production operator in the Dutch sector of the North Sea," said Jean-Marie Dauger, executive vice president in charge of GDF Suez's global gas division.

The news underscores that exploration and production are "more and more important" for GDF Suez, said Société Générale analyst John Honoré.

GDF Suez, which was formed this summer through the merger of French state-controlled utility company Gaz de France with utility Suez, plans capital expenditures of €30 billion until 2010. Since making its stock-market debut July 22, the unified company has unveiled a flurry of investments.

Thursday, GDF Suez announced the acquisition of a 15% stake in an offshore exploration and production license in Azerbaijan. If an exploration phase to run through 2011 is successful, GDF Suez said it could boost its reserves by approximately 35 million barrels. At the end of last year, GDF Suez had proven and probable reserves of 667 million barrels, said a spokeswoman.

Dell shifts business mode

PC maker will sell factories to cut costs in changing market

By Justin Scheck

Dell Inc. is trying to sell its computer factories around the world, moving to sharply overhaul a production model that was long a hallmark of the PC giant's strategy.

In recent months, according to people familiar with the matter, Dell has approached contract computer manufacturers with offers to sell the plants. One person briefed on the plan said he expects the company to sell most—and possibly all—of its factories "within the next 18 months." Other factories could close, this person said. Dell would enter into agreements with the contract manufacturers to produce its PCs.

The plan is the latest sign of changes in the global PC business, and the increasing pressure on Dell to improve its profitability. The Round Rock, Texas, company last month reported disappointing quarterly profit that helped send shares down more than 18% and has been trying to reduce expenses since early last year. Dell, which led the industry in lean manufacturing approaches and build-to-order PCs, now finds itself lagging behind its rivals in wringing savings by outsourcing operations to production partners.

Bloomberg News/Landov

Michael Dell, chairman of Dell, at a conference in Idaho earlier this year

The most likely candidates to buy the factories are big contract manufacturers—most of which are based in Asia—that may hope to get a bigger piece of Dell's business. A company that purchases a Dell factory would likely be contracted to continue making computers there for Dell, a person with knowledge of the talks said.

Dell's factories had been tailored for a market was driven by corporate customers ordering large volumes of desktop computers. But over the past three years, growth has shifted to laptops sold to consumers at retail stores. Dell has lagged behind competitors in coming up with a streamlined system to build portable PCs.

A Dell spokesman referred to a filing with the Securities and Exchange Commission earlier this year that said Dell is "continuing to expand our use of original design manufacturing partnerships and manufacturing outsourcing relationships."

Dell could face several obstacles to selling its plants. Contract manufacturers may be hesitant to buy factories in places with high labor costs, like the U.S., a person with knowledge of the talks said. And some facilities could be encumbered by agreements with local governments. Dell's North Carolina plant, for example, received several million dollars of state and local tax incentives that are contingent on the factory meeting certain employment and local-investment goals by 2015.

Michael Dell, the company's founder, drove an innovative strategy of selling computers directly to customers, only building them after they were ordered. The system eliminated idle inventory and maximized Dell's cash flow. The company owns factories in Texas, Tennessee, North Carolina, Florida, Ireland, India, China, Brazil, Malaysia and Lodz, Poland.

Dell's plants are still regarded as efficient at churning out desktop PCs. But within the industry, company-owned factories aren't considered the least expensive way to produce laptops. Rivals such as **Hewlett-Packard** Co. years ago shifted to contract manufacturers to build their portable computers. H-P builds "less than half" of its PCs in facilities it owns, according to Tony Prophet, H-P's senior vice president for PC supply chain.

Gene-research institute to get $400 million gift

By Keith J. Winstein

Philanthropists Eli and Edythe Broad said they plan to give $400 million more to a genetics-research center named for them, establishing an endowment aimed at enabling the organization to continue its work indefinitely.

The Broad Institute, which will receive the gift, was established in 2003 and has already received $200 million from the Broads to find the links between genes and complex diseases, such as cancer. At a news conference Thursday, Mr. Broad, a former real-estate and insurance executive, called the institute his most successful philanthropic venture.

Eli Broad

Jointly governed by Harvard University and the Massachusetts Institute of Technology, the institute has 1,200 researchers linked to the universities and another Cambridge, Mass., scientific organization, the Whitehead Institute for Biomedical Research.

The Broads' initial gifts are being used to finance research for a 10-year period ending about 2014. The additional funds will be used to earn investment income to keep the institute running.

Four years into the venture, the institute has become a powerhouse in the field of genomics—essentially focusing on human genes mapped by a government-funded project that was completed in 2003.

The new funds "will further ignite the imaginations of young people across this community," said Eric S. Lander, the institute's director, saying a permanent endowment would give the institute "the ability to think for the long term."

As part of the arrangement, the Broad Institute will become an independent nonprofit entity, jointly governed by MIT and Harvard. Previously, its finances had been administered by MIT. A spokeswoman said the institute hadn't yet decided how to manage its endowment.

Craig Venter, whose genome research competed with the government-funded effort in the late 1990s, said, "Eli Broad's doing a wonderful thing for science." Dr. Venter currently directs the J. Craig Venter Institute, a big nonprofit genome-research group in Rockville, Md.

Susan Hockfield, MIT's president, said the Broad Institute was an experiment in "problem-based research," working on projects aimed at answering specific questions, instead of the traditional approach of having individual researchers explore science broadly without a target in sight.

CORPORATE NEWS

Altria is in talks to buy UST for over $10 billion

Purchase would give the firm a foothold in smokeless tobacco

By Lauren Etter, Matthew Karnitschnig And Anjali Cordeiro

Altria Group Inc., the largest U.S. cigarette maker, is in talks to acquire **UST** Inc., the nation's largest smokeless-tobacco maker, for more than $10 billion, according to people familiar with the matter.

The timing of any deal is unclear, but those involved said it could be reached as soon as this week. UST's stock surged 25% Friday on news of a potential deal. Spokesmen for both companies declined to comment.

A completed purchase would give Altria a strong foothold in smokeless tobacco, a growing market that could help offset steady declines in cigarette sales. A deal also would hasten consolidation in the tobacco industry, something that analysts have been expecting for months as tobacco companies try to regain muscle after years of being battered by litigation and regulatory actions.

Altria, of Richmond, Va., is the parent company of Philip Morris USA, which makes the popular Marlboro-brand cigarette. It commands a roughly 50% share of the U.S. cigarette market. UST, Stamford, Conn., is known for its premium chewing-tobacco brands, Copenhagen and Skoal. It had revenue of $1.95 billion last year.

UST would make "a very good fit with Altria," Nik Modi, an analyst at UBS, said. "Altria is a premium player as is UST."

Altria has been rumored to be shopping ever since the March sale of its international business, **Philip Morris International** Inc., which freed up resources to pursue acquisitions. Faced with the slow decline in cigarette consumption in the U.S., Philip Morris USA and top competitor **Reynolds American** Inc., of Winston-Salem, N.C., have been expanding into smokeless tobacco and other products that can deliver a nicotine fix to smokers.

In 2006, Reynolds American acquired Conwood Co., a discount smokeless-tobacco provider, for $3.5 billion. Since that acquisition, Conwood has been encroaching on UST's turf as consumers, pinched by a weakening economy, migrate toward its popular Grizzly-brand product, which has a lower price point.

So far, Philip Morris USA's push into smokeless products has generated limited success. In January, it withdrew its spit-free Taboka Tobaccopaks product from the market and replaced it with a similar, Marlboro-branded product that is in testing. It has also been testing Marlboro Moist Smokeless Tobacco, sometimes known as "Marlboro in a can," but at times has had to lower its pricing on that product to move it off shelves.

By linking with UST, Philip Morris USA could accelerate its growth in the smokeless market and create stronger competition for Reynolds American."This is an area that makes sense for Altria," said Standard & Poor's equity analyst Esther Kwon. "This area is much more profitable than the cigarette business."

U.S. cigarette sales have been declining about 3% to 4% a year, while smokeless-tobacco sales have been increasing about 6% to 7% a year, according to Judy Hong, an analyst at Goldman Sachs.

Part of this shift is happening as cities across the country move to ban indoor smoking in public establishments, pushing smokers to seek alternatives to cigarettes.

NOL reduces its valuation of Hapag by about $2 billion

By Costas Paris

SINGAPORE—**Neptune Orient Lines** Ltd. has cut its valuation of German container shipper Hapag-Lloyd to between $4 billion and $5 billion from $6 billion to $7 billion when the acquisition was first mooted in June, people familiar with the matter said Friday.

NOL began exploring a purchase of the German company earlier this year and was expected to pay as much as $7 billion. While a tie-up continues to make strategic sense, the world economic slowdown has clouded the shipping industry's prospects.

"NOL's second-quarter profit was less than expected; there are fewer containers going to North America, marine-fuel prices are up and Asia-Europe freight prices are still down. In this kind of environment, the original thought of offering a total of up to $7 billion is out of the question," one person said. "Around $4 billion is logical and $5 billion is a premium which NOL could consider. Anything beyond that, NOL will probably walk out."

A second person said that NOL will make the offer by early October, with **TUI** AG, Hapag-Lloyd's parent, likely to decide the winner toward the end of that month.

NOL, which is 66%-owned by **Temasek Holdings** Pte. Ltd., is among two bidders short-listed for Hapag-Lloyd. The other is a City of Hamburg-led consortium of investors.

NOL and Temasek, Singapore's state-owned investment company, declined to comment on the revised offer.

A spokesman for TUI confirmed that a sale decision would be made in the autumn but said the company wouldn't comment on any offer price from NOL.

—P.R. Venkat and John Jannarone in Singapore and Kirsten Bienk in Frankfurt contributed to this article.

GLOBAL BUSINESS BRIEFS

RWE AG

Firm sells its 50% stake in Tarragona to Iberdrola

RWE AG said it sold a 50% stake in Spanish power generator **Tarragona Power** SL to **Iberdrola** SA, marking the German utility's exit from the Spanish thermal-power market. RWE's sales and network unit RWE Energy said Iberdrola's generation company Iberdrola Generación will fully take over Tarragona. The companies didn't disclose financial details of the deal. Tarragona Power was a 50-50 joint venture between RWE and Iberdrola and operates a gas-fired, combined-cycle plant with a capacity of 417 megawatts and additional facilities to supply electricity and steam to a chemical plant nearby. RWE, Germany's largest power producer by generation capacity, has repeatedly said it intends to focus on renewable energies in Spain, but thermal power isn't part of its strategy in that market.

Xstrata PLC

Xstrata PLC moved to block the 545 million Australian dollar (US$443 million) takeover of Indophil Resources NL by the Stanhill consortium, paying A$82 million for a block of shares that boosts its holding to about 19.9%. Stanhill's offer is conditional on the consortium, led by Hong Kong-based **Crosby Capital** Ltd., winning 90% of the shares, although the consortium Friday said it is willing to review this condition. But for now, Xstrata's intervention created uncertainty that the board-recommended takeover will proceed, and Indophil's shares slid 36% to 76.5 Australian cents Friday. Indophil is Xstrata's junior partner in the giant, undeveloped Tampakan copper and gold deposit in the Philippines.

HMV Group PLC

Music, DVD, games and book retailer **HMV Group** PLC said sales are growing at a much slower pace amid worries about the economy. HMV said that like-for-like sales across its group rose 1.3% in the 18 weeks to the end of August, versus 10% growth in the previous quarter. The group's book-retailing arm, Waterstone's, posted a 4.3% slump from a year earlier, when the final installment of the Harry Potter series boosted sales. HMV—with 371 HMV stores in five countries, and 320 Waterstone's bookstores, principally in the U.K. and Ireland—began a comprehensive review in March 2007. It seeks to save some £40 million, about $70 million, by 2010 and to transform HMV's business as it faces growing pressure from digital downloading and online retailers and supermarkets.

Alstom SA

A federal judge in the U.S. has granted class-action certification in a shareholder suit against French engineering company **Alstom** SA and its U.S. subsidiaries over alleged accounting improprieties. In an Aug. 27 order, U.S. District Judge Victor Marrero in Manhattan certified a class of shareholders who purchased the French engineering giant's then-American depositary shares in the U.S. between Aug. 3, 1999, and Aug. 6, 2003. But the judge also narrowed the class and excluded some foreign purchasers who acquired shares overseas, including French shareholders. Kevin Abikoff, a lawyer for Alstom, said the company is pleased with the ruling, in particular because of the exclusion of French shareholders. "It reduced the exposure significantly," he said.

OAO Mobile TeleSystems

Russia's top cellphone operator OAO **Mobile TeleSystems** said it signed a deal with **Apple** Inc. to sell the iPhone in Russia. MTS, which becomes the last of the country's "big three" providers to announce a distribution agreement for the handsets, didn't provide details of the deal. Friday's announcement was made less than a week after MTS's major rivals Vimpelcom OAO and MegaFon OAO said they reached similar agreements with Apple. The device hasn't gone on sale officially in Russia, but is available on the "gray market" for about $1,000, several times the current retail price in the U.S. Russia has an estimated 500,000 iPhones in use.

Telecom Italia SpA

Telecom Italia SpA could be interested in buying minor assets from broadband operator **Tiscali** SpA but isn't interested in its British operations, Chief Executive Franco Bernabe said. However, he added the sum that Telecom Italia could put on the table would be "very modest," not only because of limited resources, but also because the acquisition wouldn't be a priority. The company, which began a strategic review in April, said early this year it had received indications of interest from "important industrial operators." After missing a self-imposed June 30 deadline to find a buyer, Tiscali denied there was a new timing for the sale amid speculation it was struggling to find a buyer.

Daimler AG

German car maker **Daimler** AG and utility **RWE** AG said they would begin a joint project in the German capital testing electric cars and electricity filling stations. It is the second electric-car test project initiated by Daimler, after electric Smart cars started a trial as fleet vehicles for the police and other services in London last year. Daimler would provide more than 100 electric cars from its Mercedes-Benz and Smart brands, as well as service for the cars. RWE said it will handle the development, installation and operation of about 500 charging stations, the electricity and central control of the system. The program will begin testing at the start of next year and should be operational at the end of 2009. It is being supported by the German federal government because of its significance in terms of sustainable mobility in the future.

Nationwide Building Society

U.K. mortgage lender **Nationwide Building Society** said it is in advanced talks with the **Derbyshire & Cheshire Building Societies** over the terms of independent and proposed mergers, aimed at strengthening its position in the troubled banking sector. "Further announcements will be made once those discussions have concluded," Nationwide said in a brief statement after a report in the Sunday Telegraph newspaper. A Nationwide spokesman declined to comment further. All banks have had to write down the value of credit investment products linked to the performance of mortgages extended to borrowers in the U.S. with a poor credit history. These investments had represented a cash cow that replaced the low return banks obtained on their traditional lending.

Valartis Group AG

Swiss financial-services company **Valartis Group** AG said Friday that it acquired Anglo Irish Bank (Austria) AG from **Anglo Irish Bank** Corp. Financial details weren't disclosed. Zürcher Kantonalbank analyst Andreas Venditti estimates the purchase price is between 40 million Swiss francs and 60 million francs, or about $36 million to $54 million. Following the transaction, the Vienna-based private-banking services provider and asset manager, which holds assets valued at about two billion francs, will be renamed Valartis Bank Austria, the Swiss company said. Valartis said the acquisition substantially expands its wealth-management activities and increases the group's assets under management to a total of 5.5 billion francs. The sale of the Austrian unit is consistent with Anglo's focus on its core secured-lending businesses in Ireland.

Marubeni Corp.

A consortium led by Japan's **Marubeni** Corp. won an auction of **Senoko Power** Ltd. and will pay **Temasek Holdings** Pte. Ltd. four billion Singapore dollars (US$2.79 billion) for the generation facility, the Singapore state investment company said. The Lion Power consortium also includes France-based **GDF Suez** SA, **Japan Bank of International Cooperation**, **Kansai Electric Power** Co. and **Kyushu Electric Power** Co. "Lion Power's proposal was the most attractive in terms of price and commercial terms among a field of highly reputable investors," said Gwendel Tung, director of investment at Temasek.Senoko is the second of three Singapore generation companies to be privatized. Temasek began the process in March with the sale of Tuas Power Ltd., which China Huaneng Group bought for S$4.2 billion.

Canon Inc.

Camera and office-equipment maker **Canon** Inc. said it plans to expand production in Taiwan of SLR camera lenses 33% by building a new facility. While it declined to disclose how many lenses the new facility will make, Canon said it will invest two billion yen ($18.7 million) in the plant, which is scheduled to begin operations in July 2009. It will ship lenses manufactured in Taiwan to global markets. Canon manufactures SLR camera lenses in Taiwan, Malaysia and Japan.

Sharp Corp.

Sharp Corp. aims to sell five million mobile-phone handsets a year in China and plans to differentiate itself in the market by going after high-end customers, Masami Ohbatake, Sharp's general manager of overseas sales, said. Sharp began selling a high-end handset with a widescreen liquid-crystal-display screen in China in June, and on Friday unveiled a second, motion-sensing handset for sale in China. Mr. Ohbatake said the handset released in June took fourth place in sales among handsets in China priced at more than 4,000 yuan ($585), with 8.8% of that segment. Sharp is Japan's dominant handset manufacturer, with a 40% market share and sales of 15.5 million handsets in the fiscal year ended March 2008.

—Compiled from staff and wire service reports.

ECONOMY & POLITICS

G-7

Leading nations are set for economic slowdowns

THE OUTLOOK for the world's leading developed economies continues to weaken, the Organization for Economic Cooperation and Development said.

Its composite leading indicator in July fell 0.7 point from June to 96.2. The indicator was 5.2 points lower than in July 2007.

Indicators for all the Group of Seven leading nations fell for the month, with strong slowdowns seen in Germany, Italy, France and the U.K. Indicators point to modest slowdowns in the U.S., Japan and Canada.

Brazil, China and Russia show "signs of expansion," the OECD said. *—Emma Charlton*

SPAIN

Officials defend proposal to cut foreign work force

SPAIN'S government defended a plan to fight soaring unemployment by shutting the door on foreign workers.

Deputy Prime Minister María Teresa Fernández de la Vega said the government had to respond to the needs of the labor market. The Socialist government has been under fire since the labor minister said last week that work visas for low-skilled jobs "will get close to zero."

Labor Minister Celestino Corbacho is finalizing a separate plan to pay unemployed foreigners to go home—through lump-sum payments of their jobless benefits—with the right to come back when things get better. *—Associated Press*

GERMANY

Industrial-production fall spurs fears of a recession

FEARS of a German recession grew, as the country's Economics Ministry on Friday released data revealing a much steeper-than-expected drop in industrial production in July.

Coupled with Thursday's data showing Germany suffering its eighth-straight drop in manufacturing orders in July, economists said they see little hope for the country to avoid a contraction in the third quarter. After a 0.5% contraction in the second quarter, that would spell a technical recession for Europe's economic powerhouse, analysts said. German industrial production fell 1.8% in July from June in seasonally adjusted terms. *—By Niels C. Sorrells*

Piracy grips Gulf of Aden

Heightened attacks in key shipping lane raise insurance costs

BY CHIP CUMMINS

PIRATES HAVE stepped up attacks on merchant vessels in the Gulf of Aden, increasing insurance costs for ship owners and raising the specter of military intervention in one of the world's most important sea lanes.

The waterway lies between Yemen and Somalia and connects the Red Sea with the Indian Ocean. It is an important energy corridor, especially for Persian Gulf oil heading west through the Suez Canal. Ships laden with some 3.3 million barrels of crude—almost 4% of daily global demand—move through the waters each day, according to U.S. Department of Energy estimates. The waterway is also an important thoroughfare for goods heading to Europe and the U.S. from Asia.

The surge in piracy has suddenly turned it into one of the most dangerous passages in the world for sea captains.

"They've been just running the gauntlet" in the gulf, says Gavin Simmonds, head of international affairs for the British Chamber of Shipping, an industry trade group based in London.

Pirates have long plied the waters along the southeastern coast of Somalia, which for years has lacked a functioning central government. But this spring and summer, bands of well-trained pirates appear to have moved north into the Gulf of Aden.

The International Maritime Bureau, a marine-crime watchdog, reported 33 attacks or attempted attacks in or near the gulf this year. That is up from 13 for all of last year. In recent weeks, reported incidents have surged: Three ships were seized by pirates within 12 hours between Aug. 20 and 21. An additional four ships were captured over a 48-hour period the following week, according to reports made to the IMB.

A handful of ships are still being held by pirates in the area, including two large Malaysian vessels and a French yacht. Pirates typically seize ships and crew, and demand large cash ransoms.

In response to the increased number of attacks, a consortium of marine-insurance underwriters in London added the Gulf of Aden to its list of war zones in May. The designation spurred many insurance brokers to boost premiums for ship owners seeking coverage for a transit.

In late August, the U.S. Fifth Fleet said it would set up a special patrol area, monitored by American and other naval vessels and aircraft, to counter the piracy threat in the gulf. A United Nations Security Council resolution in June authorized international naval vessels to enter Somalia waters in pursuit of pirates.

Piracy has been a problem in other critical shipping lanes in the past, including in the Strait of Malacca between Malaysia and Indonesia, and in West African waters. But the surge in piracy in the Gulf of Aden is worrying officials because of its sophistication.

In a warning to mariners in late August, the IMB's Piracy Reporting Centre described three large "mother ships"—two Russian-made stern trawlers and a tugboat—that officials suspect are coordinating at least some of the recent attacks.

"There is a degree of organization" in recent attacks, said Commodore Keith Winstanley, a British naval officer and deputy chief of a coalition of U.S.-led navy ships operating in the Middle East region. "Which is why we're taking action," he said.

Other governments are, too, raising the possibility of armed confrontation in the strategic waterway. In April, French forces arrested a number of alleged pirates after they released crew members aboard a luxury yacht that was captured in the Gulf of Aden. Further military action could rattle energy markets, which have reacted sharply to even minor shipping disruptions in other important choke points.

On Tuesday, Malaysian shipping heavyweight **MISC** Bhd. said it had stopped sending its vessels into the Gulf of Aden entirely. The company is negotiating for the release of two ships seized there last month.

The MT Bunga Melati II, with a crew of 39 and a cargo of palm oil, was seized on Aug. 19. The Malaysian Foreign Ministry said pirates are demanding a ransom of $3 million.

Ten days later, MISC's MT Bunga Melati V was attacked. It was carrying 41 crew members and a 30,000-ton cargo of petrochemicals bound for Singapore from Saudi Arabia. MISC said it has recently made contact with the ship.

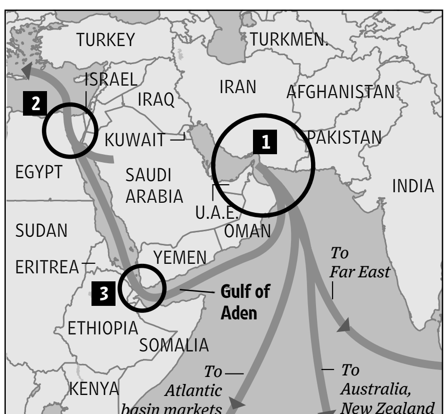
The country's deputy prime minister was quoted last week in the local press ordering Malaysian naval ships into the waterway. A Malaysian Foreign Ministry official, contacted late Friday in Kuala Lumpur, said the government was discouraging Malaysian ships from the gulf, but he couldn't confirm whether ships were being deployed to the waterway.

Trade lanes

Oil-transit points in the Middle East, 2006 oil flows, in millions of barrels a day, and share of global demand

	Oil flows 2006	Share of global demand
1. Straits of Hormuz	16.5–17	19.4%
2. Suez Canal	4.5	5.3%
3. Bab el-Mandab	3.3	3.9%

Source: U.S. Energy Information Administration



White House will press to seal India nuclear deal

By **Jay Solomon** *in Rabat, Morocco, and* **Niraj Sheth** *in New Delhi*

The administration of George W. Bush, seeking to secure a landmark nuclear-cooperation deal with India before its term expires, will push the U.S. Congress to pass the required legislation by the end of the month.

The State Department will likely begin as early as this week to submit to congressional committees the comprehensive legislation, knows as the "Hyde Package," U.S. officials said. The goal is to force an up-or-down vote by Sept. 26, the end of the current Congress's term.

"If we have any hope at all, we need to get this done before the adjournment," said a senior U.S. official working on the India legislation. "We still have a lot of hurdles in front of us."

The deal would pave the way for the U.S. to supply India with nuclear fuel and technology for civilian use. It could also open up more opportunities for American civilian and military-technology companies, like Boeing Co. and Lockheed Martin Corp., to do business in the world's second-most-populous nation.

India's Congress Party, which leads the country's coalition government, has put a priority on improving India's access to nuclear power through this deal. Although the country's economy is slowing, it is still growing fast, and the nation needs to increase power generation.

U.S. Secretary of State Condoleezza Rice said on Saturday during an overseas trip to Algeria that she has already been in contact with congressional committee chairmen to see if they can expedite the India legislation before the Congress breaks.

Administration officials identified two congressional players, both Democrats, as central to determining the legislation's fate: California's Howard Berman, chairman of the House of Representatives Committee on Foreign Affairs; and Joe Biden of Delaware, chairman of the Senate Foreign Relations Committee and the Democratic vice-presidential nominee.

Sen. Biden has been a key administration ally in supporting the India deal and had vowed earlier this year to "work like the devil" to secure its passage. Rep. Berman has been more circumspect, demanding from the Bush administration greater assurances that any U.S. nuclear assistance to India wouldn't be utilized for military purposes.

Sen. Biden's office didn't respond to a request for comment.

In a statement, Rep. Berman on Sunday expressed support for cooperation on civilian nuclear energy with India. But he said that before it votes, Congress needs to study a decision made on Saturday by the Nuclear Suppliers Group, an international body that regulates trade in nuclear materials, to lift a three-decade-old ban on doing such trade with India.

"The burden of proof is on the Bush administration so that Congress can be assured that what we're being asked to approve conforms with U.S. law," he said.

Ms. Rice has acknowledged in recent days that time is running out on one of her administration's principal foreign-policy initiatives. But she said on Saturday that even if the India deal isn't approved this year, Mr. Bush will "leave behind a good package" for the next administration to take up.

The board of governors of the United Nations' atomic watchdog, the International Atomic Energy Agency, has unanimously approved an inspections agreement with India—a key precondition for completing the deal.

Ms. Rice secured a key victory when the Vienna-based Nuclear Suppliers Group lifted the ban on India, which has never signed the Treaty on the Nonproliferation of Nuclear Weapons.

Indian Defense Minister A. K. Antony arrived on Sunday for a four-day visit to Washington, where he is expected to meet with Defense Secretary Robert Gates to discuss potential deals to buy U.S. military technology, among other issues.

—Christopher Conkey contributed to this article.

Zardari elected president

Pakistan win adds political-party clout amid rising tensions

By Peter Wonacott

ISLAMABAD, Pakistan—Asif Ali Zardari, who handily won election Saturday as Pakistan's president by an electoral college, is expected to be sworn in Tuesday.

His victory continued Pakistan's shift from military rule and completed a political resurrection for the controversial spouse of slain Prime Minister Benazir Bhutto. Until recently, Mr. Zardari was known mostly as a polo-loving playboy who tainted his wife's governments with corruption charges that landed him in jail.

Associated Press

Asif Ali Zardari's victory gives control of the presidency and the prime minister's post to Pakistan's largest grass-roots political organization.

But the sense of triumph for Pakistani democracy tied to Mr. Zardari's election was clouded by a huge car bomb Saturday in the city of Peshawar, in the Northwest Frontier Province, which killed at least 35 and injured dozens. The explosion was triggered by a suicide bomber driving a four-wheeled vehicle that slammed into a police post. The blast caused the partial collapse of a nearby market.

The final tally from an electoral college showed Mr. Zardari capturing about two-thirds of the votes cast. His win underscored the political clout of his Pakistan People's Party among provincial and national assemblies as well as the Senate, which together made up the body casting the votes. (There is no general election for president).

The lawmakers voted for Mr. Zardari over two other candidates, a retired judge, Saeeduz Zaman Siddique, and Mushahid Hussain, a leader of a party that supported Mr. Zardari's predecessor, Pervez Musharraf. Mr. Musharraf is a former army chief who had ruled Pakistan since a 1999 military coup. He resigned last month rather than challenge a drive to impeach him.

Mr. Zardari said his election represents "a historical opportunity for all political forces to change the future direction of the country," according to a statement. "We must rise above party lines to shut the doors on nondemocratic forces, once and for all."

The election comes amid heightened tensions with the U.S., Pakistan's largest foreign donor. Last week, Pakistan accused U.S.-led forces in Afghanistan of leading a cross-border raid into a Pakistani village that killed 20 people, including women and children. In a sign of rising anti-American anger, Parliament passed resolutions condemning the attack and the government summoned the U.S. ambassador to protest. A senior U.S. military official confirmed the raid but provided no details on the target or any Pakistani casualties.

Mr. Zardari's win doesn't end political uncertainty in the world's most volatile nuclear power. The military, which has run Pakistan for more than half its history, remains influential and its degree of confidence in Mr. Zardari is unclear. His five-year term is slated to stretch into 2013. Despite gaining overwhelming support Saturday from lawmakers, Mr. Zardari remains a polarizing figure.

—Shahid Shah and Neil Shah contributed to this article.

Cheney scolds Moscow at Italy security meeting

By John D. McKinnon

CERNOBBIO, Italy—U.S. Vice President Dick Cheney issued blunt new criticisms of resurgent Russia and called for Western unity in meeting its challenges in a major speech to a European security conference.

The vice president, a longtime vocal critic of Russia, offered some of the Bush administration's toughest rhetoric yet in his speech Saturday. He accused Russia of seeking to reinvent the old Soviet Union's sphere of influence and beat back the advance of democracy in Eastern Europe. He also charged that Russia has been selling weapons to Syria and Iran that have wound up in the hands of terrorists.

Dick Cheney

"In the Middle East, Russian arms-dealing has endangered the prospects for peace and freedom in the region," Mr. Cheney said. "Russia has sold advanced weapons to the regimes in Syria and Iran. [And] some of the Russian weapons sold to Damascus have been channeled to terrorist fighters in Lebanon and Iraq."

More broadly, Russia's leaders are lapsing into "the discredited notion that any country can claim an exclusive zone of authority, to be held together by muscle and threats," he said. "That is the old thinking, which created artificial divisions, militarized borders, the domination of client states, and a half-century division of East against West....In the 21st century, nations that want constructive and positive relations with one another won't get there by trying to carve out spheres of influence and trying to play balance-of-power games. The old ways are gone, the Cold War is over."

Still, the speech offered little in the way of new proposed international responses to Russia's recent incursion into Georgia, or the Kremlin's new assertiveness overall. The speech also stopped short of direct criticism of individual Western European countries that have been reluctant to confront Russia with stronger countermeasures. To varying degrees, those include Germany, France and Italy, the host country for the conference.

Instead, Mr. Cheney again called on Western nations to push forward on new oil and gas pipeline projects—such as those planned through Azerbaijan and Georgia—to help break Russia's vital grip on Europe's energy supplies.

The vice president also pushed for quick action to put Georgia and Ukraine on a fast track for NATO membership, despite Russia's opposition—and the still-long odds that European leaders will approve the applications at a meeting in December.

"Let us make clear that the enlargement of NATO will continue as and where the allies decide," Mr. Cheney said. "Allies agreed that those nations will be NATO members, and the time to begin their membership action plans has come."

Saturday's speech reflected the concern of many in the Bush administration and elsewhere that Russia's ambitions—quietly nurtured over the years since the Soviet Union's collapse—are beginning to come to fruition, exposing the impotence of the U.S. and its Western allies to respond effectively, at least in the short run, through the consensus-driven NATO.

Sarkozy to press on Georgia pact

By David Gauthier-Villars

PARIS—French President Nicolas Sarkozy heads to Moscow on Monday in an attempt to convince the Kremlin to fully implement a month-old cease-fire agreement between Russia and Georgia.

Although fighting on the ground has stopped, Russia has recognized the independence of Abkhazia and South Ossetia and stationed troops in the Georgian separatist territories.

The European Union wants Russia to back away from what it regards as a unilateral redrawing of international borders.

Yet the EU has few diplomatic levers on hand. When they met in Brussels on Sept. 1, the EU's 27 heads of state and government condemned Russia's actions, but stopped short of adopting concrete sanctions against Moscow. Some EU officials have acknowledged that taking too hard a line against Russia, a key supplier of oil and natural gas to Europe, would be counterproductive.

Instead, EU leaders asked Mr. Sarkozy, who helped broker the cease-fire deal between Russia and Georgia four weeks ago, to pursue talks with the Kremlin. On Monday, the French president, who also plans a stop in Tbilisi, Georgia's capital, will travel with EU Commission President José Manuel Barroso and the EU's chief diplomat Javier Solana.

The troika hopes to convince Russian President Dmitry Medvedev to make good on three pledges, according to French diplomats: complete the withdrawal of Russian troops, accept the presence of EU observers in Abkhazia and South Ossetia and set a date to begin talks on "security and stability" in the two separatist territories.

But the EU's requests may fall on deaf ears. Russia insists it is abiding by the terms of the cease-fire deal signed in August.

Fighting erupted early in August when Georgia tried to regain military control of South Ossetia. Russia struck back instantly, sending tanks and troops into Georgian territory.

While the EU aims to continue dialogue with Russia, the U.S. has adopted a more belligerent tone toward the Kremlin.

On Saturday in Italy, U.S. Vice President Dick Cheney said Russia's "brutality" against its southern neighbor was unacceptable.

Ukraine's leaders are urged to end feuding to ensure aid

By John D. McKinnon

KIEV, Ukraine—Vice President Dick Cheney on Friday suggested Ukraine's feuding leaders settle their disputes to be sure they get the help they might need from Western allies in fending off a newly aggressive Russia.

In light of the threats of "economic blackmail or military invasion or intimidation" in the region, Mr. Cheney said, Ukraine's "best hope to overcome these threats is to be united—united domestically first and foremost, and united with other democracies." He spoke at a joint appearance with President Viktor Yushchenko in Ukraine's presidential office building.

Later, as Mr. Cheney flew to Italy for a speech on Saturday that is expected to take a tough line on Russia, a senior administration official elaborated on the vice president's comments.

"In the aftermath of the events in Georgia, we have a great interest in supporting Ukraine's aspirations to have deeper integration into [the North Atlantic Treaty Organization] and other Euro-Atlantic institutions," the official said. "And the more that Ukrainians and Ukrainian leaders can do to fulfill all the hopes and aspirations that people have...the more the United States and Ukraine's other friends in Europe and the international community will be able to do to help Ukraine."

The official noted that Friday's discussions in Kiev came in the context of a "political situation in Ukraine which is clearly in flux." He added that U.S. officials weren't seeking to involve themselves in the dispute.

Mr. Yushchenko this week withdrew his party from the pro-Western coalition government, saying Prime Minister Yulia Tymoshenko had become too close to a pro-Russian opposition party. If no compromise is found, there will be new elections or a new coalition government that likely would be closer to Moscow—an indication of how Russia's assertiveness is polarizing politics in the region. The effect is a potentially powerful one in Ukraine, which is sharply divided between the Russian-speaking east and the Ukrainian-speaking west.

Taken together, Friday's comments reflect the worries of President George W. Bush's administration—as well as those of many leaders of young nations rising in Russia's shadow—that Russia's incursion into Georgia could be a sign of things to come elsewhere along its borders.

Rock slide kills 31 in Cairo shantytown

By Mariam Fam

CAIRO, Egypt—At least 31 people were killed over the weekend when a rock slide crashed down on homes in a shantytown here, raising criticism of the government for ignoring warnings at a time when it is already under pressure over rising food and fuel prices.

Forty-eight people were injured Saturday in the crowded Manshiyet Nasser slum, one of several areas in Egypt known as "*ashwa'iyat*"—literally "random areas," in Arabic. Amid a swelling population here, illegal housing has been cropping up in such areas for years.

Casualty figures could rise dramatically. An unknown number of people are still trapped under rocks and debris. Some residents and government critics accused officials of ignoring warning signs that could have prevented the loss of life.

"Little problems are left unsolved by the governments of the [ruling] National Democratic Party...to the extent that they come back and explode in our faces," said Mohammed Sherdy, an opposition lawmaker. "The negligence that is so apparent in this case should not go unpunished."

Ahmed Mohammed, a 29-year-old resident, said he heard from neighbors that some had notified local authorities at least two weeks before the incident that pieces of cliff were crumbling above the settlement.

Ruling party officials defended their response. Ruling party official Mohammed Ragab told the Arabic-language Al-Arabiya satellite channel that "no one [found responsible] will escape punishment."