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## What's News

U.S. stocks fell, with the DJIA down 2.3%, as investors showed trepidation ahead of Alcoa's kickoff of earnings season after the market closed. Shares in Europe also lost ground on jitters about corporate earnings. **Page 20**

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■ **European airlines reported steep declines in March traffic, with Air France-KLM hit especially hard.** **Page 6**

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### EDITORIAL OPINION

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Breaking news at europe.WSJ.com

## Fight to save Italy's gems

With quake deaths topping 200, rescuers try to reach imperiled artwork

By Stacy Meichtry

L'AQUILA, Italy—Anna Maria Reggiani, head of the local branch of Italy's Ministry of Culture, surveyed the crumbling entrance of the Castello Spagnolo—the Spanish Castle—on Tuesday morning. She delivered a dire prognosis on the paintings and sculptures inside the 16th-century castle, built during the rule of Holy Roman Emperor Charles the V.

"There are thousands trapped in there and we can't get to them," she said. "These works are what connect us to our past."

nect us to our past."

The magnitude 6.3 earthquake that hit this area of central Italy left 207 people dead in L'Aquila and surrounding villages by Tuesday night. Up to 15,000 buildings were damaged or destroyed and 17,000 people had to stay in tents because their homes were too fragile.

Already, as rescue workers continue to dig through the rubble, experts are thinking about how to save works of culture and art. Italy has a long history of quakes, and its large number of old buildings make it particularly vul-

nerable. Many of these historic structures contain works of art stretching back for centuries. Italy has the largest number of World Heritage Sites, as listed by Unesco—43, of which 37 count as "cultural."

L'Aquila and its surrounding area contain thousands of monuments and works of art, some of which are centuries old. Hundreds of paintings and sculptures are trapped inside damaged or collapsed buildings.

Most churches throughout the area were severely damaged—in two cases toppling the cupolas and in one

more collapsing one of the main walls. Another historical building was destroyed.

"L'Aquila is extremely rich in art and architecture," said Francesco Benelli, a professor of art history and archeology at Columbia University in New York. "The artistic heritage in the region has been severely damaged by the earthquake."

After rehousing the homeless, he added, "the first operation should be to rebuild the damaged structures."

On Tuesday, Mrs. Reggiani had two main worries:

*Please turn to back page*



The Cathedral of L'Aquila is one of the many historic treasures among the 15,000 buildings damaged or destroyed in Monday's earthquake.

## Crackdown shackles Swiss private bankers

By Stephen Fidler

LONDON—Swiss private bankers are becoming wary about travelling abroad, underscoring how hard a global crackdown on tax avoidance is hitting the discreet business of providing banking services to the wealthy.

UBS AG, the world's largest manager of private wealth by assets, has barred "client-facing" staff in its wealth-management divisions from traveling abroad—a move aimed at avoiding further trouble for the bank, which already has had two bankers arrested as part of a continuing U.S. investigation into tax fraud.

At the same time, other private bankers in Switzerland are being advised to exercise personal discretion in their travel decisions, people

familiar with the matter said.

The travel jitters come as leaders of the Group of 20 developed and developing nations have redoubled their efforts to crack open the secretive tax havens where private bankers often park their clients' money. Following last week's G-20 meeting, the Organization for Economic Cooperation and Development included Switzerland on a "gray list" of countries that hadn't yet followed through on promises to comply with its directives on sharing tax information.

Meanwhile, U.S. authorities have been offering leniency to tax evaders in exchange for information on the bankers who helped them hide the money.

For UBS, the travel ban could hinder the lucrative wealth-management busi-

ness on which it has relied to survive the financial crisis. That business was already declining as U.S. tax authorities pushed the bank to provide them with names of U.S. clients suspected of tax evasion.

UBS has turned over information on nearly 300 accounts as part of a deal in which it admitted to conspiracy to defraud the U.S. Internal Revenue Service. The bank is still under pressure from the IRS to provide information on 52,000 other accounts. UBS says bank secrecy laws forbid it to do so.

Two UBS bankers have been arrested and a further senior executive is being sought in connection with the case. U.S. investigations continue into some of the bank's U.S. clients.

Private clients at UBS

withdrew a net 123 billion Swiss francs (\$108.17 billion) in 2008, compared with a net inflow of 156 billion francs in 2007. That means the bank lost market share to its chief rival, Credit Suisse Group AG, whose private-banking business saw 51 billion francs of inflows last year. UBS had a total of 1.6 trillion francs under management at the end of last year, compared to 789 billion francs at Credit Suisse.

A UBS spokesman said the travel ban, which went into effect April 1, was a "precautionary measure" that would last at least several more weeks while the bank reviews its compliance procedures.

The ban affects about 1,000 of the bank's roughly 14,000 client advisers.

Most advisers deal only *Please turn to page 31*

## Obama's measured progress on trip

By Jonathan Weisman

ISTANBUL — U.S. President Barack Obama capped his eight-day introduction to the world diplomatic stage with a trip to the war he hopes to end—an unannounced stop in Baghdad.

The U.S.-led invasion of Iraq strained diplomatic relations throughout Europe, and Obama aides said the president's first major trip abroad—a voyage of more than 20,000 kilometers that included six countries, private meetings with 19 world leaders and dignitaries, three summits, two town-hall meetings, one parliamentary and one public address—was aimed as much at easing tensions with allies as at racking up immediate, tangible achievements.

"Why didn't the waters part, the sun shine and all the ills of the world disappear because President Obama came to Europe? That wasn't our expectation," said White House senior adviser David Axelrod. "That'll take at least a few weeks."

The president did emerge with some concrete achievements, in part because he lowered expectations. Grand aims at global economic stimulus gave way in London on Thursday to a framework for international financial regulation, a published list of tax havens and billions more dol-

*Please turn to page 31*

### Inside



#### Power player

TARP's CIO turns the screws as Washington culture shifts **News in Depth, pages 16-17**

### Markets

4 p.m. ET

	CLOSE	PCT CHG
DJIA	7789.56	-2.34
Nasdaq	1561.61	-2.81
DJ Stoxx 600	183.46	-0.84
FTSE 100	3930.52	-1.58
DAX	4322.50	-0.63
CAC 40	2902.31	-0.94
Euro	\$1.3275	-0.88
Nymex crude	\$49.15	-3.72

LEADING THE NEWS

# Obama makes a surprise trip to Baghdad

**U.S. leader praises Iraqi political gains, meets with Maliki**

BY JONATHAN WEISMAN

ISTANBUL—U.S. President Barack Obama made a surprise visit to Baghdad, saying such a trip was critical because progress in Iraq, which has been rocked by a new round of bombings, lies “in political solutions.”

Meeting with Gen. Raymond Odierno and about 600 U.S. troops at Camp Victory, outside Baghdad, on Tuesday, Mr. Obama said that “we’ve made significant political progress” in Iraq. But, he added, “with the national elections coming up, many of the unresolved issues may be brought to a head.”

Iraqi Prime Minister Nouri al-Maliki planned to join Mr. Obama at Camp Victory on Wednesday. The U.S. president will confer with

Iraqi President Jalal Talabani by telephone because a sandstorm has grounded the Iraqi president’s helicopter, U.S. officials said.

White House spokesman Robert Gibbs told reporters that Iraq was chosen over Afghanistan for the visit in part because of its proximity to Istanbul but also because troops in the war Mr. Obama hopes to end are just as important as troops in Afghanistan, where he hopes to intensify the U.S. campaign against Taliban militants. The president will award 10 medals of valor on Wednesday while visiting troops at the sprawling base near Baghdad International Airport. “They’re putting their heart and soul into this,” Mr. Obama said.

Mr. Obama entered the gaudy Rotunda Room of Saddam Hussein’s former Al Faw Presidential Palace on the Camp Victory grounds to the strains of “Hail to the Chief” just after 6 p.m. Tuesday, Baghdad time. Troops snapped pictures and cheered. One soldier shouted, “Love you.”



Associated Press

U.S. President Barack Obama greets military personnel in Baghdad Tuesday.

The president told them they faced strain, sacrifice, controversy and politics. Turning Iraq into a fledgling democracy is an “extraor-

dinary achievement,” he said.

The next year and a half “could be a critical period,” Mr. Obama warned. “It is time for us to transfer to the Iraqis. They need to take responsibility for their country.”

He expressed sympathy for the troops’ multiple rotations, their separation from family, and the injuries and deaths they have suffered.

“As long as I’m in the White House, you are going to get the support that you need,” he said.

The trip is Mr. Obama’s first to Iraq as president. While the White House kept the excursion under wraps for security reasons, the military was mobilizing. Army officers had intended to have at least 1,500 troops from Camp Victory and nearby Camp Liberty to greet the president, but the secret trip happened faster than expected, beating most of the troops by a couple of hours.

The trip comes amid increasing worries that a power vacuum may already be developing as the U.S. pre-

pare to slowly withdraw forces. In February, the president said he will withdraw all combat forces from Iraq by August 2010, although he could leave behind a residual force of as many as 50,000 to train Iraqi police and military, hunt terrorists and protect U.S. assets, such as the largest U.S. embassy in the world. Even most of those troops would be gone by the end of 2011.

A series of six car bombs in and around Baghdad killed 33 people on Monday alone, wounding scores more and raising the prospects of a resurgence of violence. Most of the bombs struck predominantly Shiite neighborhoods. Just hours before Mr. Obama touched down in Iraq on Tuesday, a car bomb in a Shiite neighborhood in Baghdad killed at least nine people and wounded 18, according to the Associated Press. That followed Monday’s carnage.

Mr. Gibbs said Gen. Odierno assured the president that security incidents are still at the lowest since the war began, despite the recent upsurge in violence.

## Continental steps closer to joining air alliance

BY CHRISTOPHER CONKEY AND PAULO PRADA

WASHINGTON—The U.S. Transportation Department on Tuesday gave Continental Airlines Inc. preliminary approval to join a global alliance that cooperates on scheduling and revenue sharing, a sign that the Obama administration may not support a congressional effort to limit such alliances.

The administration’s decision will allow Continental to join the Star Alliance with UAL Corp.’s United Airlines, Air Canada Corp., Deutsche Lufthansa AG and other carriers. The approval was expected and is consistent with policy under previous administrations.

But the Continental action comes as Rep. James Oberstar, a Minnesota Democrat who serves as chairman of the House Transportation and Infrastructure Committee, is pushing legislation that would curtail such international airline alliances. The agreements enable airlines to act as a single carrier for certain international services, but Mr. Oberstar, who couldn’t be reached for comment, says they limit competition and hurt consumers.

The Transportation Department also said it will allow Continental,

United, Air Canada and Deutsche Lufthansa to form a new joint venture called Atlantic Plus-Plus. Under the new venture, the carriers will be permitted to jointly manage sales, capacity, marketing and revenue. This will allow the airlines to eliminate some competing flights and instead steer passengers from their networks onto a partner’s plane. This approval doesn’t apply to domestic service.

Star Alliance members compete with two other global alliances. One is SkyTeam, an alliance that had included Continental but now includes Delta Air Lines Inc. and Air France-KLM SA. AMR Corp.’s American Airlines, currently part of the oneworld alliance with British Airways PLC and Spain’s Iberia Lineas Aereas de Espana SA, has also asked the government for antitrust immunity to cooperate more closely with those carriers on trans-Atlantic flights.

For Houston-based Continental, the switch to the Star alliance will give it a bigger and more strategic role than it currently has in SkyTeam, where many of its routes overlapped with Delta. By aligning itself with United, whose main international routes lie across the Pacific, and Lufthansa, one of the biggest carriers in Europe, the airline is expected to enjoy a greater volume of transfer traffic and broader international reach than it does at present.

In a statement, the Transportation Department said the alliance would “be in the public interest because it would support increased levels of service in international markets served by the carriers, give consumers more travel options and shorter travel times, and reduce fares.”

## Belgian Shoes



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### CORRECTIONS & AMPLIFICATIONS

Ford Motor Co.’s market share in the U.K. climbed to 16.7% in March from 15% in the year-earlier period. A Focus on Automobiles article Tuesday incorrectly said Ford’s market share slipped to 15% from 16.7%.

## INDEX TO PEOPLE

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



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## LEADING THE NEWS

# China takes steps in health-care overhaul

## Expansion planned for hospitals, clinics, insurance subsidies

BY GORDON FAIRCLOUGH

SHANGHAI—China pledged to expand medical insurance and build thousands of hospitals and clinics over three years, the first steps in a decadelong plan to repair an ailing health-care system that has fueled popular discontent.

On Tuesday, the State Council, China's cabinet, offered details on the \$120-billion-plus initial phase of the revamp, which it outlined in January. Among the plans: a construction surge that by 2011 will give every village a medical clinic and ev-

ery county at least one hospital.

The government and ruling Communist Party are trumpeting the blueprint with a major public-relations push, signaling the political importance of rebuilding a social safety net that was largely dismantled during the country's shift to a market economy over the past 30 years.

"The plan is a necessary support for developing a harmonious and stable society," said Jia Kang, director of the Research Institute of Fiscal Science, a think tank affiliated with the Finance Ministry, who said it is focused on "providing basic medical guarantees to the lowest-income people."

Under the plan, government subsidies for insurance premiums aim to extend at least basic coverage to 90% or more of China's 1.3 billion people within three years.

Chinese people are covered by a patchwork of government-run plans supplemented by some private insurance. The government estimates that about 90% of rural people are already enrolled in its insurance program, which requires them to pay premiums. Coverage is more spotty in urban areas, especially among the unemployed.

By 2020, the government says, all citizens should have access to basic health services. The proportion of medical expenses covered by state insurance plans will increase over time, and prices of so-called essential drugs, such as widely prescribed antibiotics, will be pushed down.

In the near term, many Chinese could still have to pay a significant part of health-care costs—a factor that will weigh on domestic consumption as families continue to es-

chew spending and save to be prepared in case illness strikes.

China's state spending on health has failed to keep up with its booming economy. In 2006, China's government health outlays amounted to less than 1% of gross domestic product, putting China 156th out of 196 countries surveyed by the World Health Organization.

Government spending has tended to favor urban populations. In 2005, according to the WHO, 25% of public-health money was devoted to rural areas, home to roughly 60% of the population.

The plan is designed to start narrowing that gap. The current "resource allocation is unreasonable," the State Council said Monday, leading to relatively weak "rural and community medical services."

Important aspects of the plan

have yet to be worked out. The government is drawing up a new essential drug list, and will announce recommended retail prices for medicines. Local governments will buy the drugs from low bidders in a public tender and distribute them.

Decisions on one thorny issue—how to remake the public hospital system—have been put off pending the outcome of studies. Hospitals, which have been pressed to generate income, rely on drug sales and expensive tests to boost revenue, critics say.

Beijing wants to sharply limit hospitals' ability to earn money from drug sales, and instead push them to cover their costs by charging for physicians' work and other services. Most prescription drugs in China are sold through hospitals and clinics.

—Ellen Zhu  
contributed to this article.



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## CORPORATE NEWS

## Smoothies burnish Coke's image

Stake in fast-growing drink maker Innocent gives beverage giant entree to ethical market

BY AARON O. PATRICK  
AND VALERIE BAUERLEIN,

Coca-Cola's investment in British smoothie-maker Innocent not only connects the beverage giant to a fast-growing product but also to a company known for good social and environmental behavior.

Coke said this week it will take a minority stake in London-based Innocent, which has quickly become one of Britain's top brands by marketing its healthy ingredients and social commitment. By giving 10% of its profits to charity and using recycled bottles, Innocent was one of the first consumer brands launched in Britain to develop a big following through ethical marketing.

The investment of £30 million, or about \$44 million, may be small, but it speaks to Coke's continued interest in expanding beyond soft drinks, and in owning small stakes in innovative companies. Details of the transaction weren't disclosed, but Coca-Cola will have a stake between 10% and 20%, valuing Innocent between £150 million and £300 million, Innocent co-Chief Executive Richard Reed said. Founded 10 years ago, it now has 82% of the U.K. smoothie market, according to an spokeswoman.



Coca-Cola's purchase of a minority stake in Britain's Innocent brings linkage to a marketer with an environment halo. Its Dancing Grass Van peddles smoothies.

Innocent cuts a quirky public figure. Some of its trucks are covered in fake grass and daisies. Those trucks are mounted on hydraulics that make them appear to dance, with drop-down windows for giving away samples.

The deal's structure should allow Innocent to keep its funky attitude rather than risk being assimilated

into a vast corporate culture whose focus remains carbonated soft-drinks. Coca-Cola won't have any management control over Innocent, but Innocent will share its expertise with the Atlanta-based drinks group, Mr. Reed says. "They are very interested in our recycled bottles," he says.

The Coca-Cola money will be

used to expand Innocent's operations in Europe, where only 25% of European supermarkets sell smoothies, Mr. Reed says. The money will be used to pay for distribution, stocking fees, sales staff and advertising, he says.

While Innocent has run TV and newspaper ad campaigns, it has also specialized in less-traditional advertising. One of its ad agencies, Albion, created a board game for schools promoting the health benefits of fruit and vegetables. Some 200,000 people turned up to a Innocent musical concert in London named Fruitstock in 2006. In following years it replaced the event with smaller village fetes.

Innocent's charitable giving is sometimes interactive. Volunteers last year knitted more than 506,000 little hats for smoothie bottles, which were then sold, raising £250,000 to provide meals, blankets and other help for older people during the winter.

To be sure, Coke has been sporting its good deeds, expanding its recycling plants, reducing water consumption and using environmentally friendly coolants in vending machines. Coke and its foundation made more than \$82 million in charitable donations in 2008.

## Decline in sales for luxury cars slowed in March

BY CHRISTOPH RAUWALD

FRANKFURT—The declines in luxury-car sales at BMW AG, Daimler AG and Audi eased somewhat in March from earlier in the quarter, but the world's three biggest manufacturers of premium cars remain affected by the recession.

"We have seen some encouraging signs in key markets like the U.S. and Germany. However, it is still too early to talk about a global turnaround," BMW executive-board member Ian Robertson said in a statement.

The company's core BMW brand sold 104,417 vehicles in March, down 17% from a year earlier. For the first quarter, the BMW brand posted a 21% sales drop from a year earlier to 233,498 vehicles as the downturn in the U.S. auto market, BMW's single biggest market, took its toll.

The world's top-selling premium-auto maker launched a revamped version of its flagship 7-series in the U.S. in March and said it expects the new model to "boost sales throughout the rest of the year in what has traditionally been this series' most important market."

The world's second-best-selling luxury-car maker, Daimler's Mercedes-Benz unit, sold 98,500 cars in March, down 18% from a year earlier. In the January-to-March period, Mercedes-Benz saw sales contract 25% to 216,000 cars.

The Stuttgart-based auto maker expects a push from a new version of the Mercedes-Benz E-Class, which is widely seen as the company's most important model launch this year. The E-Class is a crucial car for the company in terms of sales volume and revenue per vehicle.

"Orders for the E-class sedan in Germany in the first quarter of this year were more than double the number posted in the same period in 2008. We had already received about 50,000 orders for the new E-Class sedan by its market launch at the end of March," Mercedes-Benz Cars' sales chief Klaus Maier said in a statement.

Incentives to scrap older vehicles in Europe had little effect on demand for luxury cars, as it mainly boosted sales for smaller, mass-market models. Mercedes-Benz, however, noted that sales for its compact A-Class and B-Class models saw an improvement in recent weeks.

Audi continued to narrow the gap on its two larger German rivals because of several new and revamped models, such as the best-selling A4. Global sales fell 11% in March to 90,400 vehicles, and sales slipped 16% in the January-to-March period from a year earlier to 210,026 cars. The decrease was cushioned by Audi's best sales month ever in China.

The premium division of Volkswagen AG, Europe's largest auto maker by sales, expects sales momentum to pick up in coming months.

"Thanks in part to the successfully launched Audi Q5, our order intake is now significantly increasing," Audi sales chief Peter Schwarzenbauer said in a statement.

Audi has previously said that it wants to become the world's best-selling luxury-car maker by 2015, outpacing both BMW and Mercedes-Benz, partly by significantly boosting its presence in the U.S., where it still lags behind its peers despite strong growth in Europe and Asia in recent years.

## Auto makers step on the gas for electric cars

BY ALEX P. KELLOGG

Auto makers continue to push ahead with battery-powered cars despite waning demand for fuel-efficient vehicles in the U.S.

On Monday, Fisker Automotive Inc. said it received \$85 million in additional venture capital that will help the 18-month-old California start-up begin producing the Karma luxury sports car it has been developing.

Fisker hopes to sell 15,000 Karmas in 2010, and plans to show the car at the New York Auto Show starting this week.

Separately, Chrysler LLC selected A123 Systems Inc. of Watertown, Mass., to supply lithium-ion battery cells, packs and modules for electric cars that Chrysler expects to have in showrooms in late 2010.

The potential sales of such vehicles is unclear, however. With gasoline going for a little over \$2 a gallon (50 cents a liter) in the U.S., sales of high-mileage vehicles and gas-electric hybrids have plunged.

In March, Toyota Motor Corp. sold 8,924 Prius hybrids, down 57% from a year earlier, according to Autodata Corp. It had planned to build Priuses in a new plant in Mississippi but has frozen the project indefinitely. General Motors Corp., meantime, sold just 547 hybrid versions of the Chevrolet Malibu in March.

Last week, in an assessment of GM, the Treasury Department's auto task force expressed concern about the Chevrolet Volt, an electric vehicle GM is developing. While the Volt "holds promise," the task force said, it will probably be much more expensive to make than gasoline-powered cars and need substantial cost reductions



Chrysler selected A123 Systems to supply the batteries for electric cars it is developing, including the Dodge Circuit shown above.

to be "commercially viable."

Henrik Fisker, chief executive of Fisker Automotive, said in an interview that the new round of capital signals "that plug-in hybrids re-

ally have the mass-market potential that people have been waiting for."

The capital will come from Eco-Drive (Capital) Partners LLC, an in-

vestment consortium, and Kleiner Perkins Caufield & Byers, a veteran Silicon Valley venture-capital firm. The company says it has funding well over \$100 million but declined to be specific.

The Fisker Karma is a sleek sports car that is supposed to start at \$87,900 and travel 80 kilometers on electrical power and for an additional 400 kilometers on a 2.0-liter gasoline engine before requiring refueling. The Irvine, Calif., company has orders for 1,300 vehicles, Mr. Fisker said.

"I definitely believe the plug-in hybrids will be the dominant alternative type of vehicle in the next five to six years," Mr. Fisker said, "and we feel we can actually take the lead in this new technology."

Chrysler is aiming for a similar spot in the market with the Dodge Circuit sports car. It also is working on battery-powered versions of the Jeep Wrangler, Jeep Patriot and Chrysler Town & Country minivan.

## GM, Segway to develop urban vehicle

BY SHARON TERLEP

General Motors Corp. is teaming with Segway Inc., maker of the upright, self-balancing scooters, to build a new type of two-wheeled vehicle designed to move easily through congested urban streets.

The machine, which GM says it aims to develop by 2012, would run on batteries and use wireless technology to avoid traffic backups and navigate cities.

The struggling auto maker, surviving on a government lifeline, is looking to generate enthusiasm for its in-

creasingly uncertain future ahead of the New York auto show this week.

GM has slashed product-development programs, advertising and spending on auto-show events. But it was planning to take to the streets of Manhattan on Tuesday to show off a prototype of the vehicle, called PUMA, for Personal Urban Mobility and Accessibility.

The Segway Personal Transporter was launched with considerable hype eight years ago but practical issues prevented it from becoming a mass-market product, including its relatively high cost and restric-

tions on its use in many jurisdictions.

GM is betting PUMA's more carlike traits—an enclosed compartment and top speed of 55 kilometers per hour—will lead to better results. GM didn't say how much the machines would cost, but research chief Larry Burns said owners would spend one-third to one-fourth of the cost of a traditional vehicle.

PUMA would have a range of about 55 kilometers. GM said it aims to use so-called vehicle-to-vehicle technology to avoid traffic problems and potentially have it navigate itself through city streets.

## CORPORATE NEWS

# Israel's high-tech sector stumbles

*As buyers disappear, experts worry of risks to nation's economy*

BY CHARLES LEVINSON

MOSHAV MAZOR, Israel—Groomed in a secretive electronic-warfare unit in the Israeli army, Motti Avrahami went on to become a top executive at a software firm here in Israel's high-tech belt.

Just months ago, he was the classic Israeli high-tech success story. Today, he is collecting unemployment, tending to the fruit trees and rose bushes in his spacious yard, and preparing for a new career—leasing cars.

"There's no future for me in high tech," said Mr. Avrahami, 36 years old.

His sudden change of fortune is part of a deepening slump hitting Israel's high-tech sector, which generates \$25.5 billion of annual sales in the nation's \$200 billion economy. The industry has churned out fire-wall security software now protecting many of the globe's biggest corporations, along with USB memory drives, which revolutionized data storage. And Israel boasts more Nasdaq-listed companies than any country besides the U.S. and China.

It is also a crucial driver for Israel's small, export-dominated economy, accounting for 47% of exports, according to the Israel Manufactur-

ers Association. With buyers disappearing in Israel's biggest markets—North America, Europe and Asia—the sector is suffering and some experts worry it could pull down the rest of the Israeli economy with it. In 2000, the bursting of the Internet bubble helped send the country into its worst recession since the early 1950s. The 2000 recession was short-lived, however, and by 2003 the economy had largely recovered.

Israel's central bank predicts the country's economy will shrink a moderate 1.5% in 2009. The Israeli government has announced a modest stimulus package to bolster demand and prop up bond markets.

Israel's economy has held up better than most so far in the global downturn. Its banks appear to be sound. Stock-market and real-estate prices are down, but they haven't crashed like they have elsewhere.

But the high-tech sector's woes have many here worried that much more serious economic pain is right around the corner, once the full impact of declining demand for Israeli exports hits home. The high-tech industry employs 7% of the country's work force, and some analysts say each high-tech worker supports the jobs of six workers in other sectors. The government reported this month that 20,072 people were laid off in Israel in March, an all-time monthly record.

"People are still underestimating the damage being done to Israeli high tech and what this can mean

for the whole economy," said Moshe Zviran, founder of a high-tech-focused consulting company and a professor at Tel Aviv University.

The government estimates nearly 8,000 high-tech workers, some 6% to 8% of the sector's work force, have been laid off since October. Companies announce new job cuts almost every day.

As many as 10,000 more high-tech jobs will be cut this year, according to the IDC Research Co., a Boston-based, global high-tech research firm. Demand for Israeli high-tech exports has already dropped 10-15%, according to IDC.

If the slump continues too long, and the layoffs cut too deep, Mr. Zviran worries that the country's leading engineers and innovators won't return. Israel could emerge from today's global slump with its technological edge blunted, he said.

Laid-off high-tech workers are already seeking work elsewhere. The Ministry of Education has begun a program providing teaching jobs for unemployed university graduates. Of the 2,200 people who have registered so far, 1,200 are from the high-tech sector, according to ministry spokeswoman Hagit Cohen.

The sector has been a source of pride for a country often associated with conflict and war. It has fostered an internationally recognized pool of entrepreneurs, research-and-development whiz kids, and government funding and private-venture capital to harness all that talent.

Israel even has its chief scientist,

who doled out some \$250 million last year in research and development grants to promising Israel start-ups.

"A young Israeli dreaming of making it big looks to high tech," said Eytan Avriel, editor of Israel's leading economics journal.

Mr. Avrahami typified the Israeli technology highflier. After military service, he enrolled at Haifa's prestigious Technion technology institute, and then landed a job with Silicon Valley-based VeriFone Holdings Inc.

In 2007, he was made vice president at a young software-testing company based in Israel's high-tech belt, north of Tel Aviv.

In September, with his wife seven months pregnant with their second child, the first signs of trouble emerged. Smaller clients started canceling contracts as they cut down on outsourcing costs. By December, the company's largest clients had all canceled as well.

"There was no problem with our company or our product. It was a problem with the customers," Mr. Avrahami said.

Faced with a 50% pay cut, he considered starting his own software-testing business. But capital-raising among start-ups in Israel has fallen off a cliff in recent months, and he didn't think he could tap the necessary funds from investors.

So, he changed careers. Next month, he begins classes at Cal Auto College and intends to get into the car-leasing business.

## Indian agency files charges in Satyam case

BY ROMIT GUHA AND R. JAI KRISHNA

The Indian federal agency investigating the accounting issues at Satyam Computer Services Ltd. said Tuesday it has filed charges of cheating and forgery against the former chairman of the Indian software exporter, B. Ramalinga Raju, and eight others.

The Central Bureau of Investigation said in a statement that in addition to Mr. Raju charges have been filed against his brother and former managing director B. Rama Raju; former Chief Financial Officer S. Vadlamani; auditors S. Gopalakrishnan and S. Talluri; B. Suryanarayana Raju; G. Ramakrishna; D. Venkatapati Raju; and Srisailam Chetkuru.

The CBI statement said the charges include offenses of criminal conspiracy, cheating, forgery, falsification of accounts and causing the disappearance of evidence.

Lakshmi Narayana, who is in charge of the CBI investigation, said the probe is still ongoing and if necessary further charges can be filed.

Hyderabad-based Satyam plunged into turmoil following revelations in January by B. Ramalinga Raju of overstating profits, revenue and creating a fictitious cash balance of more than \$1 billion. Other government agencies currently investigating the company include capital markets regulator, SEBI, the registrar of companies, and the serious fraud investigations office.

G. Ramakrishna; D. Venkatapati Raju; and Srisailam Chetkuru were arrested April 5, while the others have been in custody since soon after the financial scandal came to light in early January. All the people charged worked for Satyam or a Raju family company except for Messrs. Gopalakrishnan and Talluri, who worked for Price Waterhouse, the Indian affiliate of Price-waterhouseCoopers.

Lawyers for B. Ramalinga Raju, B. Rama Raju and Mr. Vadlamani said they haven't yet received a copy of the charges and will respond after that.

Lawyers for B. Suryanarayana Raju, G. Ramakrishna, D. Venkatapati Raju and Srisailam Chetkuru couldn't immediately be reached for comment.

Mastan Naidu, lawyer for Messrs. Gopalakrishnan and Talluri said his clients are innocent. "They were just performing their duties," he said. Price Waterhouse audited Satyam's financial statements from mid-2000 to late 2008.

Price Waterhouse said it was "surprised and disappointed" that the CBI pressed charges against the two auditors. "The fraud perpetrated by Mr. Raju and his cohorts was designed to and did circumvent PW India's audit process; the two Satyam audit partners—and PW India—were victims of that fraud," the statement said.

A Satyam spokeswoman said that company is "cooperating with the investigations" but declined to comment on the charges.



B. Ramalinga Raju

## Veolia to take 50% stake in Hong Kong tram

BY YVONNE LEE

HONG KONG—Hong Kong's iconic streetcars are going under French management as Wharf Holdings Ltd. sells a half stake in the network to utility Veolia Environnement.

Hong Kong's tram system, known locally as the "ding ding" for the clanging bells on the streetcars, will be held in a 50-50 joint venture between Wharf Transport Investments Ltd. and Veolia Transport China Ltd., under the deal announced Tuesday.

Veolia will operate the trams and receive an option to buy Wharf's stake, Wharf Transport director Frankie Yick said at a news conference. He declined to provide financial details.

Hong Kong Tramways, dating to 1904, operates 163 tram cars on Hong Kong Island, transporting around 240,000 passengers daily.

Bruno Charrade, head of operations at Veolia Transport China, said the tram system might be expanded with a loop along a waterfront development between the Central and Wan Chai business districts.

Wharf also owns and operates the Star Ferry, Hong Kong's oldest ferry service linking Hong Kong Island with the Kowloon peninsula. Wharf plans to keep the ferry, Mr. Yick said.

Hong Kong's trams and the Star Ferry are popular attractions for tourists and are Hong Kong's least expensive form of transportation, with fares a fraction of the price of subway tickets. Hong Kong Tramways charges adults two Hong Kong dollars, about 25 U.S. cents, for single journeys. Mr. Yick said the tram is profitable but he didn't provide figures.



Wharf Holdings' Hong Kong streetcars, known locally as the 'ding ding,' carry about 240,000 passengers daily.

## HTC sees signs of revival in smart-phone market

BY TING-I TSAI

TAIPEI—HTC Corp. sees signs that the global smart-phone market is reviving after a relatively weak first quarter, Chief Executive Peter Chou said.

"The market is picking up again, and we think it should perform well," Mr. Chou said in an interview Tuesday. His comments came a day after the Taiwan smart-phone company posted a 30% drop in its first-

quarter net profit from a year earlier amid economic weakness and delayed shipments of some products.

Mr. Chou said HTC remains optimistic about its full-year forecast for double-digit revenue growth. He said the company is starting to ship new smart-phone models again this quarter, and that it plans this year to introduce 15 new models of smart phones, which are handsets that include wireless email, video and other sophisticated data functions.

Smart phones were one of the few fast-growing sectors in the technology industry last year, with more than 20% growth globally in unit sales.

HTC started by making products mainly on contract for other brands or for wireless companies, but it increasingly has focused on building its own brand. Last year, HTC held 4.5% of the global smart-phone market, according to research firm Gartner Inc.

## CORPORATE NEWS

# Europe air traffic slumps

## Air France-KLM hit particularly hard by global trade drop

A WSJ NEWS ROUNDUP

PARIS—European airlines, including Air France-KLM SA, reported steep declines in March traffic as cargo loads continued to fall and empty business seats added to widening losses.

The Franco-Dutch airline—Europe's largest—said Tuesday that it carried 5.7 million passengers last month, down 9.8% from March 2008, while traffic fell 9.4%. Its passenger-load factor, which measures how full a carrier's aircraft are, fell 5.5 percentage points to 75.5%.

"This decline was accompanied by a significant deterioration in unit revenues," said Air France-KLM, without providing further details.

Like other airlines, Air France-KLM has been hit particularly hard by the decline in international trade. Stripping out the contribution of its Dutch Martinair subsidiary, cargo traffic at the airline fell 19% in March. Including Martinair, which specializes in hauling cargo, the carrier's overall cargo traffic rose 1.3% last month. Air France-KLM started consolidating Martinair's results in January.

Cargo-load factor excluding Martinair fell 7.8 percentage points to 61.4%. Including Martinair, cargo-load factor fell 6.8 percentage points to 62.5%. March was the fourth month in a row that the world's largest carrier of international freight, has seen cargo bookings drop about 20%.

Air France-KLM has been trying to shore up its profitability by trim-



Air France-KLM, Europe's largest airline, posted sharp year-to-year declines in March passenger and cargo traffic as international trade fell amid the recession.

ming capacity as key markets slacken amid the global economic slump. Yet in March, the declines in both passenger and cargo traffic, excluding Martinair, outpaced capacity cuts in both business lines of 2.9% and 8.9%, respectively.

The weak numbers didn't come as a surprise. Air France-KLM had flagged a lower trend for March two weeks ago, warning that falling passenger and cargo activity as well as fuel-hedging losses would push it into an operating loss of about €200 million, or \$268 million, for its fiscal year ended March 31.

"Conditions on the European network remain tough," the airline said, adding that traffic on its Caribbean and Indian Ocean network was hit by strike action in the French Antilles.

Other European airlines didn't fare much better last month, partly because year-earlier results were boosted by an early Easter holiday.

Scandinavian carrier SAS AB said it carried 2.2 million passengers in March, off 9.3% from a year earlier, while traffic dropped 17% and its passenger-load factor fell 9.9 percentage points to 64.5%.

Finnair Oyj, meanwhile, said traffic fell 8% and added that it expects capacity this year to be 6% lower than in 2008. Air Berlin PLC said its passenger levels fell 6% in March, as the German carrier's load factor dropped 3.7 percentage points to 74.1% despite a 4% cut in capacity.

Tuesday's stream of data arrived after U.S.-based Delta Air Lines Inc., the world's largest carrier after taking over Northwest, said its international passenger traffic fell 15% and cargo activity dropped 36% last month. Delta and Northwest together make up the third-biggest domestic airline freight network, according to IATA data for 2007, the most recent available.

# Pfizer splits R&D into two groups

BY AVERY JOHNSON

Pfizer Inc. outlined the leadership structure of its sprawling research efforts once it merges with Wyeth, moving ahead on its commitment to swiftly integrate the two organizations.

Pfizer said on Tuesday it will break research and development into two separate organizations, one that looks at traditional chemical pills called small molecules and another that studies large-molecule, or biologic, drugs made from living cells. Pfizer's current R&D chief Martin Mackay will lead the small-molecule researchers, while Wyeth's R&D leader Mikael Dolsten will oversee the biologics efforts.

Pfizer also said it would retain Wyeth's head of vaccines, Emilio Emini, and Wyeth's head of discovery, Menelas Pangalos. Dr. Emini and Dr. Pangalos will be chief scientific officers at Pfizer for vaccines and neuroscience, respectively.

"Creating two distinct, but complementary, research organizations, led by the top scientist from each company, will provide sharper focus, less bureaucracy and clearer accountability in drug discovery," Pfizer Chief Executive Jeffrey Kindler said in a news release. Pfizer's roughly \$62 billion acquisition of Wyeth announced in January is expected to close in the third quar-

ter.

The new company will be made up of nine businesses, a continuation of Mr. Kindler's push to make its units nimbler and more accountable. The new businesses include primary care, vaccines, oncology, consumer and nutritional products. Pfizer, which sold its consumer-health unit to Johnson & Johnson in 2006, is making a renewed effort to diversify its businesses as blockbuster breakthroughs are fewer and further between.

In addition to Drs. Dolsten, Emini and Pangalos, Pfizer has signed on another five members of Wyeth's top brass.



Martin Mackay

# Tate & Lyle loses ruling on sweetener

BY ERICA HERRERO-MARTINEZ AND MICHAEL CAROLAN

Tate & Lyle PLC suffered a setback when a U.S. court upheld a ruling that leaves its Sucralose sweetener exposed to low-cost generic imports.

The U.S. International Trade Commission in Washington late Monday upheld a September ruling that rejected a Tate & Lyle claim that Chinese manufacturers and six importers had infringed its patents on the manufacturing process for its artificial sweetener Sucralose.

While the patent on Sucralose itself has expired, Tate & Lyle holds a host of patents on its manufacture, which the company says cover all known economically viable routes for making the product, which is also sold under the Splenda brand.

London-based Tate & Lyle filed suit in 2007, after products containing Sucralose it didn't make began appearing in U.S. stores. Tate & Lyle manufactures Sucralose for food companies, while Johnson & Johnson's McNeil Nutritionals owns the Splenda brand and the tabletop business.

Sucralose has been a key element of Tate & Lyle's portfolio. With a monopoly on its production, the company has pushed Sucralose hard in recent years as the company sought to transform itself from a commodity-driven concern into a value-added food producer with more control over pricing and margins. Even though Sucralose accounts for only 4% of Tate & Lyle's sales, it generates 21% of the company's profit thanks to its strong margins.

Tate & Lyle said it will review it and evaluate options for appeal.

## GLOBAL BUSINESS BRIEFS

## Segro PLC

## REIT successfully places \$738 million rights issue

U.K. industrial-real-estate investment trust Segro PLC said it successfully placed its £500.6 million (\$738 million), 12-for-1 rights issue. Shareholders representing 95% of the new shares had subscribed to the issue early Tuesday, and Segro's book-runners later found buyers for the remaining 247 million shares. Segro joined a list of property companies that have raised cash to weather the financial crisis that has seen valuations plummet and vacancy rates rise as tenants move to cheaper premises or have gone out of business. Segro said it will use the proceeds of the rights issue to help cut its debt. The capital raising comes just days after the company secured a deal with banks that provides new terms on £1.7 billion of debt to help it through the downturn.

## AstraZeneca PLC

AstraZeneca PLC on Tuesday said it filed a lawsuit in a U.S. court seeking a patent-infringement ruling against Apotex Inc. after the Canadian drug maker won approval for a generic version of the children's asthma medication Pulmicort Respules. The U.K. pharmaceutical company is also seeking to stop sales of Apotex's generic drug until the patent-infringement case is concluded. The U.S. District Court of New Jersey will hear oral arguments on the motion April 16. AstraZeneca said the U.S. Food and Drug Administration granted approval for a generic version of Pulmicort Respules to Apotex on March 30. "The lawsuit follows Apotex's indication of intent to market a generic version of AstraZeneca's Pulmicort Respules in the U.S. prior to the expiration of AstraZeneca's patents," the London-based company said.

## PartyGaming PLC

PartyGaming PLC reached a settlement with authorities over its defunct operations in the U.S., with the online-gambling company agreeing to pay a \$105 million fine. Under the agreement, the U.S. attorney's office for the Southern District of New York won't prosecute PartyGaming or its subsidiaries for providing Internet gambling to customers in the U.S. before the federal government's ban of the industry in October 2006. PartyGaming will pay the fine in eight installments until Sept. 30, 2012. The payments will come from the U.K.-listed company's existing resources. Separately, PartyGaming said first-quarter revenue fell 22% to \$100.1 million from \$128.9 million a year earlier, hurt by the U.S. currency's strength against the euro, pound and Canadian dollar.

## Esprit Holdings Ltd.

Esprit Holdings Ltd. said Ronald Van der Vis will succeed Heinz Krogner as chief executive of the fashion retailer. Mr. Van der Vis, 41 years old, will become a director of the company on June 22. By Nov. 1, following a transition period, he will take over as CEO. He has been CEO of optical retailer Pearle Europe BV for five years. Mr. Krogner will step down as chief executive but will stay on as executive chairman. Mr. Van der Vis's appointment is the latest in a series of changes in Esprit's top management, which has sparked investor concern about the firm's stability.

## France Télécom SA

France Télécom SA said Tuesday the Egyptian stock-market regulator has rejected its takeover offer for mobile operator Egyptian Co. for Mobile Services. France Télécom said it offered to buy the 49% in ECMS it doesn't own at a premium of 33.1% to the stock's April 5 closing price and a 54.2% premium to the average closing price of the past six months. "It seems that our offer wasn't high enough in the eyes of the regulator," said a France Télécom spokesman. He declined to say whether France Télécom would consider making a higher offer. France Télécom late Sunday said that a ruling by an arbitration court ordered Orascom Telecom Holding SAE to transfer its 28.75% stake in mobile operator Mobinil to France Télécom by April 10. France Télécom already owns the other 71.25% of Mobinil.

## Rio Tinto Ltd.

Rio Tinto Ltd. said it is slowing expansion of an alumina refinery and cutting bauxite output from a mine, which will result in the loss of more than 700 positions for contractors and permanent staff. The slowdown at the Yarwun alumina refinery in Queensland state means completion of the \$1.8 billion expansion, which will lift the plant's alumina output to 3.4 million metric tons a year from 1.4 million tons, will be pushed back a year to the second half of 2012. At its Weipa mine, Rio Tinto said it plans to cut annual bauxite output to 15 million tons from 19.4 million last year. The latest curtailment comes on top of deep cuts already made by Rio and other aluminum producers as the global recession has sent prices tumbling 55% from their highs last year.

## GM Daewoo Auto

GM Daewoo Auto & Technology Co., the South Korean unit of General Motors Corp., swung to a net loss in 2008 amid low demand and investment losses. GM Daewoo Vice President Jay Cooney said high oil prices last year hurt sales of sport-utility vehicles, while rising manufacturing costs and volatile foreign-exchange rates hurt profit. The company posted a net loss of 875.69 billion won (\$670.8 million) last year, compared with a net profit of 540.51 billion won a year earlier. Sales fell 1.6% to 12.31 trillion won, while operating profit declined 39% to 290.31 billion won. Losses from derivative investments jumped to 2.33 trillion won from 206.45 billion won.

## Total SA

French oil company Total SA on Monday said it was considering delaying its decision to build the \$9 billion Canadian-dollar (\$7 billion) Joslyn oil-sands mine in northern Alberta. The move is the latest by an international oil company to delay investments to negotiate better deals with contractors. On Monday, the Qatari oil minister said a natural-gas-development project with Exxon Mobil Corp. would be pushed back to benefit from a drop in construction costs. Total spokesman Kevin Church said: "We're looking at costs...and design and discussing these issues with our contractors....Part of the strategy [in delaying the investment decision] is talking to suppliers as the cost of raw materials has come down, to get the best deal."

—Compiled from staff and wire service reports.



# ECONOMY & POLITICS

Shifting priorities | Winners and losers in the proposed U.S. defense budget

## Winners:



**F-35 Joint Strike Fighter:** Buy 30 planes in 2010, up from 14 in 2009



**Predator drone:** Increase funding of unmanned aircraft widely used in Iraq and Afghanistan



**Littoral Combat Ship:** Buy three vessels in 2010, up from two in 2009



**Theater missile-defense systems:** Add \$700 million in funding

## Losers:



**F-22 Raptor:** End production of the aircraft after 187 produced



**C-17 airlifter:** End production after 205 built



**VH-71 presidential helicopter:** Terminate the program that is late and over budget



**CSAR-X helicopter:** End troubled effort to replace Air Force search and rescue fleet

Sources: Defense Department; Photos (clockwise from top left): Defense Dept.; Associated Press; Lockheed-Martin (2); Boeing (rendering); Boeing; Defense Dept. (2)

# U.S. defense overhaul faces opposition

Contractors, lawmakers and unions are worried about loss of weapons-manufacturing jobs under Gates plan

BY AUGUST COLE  
AND YOCHI J. DREAZEN

WASHINGTON—U.S. Defense Secretary Robert Gates's proposed shake-up is expected to stoke debate about the importance of weapons-manufacturing jobs and appears to mark a turning point for an industry that enjoyed record business during the Bush administration.

Mr. Gates said Monday that he planned to halt new purchases of the F-22 Raptor fighter jet from Lockheed Martin Corp. after delivery of 187 of the aircraft already ordered. He also said there would be no more orders for Boeing Co. C-17 transport planes beyond the 205 planned.

Both companies said his decision would prompt thousands of layoffs, handing congressional opponents a potentially potent political weapon. Mr. Gates tried to preempt criticism, saying Monday that any job losses would largely be offset by new positions to be created by companies receiving additional Pentagon money in coming years.

Mr. Gates proposed boosting certain programs, including Lockheed Martin's F-35 Lightning fighter jet, as well as a variety of unmanned aerial vehicles.

The Army's \$200 billion Future

Combat Systems program, led by Boeing and SAIC Inc., would be trimmed through a call to cancel an \$87 billion high-tech ground-vehicle effort. Mr. Gates said plans for the program "do not adequately reflect the lessons of counterinsurgency and close-quarters combat in Iraq and Afghanistan."

Other cancellations included an advanced satellite communications program, and the replacement of Air Force search-and-rescue helicopters. Shipbuilding is also getting trimmed, with the Navy holding off on a futuristic cruiser program. An older destroyer design will go back into production.

The International Association of Machinists and Aerospace Workers denounced the decision to discontinue the F-22 jet as unwise. "We simply cannot afford to cannibalize our national defense to repair damage caused by reckless financial institutions and greed-crazed corporate executives," union president Tom Buffenbarger

said in a statement.

Contractors, including Boeing and Lockheed, said they were still studying Mr. Gates's decisions.

Mr. Gates's plans have clear international implications. His decision to increase spending on the F-35, which involves European nations and defense companies, from \$6.8 billion in 2009 to \$11.2 billion in 2010 secures the program's future and will help keep costs in check for such allies as the U.K. and the Netherlands.

Mr. Gates also said he intended to cancel the Lockheed-led effort to build a new fleet of Marine One helicopters for the president.

Finmeccanica's AgustaWestland is a partner on that program, which had called for heavily modifying a US101 helicopter into a flying limousine. Mr. Gates said he decided to cancel the program because costs doubled to more than \$13 billion and the schedule slipped to six years overdue. Finmeccanica said in a statement that the move

would have no impact on the company's financial guidance and is in no way related to the technical characteristics of the helicopter."

Defense stocks rallied Monday after the budget announcement, ending a drawn-out period of uncertainty. Lockheed shares rose \$5.97, or 8.9%, to \$73.28; Northrop Grumman Corp. gained \$3.96, or 9%, to \$47.94; Boeing was up 47 cents, or 1.3%, at \$38.16; General Dynamics Corp. rose \$2.90, or 6.8%, to \$45.56; Raytheon Co. was up \$3.19, or 8.3%, at \$41.66.

One big test for the defense plan will be winning over key Democratic lawmakers. Pennsylvania Rep. John Murtha, chairman of the House Appropriations Defense Subcommittee, said the the plans were an important "first step in balancing the department's wants with our nation's needs," but would require careful review.

Missouri Democratic Rep. Ike Skelton, chairman of the House Armed Services Committee, said

the proposed budget was a "good-faith effort," but that "the buck stops with Congress."

Connecticut Sen. Joe Lieberman and Oklahoma Sen. Jim Inhofe urged in a letter "not to allow deep cuts in U.S. missile defense programs that are critically important to protecting our homeland and our allies against the growing threat of ballistic missiles." The Missile Defense Agency budget is being cut by \$1.4 billion.

Beyond military hardware, Mr. Gates said the Pentagon plans a 5% increase in the number of special operations forces, or 2,800 people. He called for plans to recruit more cyber-warfare experts, and to add Army helicopter pilots and maintenance crews, in a move that will help support operations in Afghanistan.

Mr. Gates also plans to hire more than 30,000 new civilian officials over the next five years, gradually reducing the number of contractors to 26% of the Pentagon work force, down from a current 39%.

## Pakistani, U.S. officials call for mutual trust

ASSOCIATED PRESS

ISLAMABAD—Pakistani and U.S. officials on Tuesday emphasized the need for trust between their countries to counter the threat from al Qaeda and the Taliban.

U.S. envoy Richard Holbrooke and Adm. Mike Mullen of the U.S. Joint Chiefs of Staff were visiting Pakistan on the heels of President Barack Obama's announcement of plans to reinvigorate the war in Afghanistan by sending more troops to the region and increasing aid to Pakistan.

Pakistani leaders say they welcome billions more dollars in assistance, but Mr. Obama's insistence that the money won't come without conditions has rankled some here and underscored a trust deficit between the two camps.

"We can only work together if we

respect each other and trust each other," Pakistani Foreign Minister Shah Mahmood Qureshi said during a joint news conference.

Mr. Qureshi reiterated his government's official opposition to American air strikes on targets in Pakistan, attacks that have angered many in Pakistan.

Mr. Qureshi said Pakistan has "red lines" that shouldn't be crossed, notably any sort of U.S. ground operation on its territory.

U.S. officials have complained that the country's spy agency still has ties to some militant groups, something Pakistan denies.

In an interview Tuesday, Pakistani President Asif Ali Zardari called it "a supposition" that Pakistan's top spy agency had helped the Taliban stage attacks in Afghanistan.



Pakistan's Foreign Minister Shah Mahmood Qureshi, left, appeared with Richard Holbrooke, U.S. special envoy to Afghanistan and Pakistan, in Islamabad Tuesday.

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## ECONOMY &amp; POLITICS

# World Bank warns Asia

*Growth forecast cut and 'painful surge' of job losses is seen*

BY MICHAEL S. ARNOLD

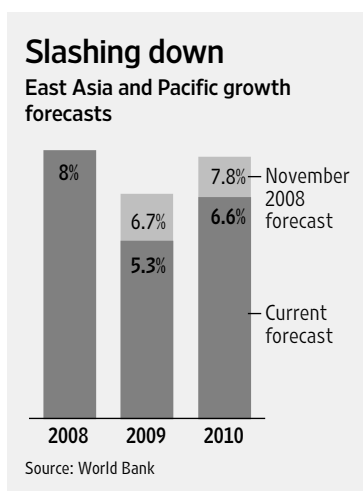
TOKYO—The World Bank cut its 2009 economic growth forecast for developing East Asia to 5.3% from 6.7% and warned of a "painful surge" of unemployment as the global recession hits home.

In its semiannual update on East Asia and the Pacific region, the bank reiterated its projection that China's economy will expand 6.5% this year and called the prospect that China's economy will bottom out midyear, as its massive stimulus package kicks in, a "ray of hope" for the region.

But a sustainable recovery will depend on the advanced economies that take most of Asia's exports, and recovery there isn't expected until 2010, said the report.

The projected 5.3% growth rate for developing East Asia this year marks a sharp slowdown from an estimated 8% expansion in 2008 and the 11.4% growth rate in 2007, but still leaves the region as the fastest growing part of the world economy.

Excluding China, the East Asian region is expected to grow just 1.2%



this year, a "lackluster performance" that places it behind the Middle East and North Africa, South Asia and Sub-Saharan Africa, the bank said.

Developing East Asia includes China, Indonesia, the Philippines, Thailand, Vietnam, Cambodia, Laos, Mongolia, Papua New Guinea and the island economies of the Pacific.

The World Bank last week forecast the global economy would contract 1.7% in 2009, for the first global decline since World War II.

With Asia's increased integration into the global economy, "the impact of the crisis in the advanced economies was transmitted to the

economies of the region with unusual speed," the report said.

As world-wide demand declines, exports and industrial production across the region are falling, leading to factory closures, job losses and lower wages, the report said.

Unemployment in the region is reported to have increased to 24 million people in January, up one million from a year earlier, the World Bank said. But it said the official numbers capture "only a small part of the deteriorating employment situation" and warned of "the beginning of a painful surge in unemployment throughout the region."

The bank praised Asian governments for reacting swiftly, cutting interest rates and taking other steps to ensure adequate liquidity in their financial markets. Governments in developing East Asia have announced stimulus packages equivalent to 3.6% of their combined GDP, and are expanding social programs.

The World Bank said Asia's rapid growth of recent years may be a thing of the past. Even when global demand picks up, the report said, "the region's outward-oriented economies are unlikely to enjoy the same success in the medium term as they did in the previous decade," as the developed world tries to save more and consume less.

# Revised euro-zone GDP points to a slow recovery

BY NICHOLAS WINNING

LONDON—The record contraction in the euro zone's economy in the fourth quarter was even sharper than initially estimated, fueling fears that it will take longer for the currency bloc to recover from recession.

Gross domestic product contracted 1.6% from the third quarter and 1.5% from a year earlier in the final three months of 2008 in the 15 countries that then used the euro—the biggest contraction by both measures since records began in 1995, the European Union's Eurostat statistics agency said. The euro zone added a 16th country, Slovakia, on Jan. 1.

Eurostat's preliminary reading, issued a month ago, had shown fourth-quarter GDP falling 1.5% from the third quarter and 1.3% from the fourth quarter of 2007.

"Worryingly, it is far from inconceivable that euro-zone GDP contraction was even deeper in the first quarter of 2008, given largely dire data and survey evidence," said Howard Archer, chief U.K. and European economist at IHS Global Insight.

The euro zone slipped into its first recession in the third quarter after registering a second consecutive

quarterly drop in GDP. In the third quarter, euro-zone GDP fell 0.3% from the second quarter, but grew 0.6% from the year-earlier period.

Eurostat said annual euro-zone economic growth slowed to 0.8% for all of last year, from 2.6% in 2007. That compares with a 1.1% increase in GDP in the U.S. last year and a 0.6% contraction in Japan, Eurostat said.

The revised fourth-quarter GDP figures are likely to fuel concerns that the recession will be deeper and more protracted than expected.

They are also likely to increase pressure on the European Central Bank to loosen monetary policy further.

The ECB cut its main interest rate to 1.25% last week, down from 4.25% in October, but it has been less aggressive than the U.S. Federal Reserve and the Bank of England. ECB President Jean-Claude Trichet has indicated that rates could drop again.

The fourth-quarter figures showed exports were 6.7% weaker than the third quarter as the credit crisis hit demand in the euro zone's main trading partners, while imports dropped 4.7%. That compares with a 0.2% drop in exports and 1.3% rise in imports between July and September.

# Economists debate recovery's shape

BY TOM BARKLEY

WASHINGTON—Two former chief economists of the International Monetary Fund disagreed Tuesday on whether the eventual global recovery will take the shape of a solid "V" or weak "L."

Simon Johnson and Michael Mussa, both senior fellows at the Peterson Institute for International Economics, agreed that the world economic recession is likely to be the worst since World War II. However, they differed not just on the outlook for the economy—but on the fundamental nature of the crisis itself.

Mr. Mussa, who served as chief economist for the IMF from 1991 to 2001, expects the world economy to remain true to the historical trend that a steep downturn in growth is followed by a sharp upturn. Such recoveries are referred to as V-shaped, as a result of how they look on a graph.

Mr. Mussa sees a 0.8% contraction in the world economy this year. But a recovery will likely be under way by year's end, he says, with glo-

bal growth bouncing back at a pace of 3.7% next year.

While the exact timing of the recovery may be debated, "when it starts, I think it is far more likely than that the U.S. economy and the world economy will see the V for victory," Mr. Mussa said at a Peterson Institute conference.

While Mr. Mussa sees the current downturn in the traditional vein, with global demand snapping back from a negative shock, Mr. Johnson views the crisis as part of a more sinister story in which the power of international banks has distorted the business cycle.

Mr. Johnson, who was the IMF's chief economist in 2007 and 2008, argued that the amount of economic and political power the financial sector has amassed in the U.S. is a "dangerous" development that has put the global economy in uncharted waters.

"The industrial countries, particularly the U.S., have become a lot more like emerging markets than we've ever seen before," said Mr. Johnson.

Thus, he sees the world economy struggling to recover over the next couple of years. For 2009, he sees a 1% contraction, fourth quarter versus fourth quarter, with the economy remaining essentially flat in 2010.

Mr. Mussa agreed that the current recession is different than others in certain ways. "But that does not repeal all of the regularities of macroeconomic behavior that we've been able to observe and document over the past 50 to 100 years," he said.

In fact, Mr. Mussa views his forecast as conservative, since the behavior of previous U.S. economic recessions in the postwar period would suggest a growth rate of 7.7% in the first six quarters of a recovery. Instead, he is projecting 6.2% growth in the coming recovery, citing weaker expectations for consumer spending and infrastructure investments.

Mr. Mussa's forecast is also closer to the IMF's latest estimates for a contraction of between 0.5% and 1% this year, followed by a rebound of 1.5% to 2.5% in 2010.

# South Korean ex-president implicates wife in scandal

BY SUNGHA PARK

SEOUL—A political bribery scandal involving figures from South Korea's two major political parties took a new twist Tuesday when former President Roh Moo-hyun announced on a Web site that his wife received money from a key figure in the case.

The development is a surprising turn for Mr. Roh, who until now appeared to be the first South Korean president since the country became a true democracy in the late 1980s not to be tarnished by a bribery or political influence scandal.

Mr. Roh posted the announcement several hours after one of his former aides, Chung Sang-moon, was arrested and charged with taking hundreds of millions of won from Park Yeon-cha, chairman of Taekwang Industrial Co., a shoe manufacturer.

In his Web posting, Mr. Roh said his wife, Kwon Yang-suk, "asked for, received and used the money" for which Mr. Chung was arrested. "I'm worried if he stated that he did it,"

Mr. Roh wrote. "The charge shouldn't be on Mr. Chung, but on us."

Mr. Roh said the money was used to repay debts. He indicated he would cooperate with investigators and believed they would reveal more details.

"I'm overwhelmed by shame," Mr. Roh wrote. "I'm more ashamed to those who have trusted and supported me. I sincerely apologize."

The Supreme Prosecutors' Office couldn't be reached to comment late Tuesday.

Mr. Park was arrested in December on tax evasion and bribery charges for making payouts to several people in Mr. Roh's administration as well as other politicians. In recent weeks, prosecutors have interviewed more than a dozen prominent political figures.

In December, Mr. Roh's older brother, Roh Gun-pyeong, was arrested on charges for allegedly colluding with Mr. Park to broker the purchase of an ailing securities firm from a state-run company in 2006.

# Ireland squeezes more in new budget

BY QUENTIN FOTTELL

DUBLIN—Ireland's government delivered a painful emergency budget that doubled income tax surcharges, cut spending and created a toxic asset company to house banks' bad debts.

"I want to assure the Irish people that we have the capacity and your government has the will to bring us out of this period of severe economic distress," Irish finance minister Brian Lenihan told parliament Tuesday. "We have faced adversity in the past and we have prevailed."

So far this year, the government

has cut public spending by €1.8 billion (\$2.41 billion), primarily with cuts in public services. The latest cuts mean an additional €1.5 billion in gross public spending, and additional revenue of €1.8 billion.

Mr. Lenihan offered a bleaker picture of the economy than the government unveiled just last week. He predicted that gross domestic product would contract by up to 8% in 2009, worse than the 6.75% contraction in last week's pre-budget outlook. He said he expects consumer prices to fall 4% in 2009. Without this budget, he said, the general government deficit would have been 12.75% of GDP.

The emergency budget will close that gap to 10.75%.

Last week, euro-zone finance ministers called on Ireland and Greece to take immediate steps to control their rising budget deficits this year, or face the possibility of sanctions or fines.

Ireland's government chose to leave its 12.5% corporate-tax rate unchanged. The low rate has been crucial in drawing U.S. companies to Ireland. However, Mr. Lenihan doubled income-tax surcharges, raised capital gains and capital acquisition taxes, and increased excise duties on cigarettes and alcohol.

# World Bank cleanup in spotlight

BY BOB DAVIS

WASHINGTON—When the World Bank signed Leonard McCarthy as its anticorruption czar last year, the bank looked to overcome divisions over how it handles graft probes.

But allegations that Mr. McCarthy in his old job as a South African investigator pursued a political agenda threaten to re-open old wounds. During the tenure of former World Bank President Paul Wolfowitz, critics charged the institution played favorites in deciding which developing-nation projects to halt because of concerns of graft.

An outside review panel found the Department of Institutional In-

tegrity under Mr. McCarthy's predecessor, Suzanne Folsom, was marred by "serious operational issues," although it praised her professionalism. Robert Zoellick, who succeeded Mr. Wolfowitz, has vowed greater transparency.

Nancy Boswell, president of Transparency International-USA, which tracks development issues, said it was too early to judge the charges against Mr. McCarthy. "Smear campaigns against corruption fighters are, unfortunately, all too common," she said.

During his year at the World Bank, Mr. McCarthy has increased the number of debarments of companies engaged in corruption.

## ECONOMY &amp; POLITICS

# Less zeal for U.S. schools

Foreign applications to graduate programs slow amid recession

BY S. MITRA KALITA

The number of Chinese and Middle Eastern students applying for fall admission to U.S. graduate programs surged, while applications from India and South Korea fell, according to a survey released Tuesday by the Council of Graduate Schools.

The council, which represents more than 500 higher-education institutions in the U.S. and Canada, said foreigners' applications for 2009 graduate-school admissions rose 4% from the year before. That compares with increases of 6% in 2008, 9% in 2007 and 12% in 2006.

The mixed results point to a meeting of new realities in the global economy: On the one hand, some countries have improved their educational systems to keep students closer to home or woo those from other countries who might have otherwise chosen the U.S. On the other, the global recession—and some signs of resistance to employing immigrants in the U.S.—means U.S. tuitions are increasingly out of reach for some, while others fear jobs won't be waiting for them upon graduation.



Chinese visitors at an educational exhibition in Shanghai in March learn about San Diego State University.

"Historically, U.S. graduate schools were the graduate schools for the world," said council president Debra W. Stewart. "Now, we cannot simply assume it's going to be a matter of turning on the spigot and the most talented people in the world will flow in." She and others in higher education say it is too soon to know the true effects of the financial crisis on higher education until enrollment numbers are available.

The council survey of U.S. institutions, which fielded more than 400,000 applications in all, showed growth of applications from China along with the Middle East and Turkey, up 16% and 20% from 2008, respectively. But applications from India and South Korea fell 9% and 7%, respectively.

"The global economy is really impacting students' ability to come to the United States," Ms. Stewart noted. "Students in India are now finding it difficult to borrow money." She cited tighter lending as another reason that doctoral programs, which typically offer stipends and assistance, would be luring more students than master's programs.

If the trend persists, it will mean a subtle but significant change on U.S. campuses, which have come to rely on foreign students to fill their seats, particularly in such depart-

ments as science and technology.

The council says declines in foreign applicants have come largely at schools with relatively few foreign students. The University of Kansas noted a drop in foreign students' applications, said assistant dean John Augusto, who works in the office of research and graduate studies, "but fortunately not as big a drop as some institutions." Mr. Augusto said that about 2,000 of the university's 29,000 students are from abroad. Admissions officials at the University of Southern California and New York University, which have among the largest international-student populations, say they have not seen a drop-off.

Other countries, such as the U.K., Australia and Canada, have enacted policies that make it easier for students to go from the classroom to the workplace without reapplying for a visa, said Ursula Oaks, a spokeswoman for the Association of International Educators. Meanwhile, amid a high unemployment rate, some U.S. government agencies and recent legislation are discouraging recruitment of foreign workers.

"There's concern that international students have about finding jobs in the U.S. economy after they graduate," Ms. Oaks said.

# Chinese firm is charged over deals to help Iran

BY CHAD BRAY AND MAYA JACKSON RANDALL

A Chinese company and its manager were charged in the U.S. for allegedly engaging in illegal financial transactions through American banks to help Iran import a variety of banned materials, including metal alloys that could be used for nuclear weapons and ballistic missiles.

At a news conference Tuesday, Robert Morgenthau, the district attorney for New York's borough of Manhattan, announced a 118-count criminal indictment against Li Fangwei, a Chinese citizen, and his company, Limt Economic & Trade Co., and its various affiliates. The charges include falsifying business records, which would carry a prison sentence of as long as four years, and conspiracy.

The U.S. Treasury Department, which worked closely with Mr. Morgenthau's office, said Tuesday it was freezing Mr. Li's U.S. assets and the assets of Limt companies, which sell metal alloys and minerals, including high-strength metals and sophisticated military materials.

"This is a case about selling banned materials and contraband by a Chinese company to Iran by using the U.S. financial system," Mr. Morgenthau said.

The district attorney said he intends to ask the Chinese government's assistance in having Mr. Li, 36 years old, of Liaoning province, extradited to the U.S. to face the charges.

Mr. Li, who is also known as Karl Lee, doesn't have an attorney in the U.S. He couldn't immediately be located for comment Tuesday.

Mr. Morgenthau said the company had been banned since 2006 by the Treasury Department from engaging in financial transactions in the U.S. for its role in assisting Iran's nuclear-proliferation program.

Limt used aliases and front companies in order to send and receive dozens of illegal payments through the U.S. between November 2006 and September 2008, Mr. Morgenthau said.

The firm was assisted by two Chinese banks in the transactions, and his office is looking into their role in the transactions, the district attorney said, adding that the probe is continuing.



Robert Morgenthau

# Peru's Fujimori is sentenced to 25 years in murder case

ASSOCIATED PRESS

LIMA, Peru—A special tribunal sentenced former President Alberto Fujimori to 25 years in prison after convicting him of what it called "crimes against humanity"—death-squad activities during his increasingly autocratic 10-year rule that ended in 2000.

The 70-year-old former Peruvian leader, who remains popular for rescuing Peru from the brink of economic and political collapse in the early 1990s, was convicted of 25 murders committed by a military hit squad in the early 1990s, and the kidnappings of a businessman and a journalist.

Presiding Judge Cesar San Martin told a hushed courtroom that there was no question Mr. Fujimori authorized the creation of the Colina military death squad that killed

some 50 people amid a lengthy struggle to crush a Maoist insurgency.

Mr. Fujimori apparently anticipated a guilty verdict. He sat alone taking notes as the verdict was read after a 15-month televised trial that produced a 711-page sentence.

Outside the Lima police base where the trial was being held, pro- and anti-Fujimori activists fought with sticks, fists and rocks after the verdict was announced, amid chants of "Fujimori innocent!" and "Fujimori killer!" Some 30 relatives of victims clashed with about 50 Fujimori supporters. Police broke up the melee and no injuries were immediately reported.

Mr. Fujimori already had been sentenced to six years in prison for abuse of power and still faces two corruption trials on charges including bribing lawmakers.

# Zapatero shuffles economic team

BY JONATHAN HOUSE

MADRID—Spanish Prime Minister José Luis Rodríguez Zapatero reshuffled his cabinet in an effort to renew his government's approach to Spain's economic crisis and improve his Socialist party's position ahead of European Parliament elections.

In the most important change, Public Administration Minister Elena Salgado will replace veteran Finance Minister Pedro Solbes.

"The fight against the economic crisis is our top priority," Mr. Zapatero said.

Mr. Solbes, 66 years old, is a former European commissioner for economic and monetary affairs and three-time Spanish finance minister.

At a recent meeting with journalists and business leaders, a visibly fatigued Mr. Solbes jokingly said he envied departing Justice Minister Mariano Fernández Bermejo for being an "ex-minister," a comment that opposition politicians criticized as showing a lack

of will to deal with the crisis.

The Socialists have seen their political fortunes dwindle in recent months as Spain suffers one of the EU's most severe economic downturns. After posting a nearly 4% growth rate for several years, Spain's economy slowed to 1.2% growth last year. The Bank of Spain

**The downturn has done damage to the political fortunes of Spain's Socialists.**

expects the economy to contract by 3% this year. The country's 15.5% unemployment rate in February was nearly twice the EU's 7.9% rate.

The Socialists lost control of the Galicia regional government to the opposition Popular Party in March. Its next electoral test comes June 7, with

elections to the European Parliament.

Ms. Salgado, 59 years old, who is also a veteran of Socialist-led governments in Spain, is known as the architect of legislation that banned smoking in public places while she was health minister from 2004 to 2007. She has also held high-level positions at the finance and industry ministries.

Mr. Zapatero said Ms. Salgado's efficiency was a key reason in her selection. As head of the public administration ministry, Ms. Salgado played a key role in overseeing the Spanish government's most recent economic stimulus package: €8 billion (\$10.7 billion) for infrastructure projects by city governments.

"In an economic crisis it is very important to, first, plan the response and, second, for the measures taken to be efficient and quickly implemented so that their impact is felt in the economy," Mr. Zapatero said.

# Malaysian opposition gets a lift

ASSOCIATED PRESS

BUKIT GANTANG, Malaysia—Malaysia's opposition won two of three by-elections held Tuesday, dealing a blow to Prime Minister Najib Abdul Razak, who took office last week with pledges to carry out wide-ranging government and social reforms.

Tuesday's results don't change the balance of power at the federal or state levels but serve as an unofficial referendum on Mr. Najib's popularity. The ruling National Front coalition downplayed the loss, saying the new premier was yet to make his mark.

"The feel-good factor from the power transition is still too new and has not sunk in," said Muhyiddin Yasin, who is expected to be appointed deputy prime minister in the new cabinet to be announced this week.

"I am confident that when the new leadership begin their duties, and when reforms are implemented, it will convince the people," he said.

Tuesday's elections were to fill one seat in Parliament from the Perak state, and one seat each in the state parliaments of Kedah and Sarawak.

The by-elections were to fill vacancies left by two deaths and one resignation.

The National Front won the Sarawak race, but lost the other two. The Perak federal seat was won by the Pan-Malaysian Islamic Party, while the Kedah state seat was won by the People's Justice Party.

The two parties are partners in the People's Alliance coalition led by opposition leader Anwar Ibrahim.