**Economy & Politics:** Is the U.S. recovery going to be fast, slow or something else?

# THE WALL STREET JOURNAL.

VOL. XXVII NO. 138 — EUROPE — WEDNESDAY, AUGUST 19, 2009

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## What's News

**GM said it reached a deal** to transfer its unprofitable Swedish unit Saab to a group led by Swedish supercar maker Koenigsegg Automotive, but the agreement hinges on obtaining $412 million in additional financing. Page 5

■ **The British inflation rate** isn't slowing as much as the Bank of England might expect. U.K. consumer prices rose 1.8% in July. Page 2

■ **London property investors** are emerging and finding willing sellers as the market stabilizes. Page 3

■ **New-home construction** and permits fell in the U.S. in July, but single-family-home starts remained strong. Page 2

■ **U.S. and European stocks** staged a partial rebound from their recent drubbing, aided by retailers' earnings. Page 18

■ **The U.S. is conducting** criminal investigations of over 150 Americans who may have evaded taxes with UBS accounts. Page 19

■ **PetroChina signed** an LNG deal with Exxon Mobil valued at $41.1 billion. The gas will come from Australia's Gorgon field. Page 20

■ **The IMF's chief economist** said the global recovery has begun, and to sustain it, the U.S. must focus on exports and Asia on imports. Page 3

■ **Officials said** they kept the location of the ship Arctic Sea quiet to protect the hijacked crew, adding that eight suspects had been arrested.

■ **The owner** of a Russian hydroelectric plant said it was doubtful any of the 64 workers still missing after an accident would be found alive.

■ **The death toll** from the suicide bombing of a police station in Russia's North Caucasus rose to 21, with nine police officers still missing.

■ **Northern Rock stopped** payment of coupons on some subordinated debt, handing bondholders a big loss. Page 17

■ **Stockbridge Real Estate** is considering a takeover bid for the management of a $2.6 billion real estate fund run by a Deutsche Bank unit. Page 3

■ **South Africa's GDP** contracted 3% in the second quarter, increasing pressure on Zuma to create jobs. Page 9

■ **Guinea's ruling junta said** a presidential election will be held Jan. 31.

### Editorial & Opinion

**Pay day**
In defense of bankers' bonuses. Review & Outlook. Page 11

Breaking news at europe.WSJ.com

Agence France-Presse/Getty Images

Members of a family hurt in a Kabul suicide attack leave the area. The Taliban took responsibility for two blasts ahead of the Afghan vote.

# Insurgents strike in Kabul

## *Taliban ratchet up violence in effort to disrupt Thursday's Afghan election*

By Matthew Rosenberg And Anand Gopal

KABUL—The Taliban stepped up efforts Tuesday to disrupt Afghanistan's coming election, launching mortar shells at Kabul's presidential palace and attacking a North Atlantic Treaty Organization convoy with a suicide car bomb on the city's outskirts.

Afghan and Western security officials say the militants have shifted from intimidating voters to attacking polling stations that are being set up for Thursday's election. That strategy, which was confirmed by a midlevel Taliban commander interviewed in Kabul, could complicate efforts to secure the vote.

Late Tuesday, Afghanistan ordered Western and domestic media to impose a blackout on coverage of violence during the vote, saying it didn't want Afghans to be frightened away from the polls.

Authorities are planning to set up nearly 7,000 polling stations—many of them in far-flung districts that are thick with Taliban fighters. Afghanistan's overstretched and undertrained army and police force are to take the lead in protecting them, with U.S. and allied forces remaining out of sight in an attempt to reduce Election Day tensions.

The presidential election Thursday, the second since the fall of the Taliban in 2001, is seen as critical to the country's political stability. Afghan and Western officials fear that such attacks could keep people from the polls, especially in the South and East, where the militants are strongest. Their success could diminish the legitimacy of the Afghan government, making it harder for Afghanistan and the U.S. and its allies to overcome the insurgents.

In a bid to stymie the militants, election officials are waiting until Election Day to release the exact location of

*Please turn to page 31*

# Corporate bonds on the rise

By Sonja Cheung And Clare Connaghan

Global corporate bond volumes, excluding banks and other financial institutions, surpassed the $1 trillion mark for the first time as tight bank lending has forced companies to seek funding elsewhere.

Bond volumes passed $1 trillion July 15 as French energy group Éléctricité de France SA sold bonds worth €3.3 billion ($4.6 billion), data compiled by data provider Dealogic showed Tuesday. The volumes have since risen to $1.10 trillion, up 22% from the previous record high of $898.3 billion set in 2007, with more than four months left in the year.

The utility and energy sector has made the largest contribution to the rise, according to Dealogic, with $188.4 billion issued so far this year.

In Europe, where companies have traditionally preferred loans from banks over bonds, the volume of non-financial bond issuance totaled $426.5 billion in the year to date, up 47% from the $290.4 billion raised in 2008, Dealogic said.

Meanwhile, loans have fallen dramatically. The volume of high-value, syndicated loans issued to European borrowers has declined to €235 billion so far this year from €651 billion in 2008, figures from Dealogic showed. On a global basis, loan volumes have dropped to $1.1 billion year to date in 2009, compared with $3 billion in 2008.

A shift to bond financing from loans was already under way in 2006 and 2007 as corporations sought to diversify and looked for longer-term funding, said Jean-Marc Mercier, head of syndicate Europe at HSBC Holdings PLC. Typically, bonds have a longer maturity than loans.

"Even when bank-market conditions ease, corporates may continue to tap the capital markets for new cash," said Mark Lewellen, head of European corporate debt capital markets at Barclays Capital.

J.P. Morgan Chase & Co. is the lead bookrunner globally of all corporate bonds, excluding those sold by financial institutions, this year with a share of 8%.

Citigroup Inc. is ranked second with a 7.3% share, according to Dealogic.

*—Duncan Kerr contributed to this article.*

## Inside

**Graceful in cleats**

Son of star ballet dancers wows U.S. baseball scouts
**Sports**, Page 30

## Markets

4 p.m. ET

| | CLOSE | PCT CHG |
|---|---|---|
| DJIA | 9217.94 | +0.90 |
| Nasdaq | 1955.92 | +1.30 |
| DJ Stoxx 600 | 227.23 | +1.34 |
| FTSE 100 | 4685.78 | +0.88 |
| DAX | 5250.74 | +0.94 |
| CAC 40 | 3450.69 | +0.91 |
| Euro | $1.4106 | +0.24 |
| Nymex crude | $69.19 | +3.66 |

# Germany weighs crunch measures

By Jan Hromadko And Andrea Thomas

COLOGNE, Germany—The German government is weighing new measures to help companies should there be another credit crisis, Economics Minister Karl-Theodor zu Guttenberg said Tuesday.

The disclosure, which overshadowed news of a rise in Germany's ZEW index of investor confidence in August, is the latest warning from a German policy maker on future risks facing the economy.

"We, as the government, are working on possible ways to thwart a feared credit crunch," Mr. Guttenberg said.

The government and central bank have been cautioning against overinterpreting recent signs that Germany is emerging from a yearlong recession. The spate of good news included the announcement last week that gross domestic product rose 0.3% in the second quarter.

Still, Deputy Economics Minister Hartmut Schauerte said the government is looking at ways to make sure companies will continue to have access to the capital they need even if there is another credit crunch. The government wants to ensure nothing clogs the pipeline of insurance for trade credits—a key financial link in the buying and selling of goods—or capital from the bond and equity markets, according to a spokeswoman.

Mr. Guttenberg said that credit conditions would deteriorate again at the beginning of 2010 as balance sheets will have to reflect this year's difficult economic situation—especially for financial-service companies.

Germany's central bank president, Axel Weber, says rising unemployment and insolvencies could hurt banks and trigger a financial crisis.

The government still has a large war chest to help banks in need. The Financial Markets Stabilization Fund, for example, has the legal authority to extend as much as €400 billion ($563 billion) in loan guarantees and €70 billion in capital injections for banks. So far, it has allocated €130.9 billion for guarantees and €21.9 billion for capital injections.

The government will hold a meeting with banks Sept. 1 to look into ways to boost lending activities.

In the latest sentiment survey released Tuesday, the ZEW measure rose 16.6 points

*Please turn to page 31*

## LEADING THE NEWS

# Prices pressure the U.K.

### *CPI rises could force BOE to boost rates sooner than hoped*

By Natasha Brereton

LONDON—British inflation isn't slowing as much as the Bank of England might expect, raising concern U.K. interest rates might need to climb to contain future price increases.

U.K. consumer prices rose 1.8% from a year earlier in July, matching June's annual gain, data from the Office for National Statistics showed Tuesday. That put the consumer-price inflation rate at just below the Bank of England's target of 2%.

The figures suggest that inflation might not slow as much as the BOE has projected, triggering concerns that its Monetary Policy Committee could increase interest rates sooner than expected or not complete the £50 billion ($81.7 billion) in asset buying that it announced this month.

"Monetary policy might need to be tightened sooner than may have been thought likely," said Kerri Maddock, economist at Barclays Capital.

The possibility of rising energy and commodity prices on the back of a global economic recovery could further boost consumer prices.

In many other big economies prices are still falling. Consumer prices in Japan and the euro zone in June dropped 1.8% and 0.1%, respectively compared with a year earlier. In the U.S., prices slipped 2.1% in July.

The prices of U.K. government bonds, or gilts, fell Tuesday as investors responded to the possibility that the Bank of England could start tightening monetary policy sooner than expected.

The pound gained more than half a cent against the dollar, rising to a high of $1.6468 for the day, while the euro fell to a low of 85.80 pence.

Government officials, however, took the figures in stride.

"If you look at all the numbers we've seen over the last few months, they are consistent, I think, with an economy that is coming through what was a pretty severe downturn," said U.K. Chancellor of the Exchequer Alistair Darling.

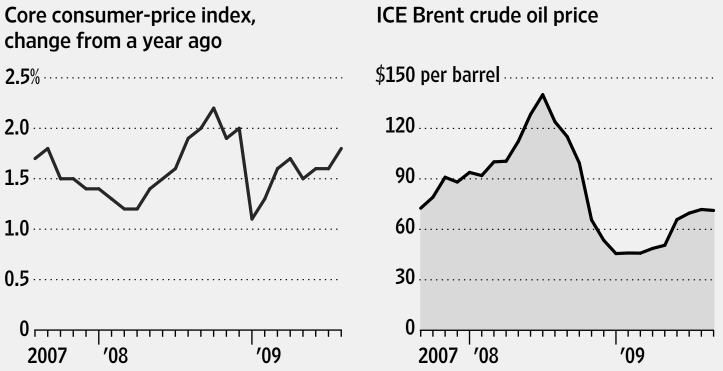
Analysts believe consumer prices may soon weaken, reflecting the impact of last year's high oil prices. But the resilience of discretionary goods prices, as well as the potential for energy price gains and an expected boost from central-bank monetary stimulus, could slow any slide in prices.

The core consumer-price inflation rate—which excludes volatile energy, food, alcohol and tobacco prices— continued to accelerate. It rose to 1.8% in July from 1.6% in June.

"It is now looking much less likely that inflation will fall below 1%," said Alan Clarke, U.K. economist at BNP Paribas.

**Still rising**

U.K. core consumer prices continued to rise in July. Energy prices could add to inflationary pressures as global recovery gathers pace.




Sources: Office for National Statistics, U.K.; CQG

## CORRECTIONS & AMPLIFICATIONS

**As of Tuesday afternoon**, a search was continuing for 64 workers missing after an explosion at the Sayano-Shushenskaya hydropower station in Khakassia, Russia. A Leading the News article in some editions Tuesday failed to include the number of workers missing after the accident.

**South Africa's MTN Group** Ltd. wants India's **Bharti Airtel** Ltd. to increase its cash-and-share merger offer by more than $1 billion, which would represent around a 5% premium to Bharti's original offer, a person familiar with the situation said. A Corporate News article Monday incorrectly said the extra $1 billion represented around a 9% premium.

# U.S. housing data show market is slowly firming

By Sara Murray

New-home construction and permits fell in the U.S. last month, but single-family-home starts remained strong, another sign of stabilization in the housing market.

Multifamily housing starts, a more volatile measure that includes properties such as condominiums and small apartment buildings, pulled overall housing starts down 1% in July from a month earlier to a seasonally adjusted 581,000 annual rate, the Commerce Department said Tuesday. That compares with a 6.5% increase in June.

Construction of single-family homes, though, rose 1.7%, to 490,000, in July after climbing 17.8% in June. Single-family permits, a sign of future construction, rose 5.8%. The rise in construction marked the fifth consecutive monthly gain, showing once again that the housing market is firming up, albeit at a slow pace.

While many economists agree the market already has hit bottom, housing-sector growth may not be a contributor to gross domestic product until next year because it is rebounding from such an extreme low. Singe-family starts are still 73% below their December 2005 peak.

"You don't want to lose sight of the fact that these are extremely depressed levels," said Wells Fargo Securities economist Adam G. York. "It's not necessarily time to break out the champagne and celebrate the boom of a returning housing market."

The increase in single-family homes falls in line with home builders' optimism in the National Association of Home Builders Housing Market Index released this week. The future-sales index rose four points, and prospective-buyer traffic rose three points.

While housing appears to be slowly recovering, a number of factors could cause hiccups. New homes are still competing with readily available, and cheap, foreclosure properties. And an $8,000 tax credit for first-time home buyers, which has helped spur interest in the single-family-home market, expires Dec. 1.

The housing report showed that overall building permits fell 1.8%. Double-digit declines in both housing starts and permits for multifamily homes were down as tight credit for commercial real estate and an abundance of multifamily homes put pressure on the market.

Total housing starts dropped in every region of the U.S. except for the Midwest, where they grew by 12.9%. In the Northeast they dropped 16.3%; in the South, 1.4%; and in the West, 1.6%

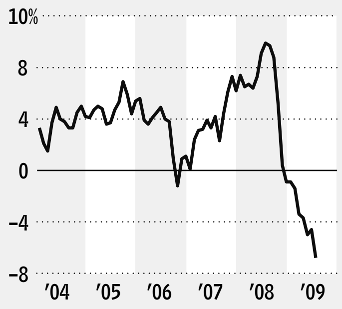
"Monthly data for housing activity are volatile but today's nominal decline stands as a reminder that the economy is still fragile," Rebecca Blank, U.S. undersecretary of commerce for economic affairs, said in a release. "Looking at the big picture, we are confident that we've created the stability necessary to turn things around."

In a separate release Tuesday, the U.S.'s producer price index for finished goods declined 0.9% in July after a 1.8% increase in June, the Labor Department said. The index is down 6.8% from a year earlier, highlighting the low risk of inflation to the economy.

Core prices, excluding food and energy, fell 0.1% last month.

**U.S. producer-price index**

Change from a year earlier




Source: U.S. Labor Department

## INDEX TO BUSINESSES

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



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## 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**

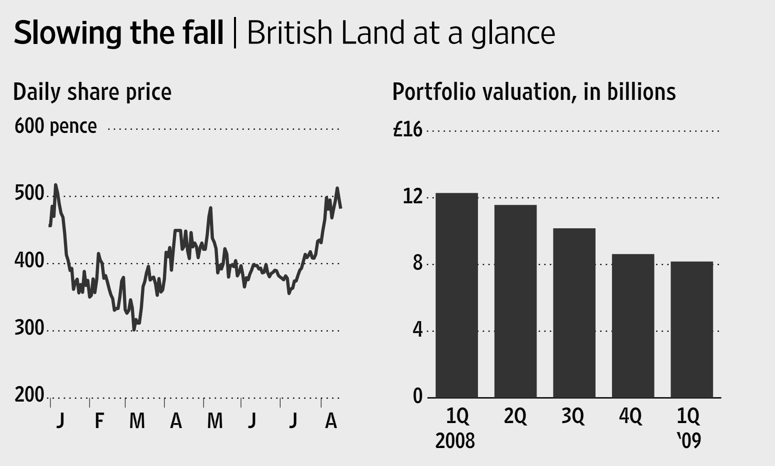
LEADING THE NEWS

# It's deal time in London property market

## *British Land in talks; Brixton finds buyer for Equiton assets*

As London property markets begin to turn the corner, it is beginning to look like deal time again.

*By William Boston, James Mawson and Anita Likus*




Sources: Thomson Reuters Datastream; the company

Bloomberg News

The Broadgate Tower, developed by British Land in London

Investors who have built war chests to scoop up property at attractive prices are coming out of the closet and finding willing sellers. The clearest sign of this happening are the talks between private-equity investor **Blackstone Group** LP and **British Land** PLC, the U.K. property group, about the sale of a 50% stake in Broadgate, a development of prime office buildings in London's City financial district.

Blackstone, which this year closed a €3.1 billion ($4.37 billion) fund to purchase European property, is keen to take a stake in the Broadgate development, according to a person familiar with the matter.

British Land Chief Executive Chris Grigg confirmed that he had received a number of approaches for Broadgate and for the company's stake in the Meadowhall shopping center in Sheffield. He wouldn't elaborate.

"All British Land assets are for sale at the right price," Mr. Grigg said on a conference call to outline the company's first-quarter results Tuesday. "Broadgate is no exception. I can confirm that we have received a number of approaches."

Separately, **Brixton** PLC, the U.K. industrial property real-estate investment trust, said Tuesday that **Equiton GP** Ltd., an industrial-property consortium in which it owns 30%, agreed to sell all the assets in its Equiton Industrial Partnership to **Universities Superannuation Scheme** Ltd. for £196 million ($320.3 million), reflecting a net initial yield of 8.7%. In addition to Brixton, Equiton's shareholders are **Edgar Investments** Ltd., which holds 44%, and **SE Industrial Unit Trust**, which holds 26%.

British Land reported Tuesday that from the peak of the property boom in June 2007 to the end of its fiscal first quarter on June 30, the value of its portfolio fell 41%, to £8.2 billion. Net asset value per share fell 9% compared with the fourth quarter, to 361 pence ($5.90), as the company's properties were hit by declining rents. British Land's shopping centers were hit hardest, with valuations falling 6% in the quarter. Office values fell 4%, while the value of British Land's superstores rose 1%.

Analysts said British Land's results were in line with expectations and showed that British Land had come through the crisis in a strong position.

"They are not under pressure to sell Broadgate, but would do it if offered the right price," said John Lutzius, head of European operations for brokers Greenstreet Advisors.

Over the past few weeks, signs of stabilization in U.K. property markets have increased. British Land's report confirms that the decline in property values has slowed and in some cases is turning around, even in the face of falling rents and rising vacancies.

There is a sense among investors that the market is about to turn. And that is creating interest in doing deals and fueling takeover talk.

In the days before British Land reported its results, speculation emerged that a group of investors including Lakshmi Mittal, the Indian steel magnate, were considering a bid for British Land. According to news reports, the investors had considered bidding for Broadgate but decided instead to consider a bid for the entire group.

The Mittal family couldn't be reached for comment.

The rumors swirling around British Land have raised the possibility that some investors may decide to go after entire property companies rather than investing in individual buildings. The strategy is appealing given that companies might be available at discounts. Also, so much money has been raised for real-estate investment that a bid for a major property company could be possible.

But such deals mightn't be easy to pull off. For one, British Land's portfolio is valued at £8.2 billion. Its shares closed in London on Tuesday at 483 pence, down 2.7%, a premium to its net asset value of 361 pence a share. Any bid would have to be at a big premium and it would appear difficult, if not impossible, to finance a deal of that size in this market.

It also is unlikely that British Land, **Land Securities Group** PLC or any of the property companies that have survived the crisis will be taken over without a fight.

"Do these companies really want to be taken over after this downturn, the recent equity raisings and their long histories?" said Harm Meijer, head of J.P. Morgan Chase & Co.'s European real-estate research team.

How does a company like British Land protect itself from an unwanted takeover? One way would be to expand its assets. Mr. Grigg said the company is no longer a net seller of property and expects to make acquisitions over the next two years.

In the 1990s, British Land took on George Soros as a strategic investor to fend off unwanted suitors and make acquisitions. It still is unclear what the Blackstone Group has in store for British Land, but the €3.1 billion in its new fund is a lot of firepower.

"I would not be surprised to see British Land team up with a capital source—institutions, sovereign-wealth funds or someone else—to make opportunistic purchases," said Greenstreet Advisors' Mr. Lutzius.

# Stockbridge may bid for Deutsche Bank fund

By Anton Troianovski

**Stockbridge Real Estate Funds** is considering a takeover bid for the management of a $2.6 billion real-estate fund run by **Deutsche Bank** AG's real-estate-investment unit.

Some of the top executives of Stockbridge know the fund well. They worked for the Deutsche Bank unit, named RREEF, when the fund made its top-of-the market investments that are now threatening to push the fund into a bankruptcy filing.

Stockbridge Real Estate Funds has expressed interest in making an investment in **RREEF America REIT III**, a move that likely would involve Stockbridge replacing Deutsche's RREEF unit as the manager of the fund, according to DeWitt Bowman, the RREEF fund's lead independent director. He said it was too early to make any deals.

"We're not discouraging any offers," Mr. Bowman said. "We'll take a look at any reasonable offer and evaluate it, and hopefully try to preserve as much of shareholders' value as we can."

By taking over the fund, Stockbridge likely would get management fees as well as a preferred return on the equity it contributes. Stockbridge executives didn't return calls seeking comment.

Like many property-fund managers, Deutsche Bank is scrambling to limit losses from risky, leveraged deals done during the boom. But the German financial firm has two other variables to consider: an assertive board of directors at America III and a third-party fund manager, Stockbridge, that sees an opportunity in the fund's distress.

Deutsche Bank acquired RREEF in 2002. The name had such cachet at the time that Deutsche Bank renamed its real estate, infrastructure and private-equity investing business RREEF Alternative Investments. But many top RREEF executives left the firm in 2007 when a five-year retention pay plan ended.

**The German bank is scrambling to limit losses from risky, leveraged deals.**

Several, including former RREEF Chairman Steve Steppe, partner Mark Carlson and America III manager Doug Sturiale, joined Stockbridge, of San Francisco.

The departures came in the wake of several transactions that are dogging RREEF. Chief among them: an April 2007 deal to build office, retail and residential buildings in downtown Sunnyvale, Calif., which included a $109 million bridge loan that came due earlier this year. Any loan default greater than $30 million triggers a default on the fund's $150 million credit line; RREEF told investors in May that it had at least six such loans coming due in 2009. To rescue the fund, Deutsche Bank presented a recapitalization plan involving a preferred equity offering, lower fees and negotiations with lenders. But people familiar with the fund said the bank has had trouble gaining traction in negotiations with lenders.

Mr. Bowman and three other independent directors have hired financial adviser Lazard Ltd. and law firm Morrison & Foerster LLP to represent shareholders' interests as America III negotiates with creditors, which include Deutsche Bank. Deutsche Bank, meanwhile, has hired J.P. Morgan Chase & Co. and law firm Skadden, Arps, Slate, Meagher & Flom LLP to explore a restructuring.

"We felt, as independent directors, that we needed to act in the interest of the shareholders," Mr. Bowman said in an interview. "Deutsche Bank is also a shareholder, they're also a lender, and there are situations which may arise where we felt independence was important."

Mr. Bowman, a former chief investment officer of the nation's largest pension fund by assets, the California Public Employees' Retirement System, has staked out an independent position for a director at a real-estate fund. The board's move, and Stockbridge's interest in RREEF, is a sign of the turmoil to come for the real-estate-fund business. Mr. Bowman said that, for now, neither RREEF nor the board is looking to replace RREEF as the manager, but that could change if negotiations with lenders don't go well.

"If down the line somewhere a refinancing was in order, then that would be an option," Mr. Bowman said of replacing RREEF.

Not all property funds have independent boards. America III is structured as a private real-estate investment trust, which provides tax advantages as well as a board.

Real-estate funds became darlings of institutional investors during the mid-2000s because they seemed to deliver big returns even as the stock-market rise slowed. But the credit crunch has exposed a flaw in the funds' strategy: It involved increasing amounts of debt and risky development projects. Plummeting property values and nearing debt maturities also have highlighted potential conflicts of interest in a structure where a single financial company can be manager, shareholder and creditor in the same fund.

Many property funds, which raised at least $350 billion from 2002 to 2007, have marked their equity down 50% or more. America III is no exception. It reported a 60% loss for the 12-month period ending March 2009. The San Joaquin County (Calif.) Employees Retirement System has written its $25 million investment in the fund down to a nominal $1,000.

# To sustain gains, U.S. must change tack, IMF says

Reuters News Service

WASHINGTON—The global economic recovery has begun, but sustaining it will require refocusing the U.S. toward exports and Asia toward imports, the International Monetary Fund's chief economist said.

In an article released by the IMF on Tuesday, Olivier Blanchard also said potential economic output may be lower than it was before the financial crisis struck. "The crisis has left deep scars, which will affect both supply and demand for many years to come," Mr. Blanchard said.

U.S. consumption, which accounts for about 70% of the U.S. economy and a large chunk of global demand, wouldn't quickly return to precrisis strength as households cope with losses from the falling housing and stock markets.

He said the financial crisis had made Americans more conscious of "tail risks"—events that are unlikely to occur, but that, when they do, have devastating consequences. That means American consumers are unlikely to return to their free-spending ways, and both the U.S. and its trading partners will have to adjust. Emerging Asian nations, especially China, must play a big role.

If the rebalancing fails, the future looks far more grim, the article said, as there would be pressure for more fiscal stimulus.

LEADING THE NEWS

# Commercial property lures investors back

*But only the safest properties can draw foreigners' money*

By Anita Likus

LONDON—International buyers have returned after a long hiatus to Europe's commercial-property market, a crucial first step to revival.

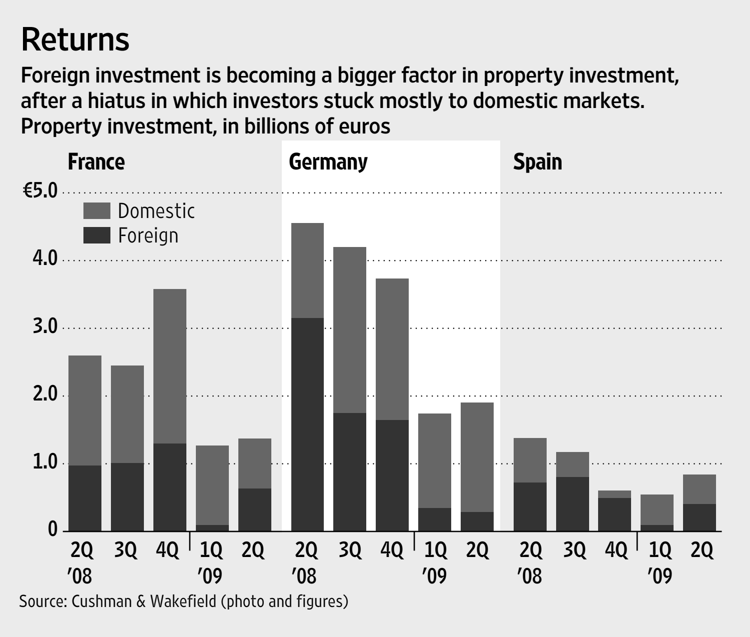
Investment volumes in 32 European countries in the second quarter rose to an aggregate €11.97 billion ($16.86 billion), or 2.5% more than in the previous quarter, according to property-services company Cushman & Wakefield. The rise was largely driven by a 16% increase in investment from foreign buyers in core Western markets.

Getting investors to venture beyond the safety of their domestic markets is only one of the requirements for a recovery in the commercial-property market. And while more investors have been willing to buy into commercial property, they have shared a narrow focus, shunning offices, industrial spaces and retail spaces that have risk attached.

They are largely focusing on so-called prime properties that have strong tenants on long leases, said European property-investment managers Aberdeen Property Investors.

"International investors are currently focusing on a narrow band of prime assets with strong income security," said Tony Horrell, Jones Lang LaSalle's head of European capital markets.

Overall, second-quarter investment volumes were just 41% of the average for 2008 and 19% of the average for the market's peak year in 2007.





TWA Pramerica bought the 22,000 sqm shopping Center, 'Le 32' in Lille, Northern France for €160 million.

Yields on all kinds of prime property rose just 0.07 percentage point, compared with 0.28 percentage point in the first quarter, the smallest quarterly increase since the end of 2007. Lower yields imply higher returns on investment, so the smaller increases should encourage buyers.

This won't, however, help so-called secondary properties, which have shorter leases and less financially stable tenants. "For a full-scale recovery in the broader sector, we will need to see investors and banks take a more active interest in the pricing of risk," Mr. Horrell said.

Most of the big crossborder commercial-property deals in Europe have involved prime properties.

In Germany, London-based real-estate fund **Europa Capital** LLP bought the Berlin Forum Steglitz shopping center from U.K. real-estate investment trust **Hammerson** PLC for €70 million. The center is 100% leased.

**Arab Investments** also bought a mixed-use property in Berlin for €70 million, which is 100% let.

In Germany, foreign investors only accounted for 15% of the €1.9 billion investment.

In France, they accounted for 46% of €1.37 billion in total second-quarter investment activity, compared with 7.2% in the previous quarter.

Deals included **TWA Pramerica**'s purchase of a 22,000-square-meter shopping center in Lille, in northern France. TWA bought "Le 31" for two of its special funds through a joint venture for about €160 million on a yield of 6%.

In Spain, foreign investors accounted for 48% of total property investment activity, or €404 million of a total €837 million, compared with 18% in the first quarter.

Dutch property-investment company **Corio** NV bought the leasehold on the Príncipe Pío shopping center in Madrid from **Grupo Riofisa** for €126 million, reflecting a 7.8% net initial yield.

Property markets traditionally lag behind the movements of the broader economy, feeling the impact some six to 18 months later. So while Aberdeen Property Investors expects commercial property to turn around sometime between the end of 2009 and the middle of 2010, it still expects property-market returns to be weak over the next 12 months as rental levels and capital values fall.

On top of that, the rental markets have seen rents go down in 26 countries of the 32 examined by Cushman & Wakefield.

Cushman also has noted a wide mismatch between what buyers want to purchase and what is available.

Finally, those who want to come back to the market still find it difficult to get financing. Banks are wary of lending for property investments. And, in commercial property, lending is unlikely to be prioritized in the short term by banks that had already amassed large exposures to property before the crisis hit.

# Hotel owners are forfeiting their properties to lenders

By Kris Hudson

"Jingle mail" isn't just for homeowners anymore. From San Diego to Dearborn, Mich., an increasing number of hotel owners in the U.S. market are simply walking away from money-losing properties and forfeiting them to lenders.

The rise in hotel forfeitures is the product of the worst hotel market since the early 1990s, with revenue declining by double-digit percentages. That has pushed the value of many hotels to less than the balance on their mortgages. Just like homeowners who mail their house keys back to the bank—so-called jingle mail—hotel owners see no hope in renegotiating their loans.

Distressed noncasino hotel loans now cover more than 1,000 properties with a cumulative loan value of $16.8 billion, according to Real Capital Analytics, a real-estate research company. That figure encompasses delinquencies, foreclosures, bankruptcies and restructurings of securitized mortgages in addition to loans from banks and other institutions.

Among them are a Mondrian boutique hotel in Scottsdale, Ariz.; a St. Regis resort in Dana Point, Calif.; the InterContinental Montelucia Resort & Spa in Scottsdale, and a Hyatt Regency in Dearborn—each of which is either in foreclosure or has stopped making payments on its debt. It includes the 680 hotels of the **Extended Stay** Inc. chain that filed for bankruptcy in June.

Delinquencies of loans on casinos that have hotels adds 31 properties and $8.6 billion in distressed loans to the mix.

One major factor in the foreclosures: Many hotel loans are difficult to restructure because they were packaged into commercial mortgage-backed securities, or CMBS, which combine hundreds of property payments into one single bond. With scores of investors owning those bonds, it is extremely hard to cut a new deal to keep the hotel in owners' hands.

"There is no one person or two people that can really represent the interests of the borrowers and strike a deal," said Art Buser, chief executive of **Sunstone Hotel Investors** Inc., which is forfeiting one hotel and has put lenders on notice that it might do so with others.

Unlike malls and office buildings with long-term leases, hotels can empty out overnight, wrecking an owner's ability to pay back a mortgage. That has pushed delinquencies upward, especially for CMBS backed by hotel properties. According to Trepp LLC, the delinquency rate for CMBS tied to hotels was 4.75% in the second quarter, up from 0.5% a year earlier. Debt-rating provider Fitch Ratings predicts that rate will jump to between 10% and 15% by year end. In the hotel crash in 1990, more than 14% of all loans tied to hotels, including those from banks and insurance companies, were in arrears, according to New York University figures.

Hotel guests are unlikely to notice many changes, because lenders and commercial mortgage-servicing companies appoint receivers and interim management companies to oversee the properties. The owners of the historic Columbia Gorge Hotel in Hood River, Ore., shut down the 42-room hotel in January and forfeited it to lender **ShoreBank** Corp. in July rather than continue paying its $5.1 million mortgage. ShoreBank retained **North Pacific Management** Inc. to run the hotel and plans to reopen it in September.

To be sure, a delinquency doesn't immediately or always translate to foreclosure. It often takes several months for a lender to foreclose on a property with a delinquent mortgage. And some delinquent borrowers manage to negotiate with lenders to avoid foreclosure or file for bankruptcy protection to thwart it.

What is striking about the current trend is that several of the companies forfeiting hotels are publicly traded. In past hotel downturns, the distress was greater for older, no-frills hotels and motels in private hands. Now, there are far more publicly held hotel owners than in the early 1990s. In particular, several owners of upscale and luxury hotels debuted in the public markets since that downturn.

Many hotel owners went on acquisition sprees during the latest boom that left their properties loaded with debt. "The amount of leverage that was put on in the late 1990s wasn't as high for the public companies as what some of them took on more recently," said David Loeb, a lodging analyst with Robert W. Baird & Co. "Pricing for hotels really got out of control in 2005 to 2008 and the public companies were aggressive in buying assets, so they piled on a lot of mortgage debt."

Perhaps the highest-profile hotel forfeiture of this recession was made by Sunstone, of San Clemente, Calif., which in June disclosed it stopped making payments on its $65 million securitized mortgage on the 258-room W San Diego and intended to turn over the hotel to the special servicer overseeing its mortgage. The move was noteworthy because the W is a prominent luxury hotel in downtown San Diego and Sunstone was among the first publicly traded real-estate investment trusts to disclose its intent to give back a hotel in this recession.

Sunstone isn't done renegotiating mortgages and walking away from some of its 39 upscale hotels. It quit making interest payments on the $30 million mortgage on the 341-room Renaissance Westchester hotel in White Plains, N.Y., in a bid to get the loan's servicer to agree to new terms.

The REIT is prepared to play hardball with other mortgage holders, too: In May, Sunstone obtained agreements from its bondholders in which the bondholders agreed not to declare a cross-default and demand immediate payment of their bonds in the event that Sunstone separately defaulted on as much as $300 million of its mortgages. That gave Sunstone the leeway to stop payment on various mortgages as a way to compel those mortgage holders to agree to revised payment terms.

Neither lenders nor the markets have punished Sunstone greatly for punting the W San Diego. Three weeks after Sunstone announced the move in early June, Sunstone and its banks completed a renegotiation of its credit line that loosened its covenants, such as the ratios by which Sunstone's cash flow must cover its fixed charges. Sunstone's stock has declined 0.2% since the REIT disclosed its plans for the W. In comparison, a Dow Jones index of 12 hotel-REIT stocks rose 5.2% in that span.

"Forfeiting a property to a lender doesn't have the same stigma attached to it in this cycle as it did in past cycles," said Bjorn Hanson, an associate professor of lodging at NYU. "Lenders and industry executives understand that this was unanticipated and outside of management's control."

# CORPORATE NEWS

# Toyota aims to close California factory

*It could be expensive to shut Nummi plant, owned with old GM; production to shift elsewhere in North America*

By Norihiko Shirouzu

**Toyota Motor** Corp. is seeking to close a California assembly plant it owns jointly with the former General Motors Corp., according to Toyota executives, in a move that could improve efficiency at its U.S. operations.

But the Japanese auto maker faces a number of unresolved issues, the executives said, including hundreds of millions of dollars in potential costs from a closure. Those factors could complicate any final decision, they said.

Toyota is now in negotiations with the former General Motors Corp.—the "Old GM" left behind in bankruptcy court after the reorganized U.S. auto maker was relaunched in July—to figure out how it could walk away from the plant, called New United Motor Manufacturing Inc. or Nummi. "Our gut feeling is we need to end production" at the plant, said one of the executives.

The reorganized GM last month decided to abandon Nummi, which has mostly been a money-losing operation since Toyota and GM established the partnership in 1984. It produces about 400,000 vehicles a year.

Separately, GM said it planned to raise production in the third and fourth quarters and announced it would reinstate 1,500 jobs.

"The uptick is an encouraging sign that vehicle sales are turning around," said Tim Lee, GM group vice president of global manufacturing and labor.

The auto maker said it plans to add about 60,000 vehicles in the third and fourth quarter production forecast. Through July, the company has sold 1.14 million light vehicles in the U.S. so far this year, down 38% from the same point last year.

Discussions over the Nummi plant come as Toyota's new chief executive, Akio Toyoda, and his management team look for ways to solve the company's excess capacity. The problem is particularly acute in North America, where the company added new plants earlier in the decade to meet then-strong demand.

By shifting Nummi's capacity to other plants in North America, Toyota would be able to shore up profitability. Toyota's North American assembly plants are operating at about 50% to 60% of capacity, according to U.S.-based consulting firm CSM Worldwide.

Production at Nummi consists mostly of Toyota's Tacoma and Corolla. Production of the Pontiac Vibe, which Nummi produces for GM, is due to end this month.

A Toyota executive said Toyota could shift production of the Corolla car to a plant in Canada and the Tacoma pickup truck to San Antonio, while a Japan plant and possibly a plant in Mexico could produce at least temporarily the Corolla and the Tacoma.

California lawmakers and Gov. Arnold Schwarzenegger have appealed to Toyota to save Nummi and its 4,600 jobs, a majority of which are represented by the United Auto Workers union.

The Toyota executives said the company is trying to make a decision on Nummi by the end of this month, but representatives from Toyota and the old GM are expected to meet later this month for only the second time in an effort to nail down terms.

"There are still a mountain of unresolved issues" concerning, among other things, the plant's hourly workers, the parts producers that established operations around the San Francisco area to supply parts to Nummi, as well as how to shift production to other Toyota plants, said one of the executives.

Because of environmental damage caused by the plant, the site in the San Francisco suburb of Fremont where GM and Toyota have operated Nummi would require substantial funds to clean up before it could be offered for sale, an executive said. Nummi also has debts on its own, said executives.

The Toyota executives argue they tried to persuade GM to uphold the joint venture down to the last minute, offering at one point the Prius, a popular gasoline-electric hybrid car, as well as a version that GM could sell under one of its own brands at Nummi. GM couldn't immediately be reached for comment.

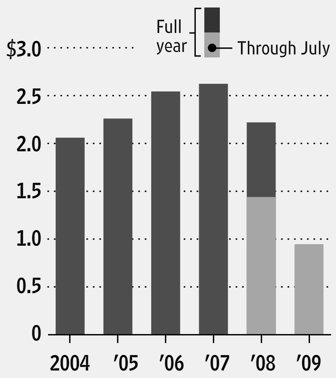
*—John Kell contributed to this article.*


Associated Press

Production at the Nummi plant, above, consists mostly of Toyota's Tacoma pickup truck and Corolla car.

**Slow lane**

Toyota vehicles sold in the U.S., in millions:




Source: the company

# GM's Saab sale still faces hurdles

By Ola Kinnander

STOCKHOLM—**General Motors** Co. said Tuesday it has reached an agreement to transfer its unprofitable Swedish unit Saab Automobile AB to a group led by Swedish supercar maker **Koenigsegg Automotive** AB, but the deal hinges on obtaining about three billion kroner ($412 million) in additional financing.

The head of Saab, Jan Ake Jonsson, and Christian von Koenigsegg, founder of Koenigsegg Automotive, said they are hopeful that the Swedish government will provide financial support as they try to restore Saab to profitability after the consortium struggled to raise capital elsewhere.

If the European Investment Bank approves an estimated €500 million ($704 million) loan, the consortium will have managed to raise 70% of the capital it thinks it needs, said Mr. von Koenigsegg.

"Normally we would be able to get a regular loan to raise the remaining 30%, about three billion kroner, but not with the capital markets today," he said. "The remaining part should come from the Koenigsegg Group and GM but we want Sweden to arrange a bridge loan with interest. Other governments have done much more to help their car companies."

However, Jöran Hägglund, a state secretary at Sweden's Enterprise Ministry and the government's main liaison to the auto industry, reiterated that the Swedish government won't buy a stake in Saab or help it in any way other than possibly providing guarantees for the loan from the European Investment Bank.


Associated Press

Saab cars in a Boston showroom. Swedish auto maker Koenigsegg intends to acquire Saab from GM, but needs to raise more capital for the deal to proceed.

The Swedish government has backed away from giving any direct financial assistance. This stand contrasts with that of the German government, which has offered billions of euros in loans to a buyer for GM's German operations, Adam Opel.

Mr. Hägglund cautioned that "several steps" remain before Saab can get the loan from the European Investment Bank. "The most decisive factor" is whether Koenigsegg can raise the additional capital required, he said.

If Koenigsegg increases its financial commitment and the European Investment Bank approves a loan, the Swedish National Debt Office must then agree to guarantee the loan and the European Union must rule that the loan guarantee doesn't constitute improper state support. GM said it was hopeful that the deal would be completed by the end of the year.

Mr. von Koenigsegg criticized GM's handling of Saab and said he planned to realign the car maker as a niche brand. Under the consortium's business plan, Saab would break even in 2012, producing at least 100,000 vehicles that year, he said.

*—Ian Edmondson contributed to this article.*

## CORPORATE NEWS

# Amcor to buy Rio packaging unit

### *Plastic-bottle maker will gain businesses in Europe and Asia*

BY ANDREW HARRISON

MELBOURNE, Australia—**Amcor** Ltd., the world's largest maker of plastic soft-drink bottles, said it will buy parts of **Rio Tinto** Ltd.'s Alcan Packaging unit for 2.44 billion Australian dollars (US$2.01 billion) to expand its business in Europe and in emerging economies.

The company will acquire Alcan Packaging's European and Asian food units, as well as its global pharmaceutical and tobacco businesses. Amcor plans to fund the acquisitions by raising A$1.61 billion through an offering of shares and establishing a committed bank facility of US$1.2 billion.

The transaction, along with an earlier sale of other Alcan businesses to **Bemis** Co., takes the total raised by Rio through asset sales in the past 18 months to US$6.6 billion, further strengthening the miner's balance sheet and helping ease market concerns about Rio's debt.

Amcor said it will be among the world's largest packaging companies after the acquisition, with a leading position in flexible packaging, folding cartons for tobacco and custom polyethylene plastic containers.

"Now is the right time in the economic cycle to be making acquisitions as asset values are substantially lower than they have been for many years," Chief Executive Ken MacKenzie said.

The purchase price will represent 5.5 to 5.7 times the adjusted earnings before interest, tax, depreciation and amortization of the Alcan businesses. Last month Bemis paid US$1.2 billion for Alcan's Americas food businesses, or an adjusted multiple of about 6.7 times earnings before interest, taxes, depreciation and amortization, when taking into account an estimated US$100 million in tax benefits.

In the past four years, Amcor has sold A$1.4 billion in assets to focus on areas where it expected strong growth and where the company has a dominant market share, such as in flexibles, or folding carton packaging, which will account for 46% of its annual sales after the deal.

Mr. MacKenzie said the acquisition complements the company's existing packaging assets and will enhance its platform for further expansion in growth regions of eastern Europe, Russia and Asia.

After the purchase, 85% of Amcor's sales will be from outside Australia, up from 80%. Western Europe will account for 37% of revenue, Mr. MacKenzie said. He declined to comment on whether Amcor will need to sell some assets to satisfy competition concerns.

Amcor plans to sell the new shares at A$4.30 each, or a 24% discount to the stock's last-traded price Friday of A$5.65, in a 4-for-9 nonrenounceable entitlement offer. Amcor stock remains suspended for the capital-raising.

Rio Chief Financial Officer Guy Elliott said the packaging sale delivers good value to Rio shareholders.

Meanwhile, Amcor said its fiscal year net profit fell 18% to A$211.7 million from a year earlier. Sales rose 3.3% to A$9.54 billion.

*—Alex Wilson in Melbourne contributed to this article.*

Bloomberg News

Coca-Cola cans move along an Amcor conveyor belt in Melbourne, Australia.



# Deadline to buy Polish shipyards is missed by bank

ASSOCIATED PRESS

WARSAW, Poland—A Qatar-based investor that had agreed to buy two struggling shipyards in Poland failed to meet a midnight deadline for payment, throwing the future of the yards into uncertainty, the Polish government said Tuesday.

The shipyards in Szczecin and Gdynia, on Poland's Baltic coast, face bankruptcy. Along with a third shipyard in Gdansk, they have been kept afloat by government subsidies in order to save jobs and because of their historic role as the cradle of the pro-democracy struggle during communist rule.

Since joining the European Union in 2004, Poland has had to do away with the subsidies, which violate the EU regulations. Plans by **QInvest**, a Qatari investment bank, to buy two shipyards seemed to offer them a future.

Polish Treasury Minister Aleksander Grad said the expected 381 million zlotys ($130 million) payment wasn't made by the deadline. He said the intended buyer failed to get funding as a result of the global economic crisis.

"Today it's hard to escape the reality of the world-wide economy," Mr. Grad said at a news conference in Warsaw. "I understand that the previous investors didn't get approval from the institutions backing them."

He said another Qatar-based investor, state-run **Qatar Investment Authority**, has expressed interest in buying the shipyards, and that it has until Aug. 31 to make a decision. If a transaction isn't concluded by then, Poland will seek damages from QInvest.

"I want to believe that this will end in success," Mr. Grad said.

QInvest spokeswoman Susie Pagan said the Qatari investment bank had no comment on the sale, and doesn't comment on client transactions. QInvest has said it was acting only as an adviser for unidentified clients, and wasn't itself the buyer.

QInvest describes itself as energy-rich Qatar's largest investment bank. Its chairman is a member of the sheikdom's ruling family.

The problems could cost Mr. Grad his job. Prime Minster Donald Tusk has warned that he would fire the Treasury minister if he failed to sell off the two shipyards by the end of August.

## CORPORATE NEWS

# Vestas says wind-project demand is on rise

### *Turbine maker sticks to revenue forecast, but earnings decline*

By Selina Williams

In a surprise move Tuesday, the world's biggest wind-turbine supplier, **Vestas Wind Systems** A/S, said it still expects its revenue to increase by nearly 20% this year as order flow has begun to pick up—a sign the sector could be starting to unfreeze.

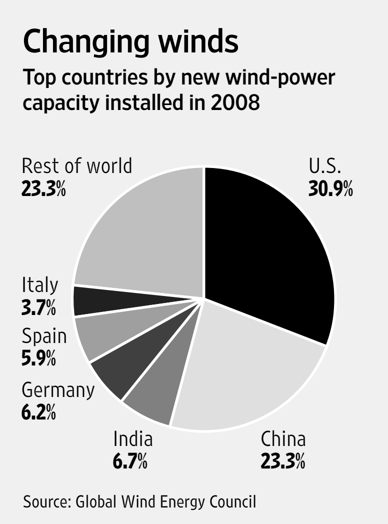
Analysts had expected Denmark-based Vestas to lower its full-year revenue target of €7.2 billion ($10.14 billion) because tight credit markets have hit funding for the multibillion-dollar wind-power industry.

Vestas Chief Executive Ditlev Engel said the company sees signs of renewed interest in wind projects from financial institutions as government stimulus plans, particularly in the U.S. and U.K., are kicking in.

"We're seeing the activity level starting to move again despite the fact that the first six months have been challenging in terms of the orders," Mr. Engel said in an interview.


European Pressphoto Agency/Belga

Vestas wind turbines turn in the wind at Cowley Ridge Windplant in Alberta, Canada




The wind-power industry, which has boomed in the past 10 years—growing almost 30% from 2007 to 2008, for example—has been in the doldrums for most of 2009. Some investment banks that were big lenders to renewables projects, such as Lehman Brothers, have collapsed, while others have severely restricted lending.

Vestas, which had ridden the boom, has felt the impact of the downturn. The company said Tuesday that its second-quarter net profit decreased to €43 million from €65 million a year earlier, partly because of higher costs and reduced gross margins. Revenue rose 11% to €1.21 billion from €1.09 billion.

The company is coping with the slowdown by cutting costs, closing its Isle of Wight wind-turbine blade factory in England last week.

Citing weaker demand in northern Europe, one of the regions hardest hit by the credit crisis, Vestas said it was shifting its geographical focus to China and the U.S. China is expected to become the largest market for new installed wind turbines this year, ahead of the U.S., according to the Global Wind Energy Council.

Still, Vestas said it is encouraged by signs the market could be turning.

Although it had a tough first half, the company said it had received orders of €700 million since the end of the second quarter. The company's corporate review board is also set to evaluate several new contracts, valued at more than €4.4 billion in total, Mr. Engel said, without elaborating.

"We've said all along that it was important to differentiate between a financial crisis and a demand crisis, and the bottom line is we're seeing a lot of interest," Mr. Engel said.

The chief executive also cited Vestas's recent 165-megawatt turbine order for the Bligh Bank offshore wind farm off the coast of Zeebrugge in Belgium as another indicator the market is again opening up. Bligh Bank, run by **Belwind** NV, a consortium of Belgian and Dutch investors, is the first offshore transaction to receive project finance since the financial crisis started.

Lower steel and energy prices this year, improving technology, and good wind-power prices due to national subsidies and stimulus money could also help get the sector moving again. Binding European Union targets on renewable energy use are also supporting the sector.

However, some analysts said there were still risks that could derail the turnaround, both for the sector as well as for Vestas.

# Doubts persist on deal planned by Bharti Airtel, MTN

By Robb M. Stewart And Costas Paris

JOHANNESBURG—Doubts are mounting that South African cellphone operator **MTN Group** Ltd. and **Bharti Airtel** Ltd. of India will be able to hammer out a complex $23 billion tie-up by the end of the month, as frustration grows among some of MTN's shareholders.

MTN and Bharti have already extended an exclusive period for negotiations by one month to Aug. 31 and, according to people familiar with the proposed deal, some MTN shareholders are looking for the Indian cellphone firm to sweeten its side of the transaction.

"The level of irritation rises as this drags on," said Anthony Sedgwick, investment manager at Polaris Capital in Cape Town, which has a stake of about 1.5% in MTN. "There has been no communication regarding the rationale... why this deal apparently has to be pursued at all costs."

The two companies in late May announced they were revisiting a possible merger that would build a company with a combined customer base of more than 200 million and revenue of more than $20 billion a year. Talks over a similar deal failed about a year earlier.

The basic terms as the companies have outlined them would see Bharti accumulate a 49% stake in MTN, buying a stake directly for cash and newly issued global depositary receipts plus receiving MTN shares as part of the swap. MTN would buy a 25% stake in Bharti for $2.9 billion in cash plus new shares, while stock received by its shareholders would take the stake in Bharti to about 36%.

"It is unlikely that there will be an agreement by the end of August. There will probably be another extension on the exclusive talks," a person familiar with the deal said.

This person said MTN management and some shareholders are now asking for an additional roughly $1 billion from Bharti.

MTN's largest shareholder, South Africa's Public Investment Corp., wasn't immediately available to comment. The state-owned investment vehicle, which has a more than 20% stake in MTN, has previously said it supports a deal with Bharti in principle but that there was some room for improvement on the price, and that it had some concerns over the influence MTN would have on a merged entity.

Polaris Capital's Mr. Sedgwick said that based on the information disclosed to date by the companies, the fund manager would vote against a transaction.

MTN would need the approval of investors holding at least 75% of its shares for a deal to go through.

"The sooner we hear more detail on the rationale the better," said Gavin Joubert, fund manager at Coronation Fund Managers in Cape Town, which holds a roughly 5% stake in MTN on behalf of clients. "Our reasons for being opposed remain unchanged."

Mr. Joubert said the price being offered is a significant issue, although Coronation also is concerned about the form payment is expected to take. Exchange controls in South Africa restrict the investment that institutions can make in foreign stock, so to hold on to Bharti Airtel global depositary receipts could mean selling other global equities.

He said there also are doubts merger synergies would be significant between a company focused on India and another with operations in 21 African and Middle Eastern countries. "Under the terms disclosed Bharti would be the proxy for Asian expansion. But as things stand today, MTN is free to expand into Asia," Mr. Joubert said.

A person close to MTN said other shareholders would like the South African company to push for a sweetened offer. However, Lebanon's M1 Group, which has a stake of about 10% in MTN, has said it fully supports a merger.

## GLOBAL BUSINESS BRIEFS

### American Axle

### Car-parts maker gets funds from GM, boosting shares

**American Axle & Manufacturing Holdings** Inc. will receive a $110 million payment as well as a large loan from General Motors Co. Shares of American Axle more than doubled, to $5.70, in afternoon trading Tuesday on the New York Stock Exchange as investors bet that bankruptcy is no longer a threat. American Axle said it reached an agreement in principle for GM to pay $110 million to cover the contracts assumed or terminated through its bankruptcy in June. The company also said GM will provide a second-lien term loan of as much as $100 million. American Axle will have the right to make multiple draws from the loan through Sept. 20, 2013. American Axle must still renegotiate loan terms with its creditors. The company has an Aug. 31 deadline.

### Brocade Communications

A federal appeals court in the U.S. has tossed out the criminal conviction of the first Silicon Valley executive to go to trial in a stock-options scandal that triggered charges against at least a dozen executives. The 9th U.S. Circuit Court of Appeals ordered a new trial Tuesday for Gregory Reyes, former chief executive of **Brocade Communications Systems** Inc., citing prosecutor misconduct. The court says a prosecutor lied when he told the jury that Brocade's finance department was unaware that Mr. Reyes was doling out backdated stock options to company employees. The jury went on to convict Mr. Reyes of all 10 felony counts, including fraud, falsified accounting, conspiracy and filing false financial statements. A judge last year sentenced him to one year and nine months in prison and fined him $15 million.

*—Compiled from staff and wire service reports.*

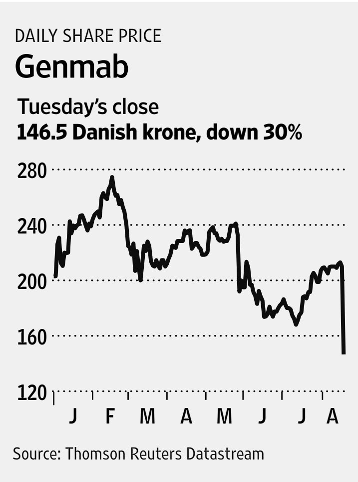
# Genmab slumps on cancer-drug data

By Gustav Sandstrom

Danish biotechnology company **Genmab** A/S on Tuesday reported disappointing results from studies of an experimental cancer drug and said it won't meet its full-year targets. Genmab is developing the drug, Arzerra, with **GlaxoSmithKline** PLC.

In a clinical trial in patients with non-Hodgkin's lymphoma, 10% of people treated with a high dose of Arzerra saw their cancer shrink, Genmab said. Analysts said that was a much lower response rate than expected.

"This is a very disappointing response rate which could make difficult a launch of Arzerra in [non-Hodgkin's lymphoma] without further...studies," Jyske Bank, based in Silkeborg, Denmark, said in a note to investors. Shares in Genmab closed down 30% in Copenhagen.




Genmab and Glaxo are also developing the drug for use against chronic lymphocytic leukemia. They expect the U.S. Food and Drug Administration to decide in the coming months whether to allow Arzerra onto the market to treat chronic lymphocytic leukemia. The drug isn't yet sold in any market.

The results also mean Glaxo won't make a payment to Genmab under their co-development agreement, leading Genmab to cut its 2009 revenue outlook to 750 million Danish kroner ($142 million) from the 1.2 billion kroner previously forecast. Genmab said it now expects a full-year operating loss of 650 million kroner, rather than the loss of 400 million kroner it previously expected.

*—Jeanne Whalen contributed to this article.*

## ECONOMY & POLITICS

# U.S. recovery: fast, slow or neither?

*Some analysts predict a sharp rebound while others foresee sluggish growth; a few say another slump is possible*

BY SUDEEP REDDY

The U.S. economy is pulling out of its deepest and longest recession since the Great Depression. Some economists expect a powerful recovery, others a sustained but muted one. Some even say it will be neither: a fleeting rebound quickly followed by a second slump.

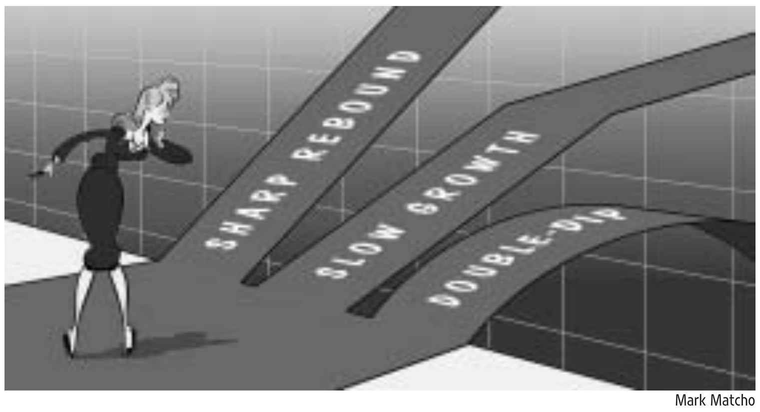
For Americans beleaguered by almost two years of economic pain, the contours of the recovery will determine how many people linger without jobs, whether cutbacks to public services are restored and how quickly savings and investments gain value.

Economists trying to predict the shape of the recovery look for parallels in previous recessions. But the current downturn, which started in December 2007, has echoes from a multitude of economic slowdowns.

It featured the same kind of deep dive in economic output of the 1970s and 1980s recessions, which were followed by sharp rebounds. The credit shock from the latest downturn also recalls the milder credit headwinds of the early 1990s, which turned a relatively short recession into a slow multiyear recovery.

But what distinguishes this recession from most others before it is a severe credit contraction whose effects, some economists believe, are likely to linger for years.

Whatever the structure of the recovery, many consumers won't detect a change in their own circumstances. So many jobs have been lost that the unemployment rate will remain high when the economy begins to rebound. Large swaths of still-jobless Americans will have exhausted their severance payments and unemployment benefits, putting them under further strain even as the overall economy picks up again. And once consumers find new work, their depleted savings will leave them more vulnerable if they were to face another job loss in the next few years.



Mark Matcho

Some sectors of the economy—and regions of the country—are likely to recover earlier than others. The manufacturing and housing sectors, for instance, have contracted so deeply that they are likely to start recovering soon. But the troubled financial sector still is in the process of contracting as banks reshape their balance sheets, putting its recovery further down the road.

Facing a range of potential recovery scenarios, Americans are displaying everything from strong optimism to anxious caution. In recent months, investors have seemed hopeful about the prospects for a robust recovery, pushing stocks up more than 40% from their recession lows in March. Private-sector forecasters in the latest Wall Street Journal survey say the economy is starting to expand, but to expect slow to modest growth of between 2% and 3% next year.

Most businesses remain hesitant, bracing for a painful year ahead.

## After steep drop, built-up demand fuels expansion

The most common path for the economy after a severe contraction has been a huge rebound in economic activity. Employers usually slashed their payrolls and output so sharply to protect themselves, and consumers postponed so many major purchases during the worst of the downturn, that a return to growth came with a fierce expansion.

After the deep recessions of the 1970s and 1980s, business activity rebounded and within several months employers were rapidly rebuilding their payrolls. "You can't find a single deep recession that has been followed by a moderate recovery," said Dean Maki, chief U.S. economist at Barclays Capital. And most forecasters proved to be too pessimistic as prior deep recessions ended. "Very few people were looking for the kind of growth numbers that were actually printed," he said.

**Businesses would ramp up output and hiring, restoring capital budgets.**

Forecasters who support the strong-rebound view expect the economy to grow at a 3% to 5% annual rate through the end of this year and provide the power needed to spark a longer-term recovery.

Businesses would ramp up output and hiring, restoring capital budgets for new computers and equipment. Rising stock values would help restore consumer confidence and spur additional spending for major goods such as cars and appliances. Some consumers put off key purchases for so long that eventually they must come around when they see good deals on store shelves. Housing construction also is coming off rock-bottom levels, giving the construction sector a bit more hope than it has had for the past three years.

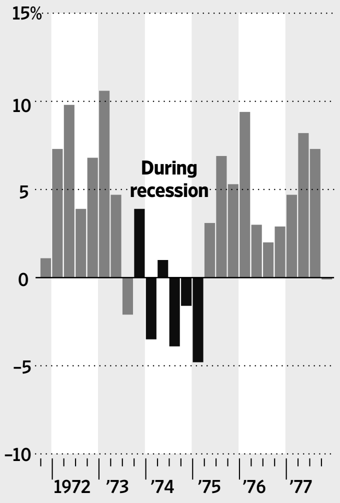
After the natural rebound for three to six months, the bulk of the government's fiscal stimulus program would kick in. That would help sustain activity at the turn of the year and in early 2010, fully propelling the economy out of the downturn.

At Vila & Son Landscaping Corp. in Miami, incoming orders for new projects are about half the level they were at a year ago. The company, which has about 900 employees working on landscaping projects statewide, suffered as the construction and real estate markets tanked. The region has been left with huge inventory, from office rentals to condo buildings.

But the firm's president, Ricardo Leal, is adding workers for maintenance projects—while cutting back its construction operations—as it prepares for the economy to grow. He already sees signs of hope with more projects getting started in local governments, assisted-living facilities and parts of the health-care sector. "We've seen more activity from designers and landscape architects that are at the beginning of these projects," he said. "They feel like they're beginning to turn the corner. My gut tells me we're bottoming out right now and we'll start to see more activity going into 2010."

**Quick bounce** | 1973-75

Quarterly change in U.S. GDP; at a seasonally adjusted annual rate




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

**WSJ.com**

**Question of the day**
What will recovery look like as the U.S. economy comes out of the recession? Weigh in at **WSJ.com/Question**

## Anxiety keeps damper on growth

The economy may bounce back, but plenty of barriers block the path to a sharp rebound. Trouble with spending and lending could potentially make the recovery a slog.

Consumer confidence is falling as job losses mount—albeit at a slower pace than before—and homeowners reshape their finances after severe declines in home values. Households are saving more than they have for most of this decade. That's suppressing consumer spending, the engine for 70% of economic output.

The credit shock is likely to impair the business and consumer sectors for years. Businesses are less likely to get easy loans as banks shrink their balance sheets. That's also true for homebuyers who are finding it harder to get new loans and would need to offer up larger down-payments. And, as real-estate prices have tumbled, existing homeowners can't borrow against the value of their homes as they once did.

The credit headwinds "will continue to hang over the economy for a long time," said Nigel Gault, chief U.S. economist at Global Insight.

"It is one reason not to expect a strong recovery coming from the consumer side. It doesn't mean consumer spending won't grow, but it won't be a big leader the way it has been in previous expansions."

So after a quick bounce, proponents of the slow-growth view say the economy is more likely to expand at a 1% to 2% rate over the next year—well below the 4% to 5% that's necessary to heal the labor market after a deep downturn. Recessions caused by bursting bubbles like the recent housing collapse—as opposed to sharp rate increases by the Federal Reserve to thwart inflation—seem to be followed by jobless recoveries.

Businesses are finding ways to stretch their existing resources rather than expect a rebound.

"People are very frightened," said Janie Curtis, chief executive of Curtis Machine Co. in Dodge City, Kan., which makes gears and gear boxes. She says the end of the pain isn't in sight for her manufacturing customers whose sales are down 50% or more from a year ago.

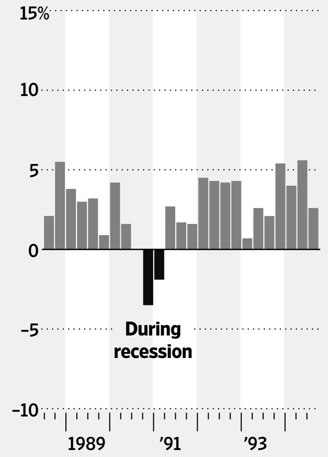
The payroll is down to about 70 employees from 200 several years ago, and Ms. Curtis isn't in a rush to hire more workers back. Instead, the firm is automating more of its operations and squeezing more out of existing employees.

"Our productivity is way up, because the people who are left are having to work harder," Ms. Curtis says.

With a strong focus on productivity—remaining employees picking up the slack—some companies are likely to avoid rehiring workers as long as possible, keeping the rest on the jobless rolls even longer.

**Long comeback**
1990–91

Quarterly change in U.S. GDP; at a seasonally adjusted annual rate




Note: GDP was unchanged in the first quarter of 1990, the start of the recession

## A brief rebound, then a new slump

The economy is likely to see a natural boost in the coming months from a rebound in production. After that, it will get some help from the bulk of the fiscal stimulus program late this year and early next year.

But then what?

The slack in the economy is so large that consumers won't see meaningful raises for years, and they will have less borrowing power to drive their spending. So consumers could make some of the big purchases they have been postponing and then close their wallets to save more.

Businesses, after a frightening period, could remain cautious about ramping up. State and local governments could continue to cut back as tax revenue plummets. And the troubles aren't over for the banking sector.

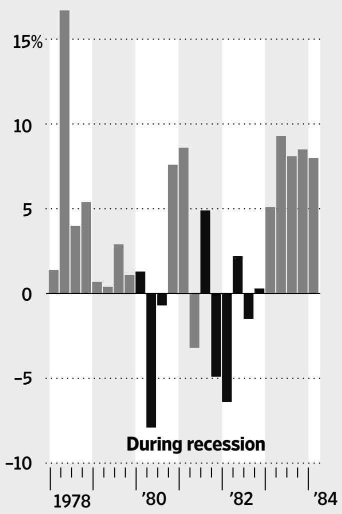
Once the boost from the federal government diminishes, the economy could still be without a major driving force such as consumer spending or business investment to push it forward—risking a return to its contractionary phase. After a brief six-month recession in 1980, the economy recovered but then relapsed within a year. Soaring inflation forced the Federal Reserve to raise interest rates to double-digit levels, pushing borrowing costs higher and spurring a painful and lengthy recession. The late 1940s and 1950s each saw recessions return just three years after the prior downturns ended. That is because businesses can bounce back from crises—such as wars—but then find that the recoveries aren't durable.

Today's fear is compounded by the heavy federal spending. Some economists worry high deficits will push interest rates—and borrowing costs—higher for consumers and businesses.

"I hope we don't have a double-dip recession, but that's a possibility," said Ron Heaton, chief executive of State Bank of Southern Utah.

**Up, then down again**
1980 and 1981–82

Quarterly change in U.S. GDP; at a seasonally adjusted annual rate



# South Korea's Kim dies

## *Former president came to symbolize democratic reform*

By Evan Ramstad

SEOUL—Former South Korean President Kim Dae-jung, who spent most of his life fighting for democracy in his country and subsequently tried to bridge the bitter divide with North Korea, died Tuesday.

Mr. Kim, who won the Nobel Peace Prize for his efforts at reconciliation with the North, died after spending more than a month in Yonsei Severance Hospital for respiratory problems and a blood clot in his lung, a hospital spokesman said. He was 83 years old, according to his official biography, though other records suggest he was slightly older.

Mr. Kim's election in 1997 sealed the arrival of multiparty democracy in South Korea. A leftist on most policy matters but a populist on economics, he led the country through the fallout of the late 1990s Asian financial crisis, which hit South Korea hard.

To the rest of the world, Mr. Kim was best known for his "Sunshine Policy" of outreach and assistance to North Korea, an effort that culminated with a summit meeting with the North's dictator, Kim Jong Il, in June 2000. Later that year, Kim Dae-jung won the Nobel Peace Prize for setting up the first meeting between Korean leaders since before the Korean War.

His efforts to improve relations with the North brought international acclaim but not lasting success. South Korean engagement with Pyongyang failed to stop North Korea's pursuit of atomic weapons. The country conducted its second nuclear test in May.

In the last weeks of his life, a parade of visitors—including United Nations Secretary General Ban Ki-moon, former South Korean political rivals and the current South Korean president, Lee Myung-bak—visited Mr. Kim in the hospital.

Associated Press

Lee Hee-ho, wife of former South Korean President Kim Dae-jung, weeps in front of a memorial altar at a Seoul hospital Tuesday.

"We lost a great political leader today," Mr. Lee said in a statement issued by his office Tuesday. "His accomplishments and aspirations to achieve democratization and inter-Korean reconciliation will long be remembered by the people."

Mr. Lee added: "I hope that President Kim's lifelong wishes will eventually be realized through reconciliation between South and North and social integration."

When Mr. Lee took office last year, he reversed course on a policy that originated with Mr. Kim of essentially unconditional aid to North Korea and instead insisted that assistance be linked to steps by Pyongyang toward abandoning its nuclear-weapons programs.

North Korea has reacted angrily to the shift. Mr. Kim earlier this year called for North Korea to end its daily invectives against Mr. Lee and urged Mr. Lee to reverse his decision.

His death marks the second in four months among key figures in South Korea's progressive movement, in the wake of the May suicide of Roh Moo-hyun, who succeeded him as president.

To South Koreans, Mr. Kim will be most remembered as one of the leading voices of dissent against the authoritarian governments that ran the country from the 1960s to the 1980s. Those governments persecuted him, targeted him for assassination twice and imprisoned or detained him under house arrest for more than 10 years.

He survived all that to become one of the three principal authors of South Korea's democratic constitution in 1987. He immediately ran for president that year but lost, and lost again in the next election five years later.

In 1997, he won a three-way race by a margin of less than 2% to become the third president elected since democracy and the first from an opposition party.

*—Gordon Fairclough contributed to this article.*

# Russia oil output expected to drop

By Jacob Gronholt-Pedersen

MOSCOW—Russian oil output has risen this year, against expectations, but industry participants and analysts say the world's biggest energy supplier faces an inevitable decline in production.

Russian oil firms have cut investment programs following a drop in crude prices from last year's record highs, but have surprised many by squeezing more hydrocarbons than expected out of maturing fields in Siberia.

But this may prove unsustainable, with a steep drop in drilling this year pointing to lower production ahead, industry observers say. Dwindling output in Russia, which pumps about 20% of the oil produced by countries outside the Organization of Petroleum Exporting Countries, could buoy global prices.

"Further oil-output growth will be extremely challenging in Russia," said Oswald Clint, an analyst at Bernstein Research in London. He estimates exploration drilling fell by more than 40% in the first half of the year compared with the same period last year, based on statistics from oil-field service companies and independent energy consultancies.

Predictions of a decline in Russia's oil production come against a backdrop of rising output this year. In total, Russian oil producers pumped 77,000 barrels a day, or 0.8%, more in the first seven months of the year than in the same period of 2008.

Six new Russian fields launched late last year produced a combined 400,000 barrels a day, helping lift total volume. Among the new fields are South Khylchuyu in the Arctic north of Russia, operated by OAO **Lukoil**; **TNK-BP** Ltd.'s Uvat and Verkhnechonskoye fields; and OAO **Surgutneftegaz**'s Talakan field in eastern Siberia.

But the new fields have already reached peak capacity and are now starting to slowly decline, according to an executive at a major oil-field services company.

"Exploration activity is sliding and operators will struggle to keep production levels up," said the executive, who asked not to be named.

He said Russian oil companies have been able to maintain volumes this year by stepping up work on maturing fields in the Russian oil industry's traditional heartland, western Siberia, rather than by drilling new wells, he said.

The pessimistic projections contrast with an upbeat report from the International Energy Agency last week. The Paris-based agency said stronger-than-expected Russian output had prompted it to revise upward its forecast for 2009 oil supply from countries outside OPEC by 160,000 barrels a day, and its 2010 forecast for non-OPEC supply by 200,000 barrels a day.

The uptick in production even appears to have taken the Russian government by surprise. In March, it forecast 2009 oil output of 9.68 million barrels a day, a 1.1% annual fall.

But in late May, when production had started to pick up, Energy Minister Sergey Shmatko said he expected output to remain flat this year and possibly even increase compared with 2008 levels.

Russian oil majors are eager to boost production at new fields farther east and in the Arctic.

Next month, Russia's No. 1 oil producer, state-controlled OAO **Rosneft**, will launch its huge Vankor field in eastern Siberia, the country's biggest greenfield project since Soviet times.

*—Spencer Swartz in London contributed to this article.*

# South Africa's economy shrank by 3% in quarter

By Robb M. Stewart

JOHANNESBURG—South Africa remained mired in recession in the second quarter of the year, increasing pressure on President Jacob Zuma's pledge to create hundreds of thousands of jobs.

Gross domestic product shrank an annualized 3% from the prior quarter in the three months to June, data released Tuesday by the government statistics agency showed. Growth contracted by 6.4% and 1.8% in the preceding two quarters, tipping Africa's biggest economy into its first recession in 17 years.

Colen Garrow, an economist at Brait South Africa Ltd. in Johannesburg, said the weak economy could prompt the Reserve Bank of South Africa to cut interest rates further. The Reserve Bank last week reduced its repurchase rate by half a percentage point to 7%, taking cuts since December to five percentage points.

Mr. Zuma, in his first state-of-the-nation address in early June, said the government planned to create about 500,000 jobs this year and reduce poverty.

However, as global demand has slumped, mining companies and manufacturers have shed thousands of jobs and cut spending. The jobless rate nudged up to 23.6% in the second quarter as employment fell by 267,000 and the number of people who gave up looking for work increased by 302,000, data in July showed.

There has been growing unrest during the president's first 100 days in office, with unionized workers flexing their muscle and striking briefly for higher wages and residents in impoverished townships taking to the streets to protest against what they say is poor service delivery.

"Just as the impact of the recession on South Africa lagged somewhat behind the rest of the world's, it seems our recovery will lag too," Finance Minister Pravin Gordhan said Monday.

The data showed that the manufacturing industry remains in the doldrums, and agriculture showed a contraction for the quarter, while areas of the domestic economy—such as finance and wholesale and retail trade—also shrank.

Countering this was output growth in the construction industry, which has benefited from government spending on infrastructure and ahead of the 2010 World Cup.

Statistics SA's figures showed the mining industry also recorded a bounce, growing modestly but after a sharp fall in the previous quarter.

# Japanese campaign season formally gets under way

By Takashi Nakamichi

TOKYO—Japan's closely watched lower-house election campaign officially kicked off as the main opposition Democratic Party of Japan attempts to end the ruling party's nearly uninterrupted reign spanning more than half a century.

Local media polls so far show the 11-year-old DPJ is well-placed to oust the ruling Liberal Democratic Party from power in the 480-seat contest on Aug. 30.

A DPJ victory could mean that Japan's economic policy becomes more focused on building domestic demand to bolster growth, as the party seeks to correct the nation's dependency on overseas demand.

The LDP, which has governed the country since 1955 except for 10 months through June 1994, has relied on an export-oriented growth model and is less focused than the DPJ on lifting local consumption.

While Tuesday marked the official start of the campaign, candidates from both parties have been in the streets for the past several weeks trying to woo the voters.

Before the official start, however, candidates are banned from directly asking people to vote for them and aren't allowed to put up campaign posters that display only the candidate.

In the latest Kyodo News survey released Monday, support for the LDP in the proportional-representation part of the ballot, which covers 180 of the lower-house seats, stood at 16.5%, up 3.2 points from a poll conducted a week earlier.

The DPJ came in at 32.6%, down 1.5 points.

Associated Press

Yukio Hatoyama, leader of the opposition Democratic Party of Japan, on Tuesday campaigned in Yokohama for the coming lower-house elections.

ECONOMY & POLITICS

# Damascus agrees to Iraq security effort

## *U.S. and Syria plan to join Baghdad in monitoring border*

By Jay Solomon
And Julien Barnes-Dacey

The Obama administration and Damascus have tentatively agreed to establish a tripartite committee, with Baghdad, to better monitor the Syrian-Iraqi border as the Pentagon draws down American troops from Iraq in coming months, said senior U.S. officials.

The proposed three-way border-control assessments could boost Iraqi security and patch one of the region's most volatile fault lines. The initiative was made by a team of U.S. Central Command officers and their Syrian counterparts last week in Damascus.

The pact awaits the green light from Baghdad, which expressed frustration at being excluded from the U.S.-Syrian talks, saying they violated Iraqi sovereignty on security matters.

Iraqi Prime Minister Nouri al-Maliki met Syrian President Bashar Assad in Damascus on Tuesday. A statement issued late Tuesday by the Iraqi prime minister's office in Baghdad said only that the two sides "discussed the expansion of the Iraqi and Syrian cooperation in the areas of border control."

"Both governments are working seriously and practically to deal with all the issues," added Alaa al-Jawadi, the Iraqi ambassador in Damascus. "The Syrians have been positive with us."

"The Syrians agree that a tripartite approach is the appropriate approach," said a U.S. official briefed on the Centcom mission. "We don't have a response back from Maliki."

Agence France-Presse/Getty Images

Iraqi Prime Minister Nouri al-Maliki, left, met Syrian President Bashar Assad in Damascus Tuesday to discuss border security.

The border-security initiative provides for the assessment of border checkpoints, dealing with technical issues such as screenings and procedures.

The Pentagon regularly accused Syria of facilitating the flow of foreign fighters and al Qaeda militants into Iraq since the overthrow of Saddam Hussein in 2003.

In June, the top U.S. commander in Iraq, Gen. Ray Odierno, said there had been a significant decrease in the number of foreign fighters entering Iraq from Syria. But U.S. officials also say there are issues to resolve. "We're still a little bit concerned with Syria's role in this," Gen. Odierno told reporters in Baghdad on Monday. "I think our bilateral discussions with them are important."

Syria says it has detained more than 1,700 militants, blocked potential combatants from passing through the country en route to Iraq and imposed stricter border policing. Syria also appears to have cracked down on former members of Saddam Hussein's Baathist regime who fled to Damascus after the Iraqi invasion.

"The Baathists have been coming under a lot of pressure in the last few months," said one senior Western diplomat. "Some have been kicked out, some have been told to shut up."

Syria's moves seem to be a response to U.S. President Barack Obama's increasingly active outreach efforts. The administration has announced the return of a U.S ambassador to Damascus and recently eased U.S. sanctions in an apparent bid to draw Syria away from its alliance with Iran.

Senior Syrian officials were unavailable for comment Tuesday. But members of Mr. Assad's government have stressed their desire for improved security cooperation with Washington.

"Now with a new administration, when we have assurances that the Unites States will withdraw from Iraq by 2011, then we do believe that full cooperation between Syria and the United States in different fields, not only security issues, will definitely be welcomed," said Fayssal Mekdad, Syria's deputy foreign minister, in a recent interview.

Over the years, Syria and Iraq have had a hot-and-cold relationship. It has been mostly frosty since the American-led invasion in 2003, but has warmed as U.S.-Syria ties thaw.

Baghdad received a high-level Syrian economic delegation in Iraq earlier this year. Iraq's finance minister visited Damascus this week.

Mr. Maliki's visit, announced suddenly following the Central Command delegation visit to Damascus last week, also may have had domestic political motivations. Iraqi parliamentary elections are scheduled for January and Mr. Maliki has positioned himself as a strong nationalist, promoting Iraqi sovereignty. Nationalist rhetoric is running high, and Iraqi officials appeared miffed about being excluded from the Damascus discussions about their country's security.

"We need to do this cooperation with the Iraqi government because we are looking forward to having an independent, sovereign Iraq," said Mr. Mekdad, Syria's deputy foreign minister, in a recent interview. "We don't accept discussions about Iraq taking place without the participation of the Iraqi government."

*—Chip Cummins in Baghdad and Peter Spiegel in Washington contributed to this article.*

# Mubarak, Obama discuss Mideast

By Judith Burns

WASHINGTON—After meeting with the Egyptian president Tuesday, President Barack Obama said "there has been movement in the right direction" toward a resolution of the Arab-Israeli conflict and said he is "encouraged."

"The interests on both sides are towards peace," Mr. Obama told reporters after his one-on-one meeting at the White House with Egyptian President Hosni Mubarak.

Mr. Obama cited improved security and increased economic activity in the West Bank as encouraging developments. But Mr. Obama also struck a note of caution. "Just because something makes sense doesn't mean it happens."

During their meeting in the Oval Office, the leaders discussed Egypt's regional concerns, including Iran's nuclear weaponry, but focused on the Palestinian question "because it's the pivotal issue," Mr. Mubarak said.

Mr. Mubarak said he has told Israelis to "forget about a temporary solution and forget about temporary borders," insisting on a solution that defines borders, establishes a home for displaced Palestinians and resolves the status of Jerusalem.

Mr. Obama said the U.S. is devoting time and resources to help advance the Middle East peace process, noting that his administration jumped in "immediately," urging all parties to take concrete steps to resolve the conflict.

"My hope is that we are going to see not just movement from the Israelis but also from the Palestinians," Mr. Obama said. He said that Palestinians seem to recognize "that Israel isn't going anywhere" and that Israelis understand it is in their nation's interest to strike a peace accord.

The 81-year-old Mubarak, who has ruled Egypt for 28 years, also indicated that he would seek another term. "I have entered into the elections based on a platform that included reforms and therefore we have started to implement some of it and we still have two years to implement it," Mr. Mubarak said, volunteering that he and Mr. Obama had spoken about U.S. concerns about repression of political opposition in Egypt.

The Egyptian Embassy later said Mr. Mubarak has made no decision on seeking a new term in 2011. Mr. Mubarak looked robust despite earlier reports that he had become increasingly frail and was preparing his 46-year-old son as a successor.

Egypt has an exploding population, ravaged by widespread poverty and high unemployment. He has kept a lid on burgeoning social and religious pressures through heavy repression of much of the political opposition in Egypt, especially the Islamic fundamentalist Muslim Brotherhood, the most organized group challenging his rule.

Mr. Mubarak had been a regular visitor to Washington during the Clinton administration. Then he stayed away to protest the U.S. invasion of Iraq and President George W. Bush's intensified pressure to open the Egyptian political system and moderate its human-rights policies.

*—The Associated Press contributed to this article.*

Reuters

Barack Obama, right, met in the White House on Tuesday with Egypt's Hosni Mubarak, who is urging a permanent solution in the Middle East.

# Pakistan captures a close associate of dead Taliban leader

By Zahid Hussain

ISLAMABAD—Pakistani security forces captured a close associate of Taliban leader Baitullah Mehsud, who was believed slain in a U.S. missile strike this month.

The capture of Mr. Mehsud's close associate, Maulvi Umar, deals another blow to a Taliban insurgency that has racked Pakistan but now appears in disarray. Mr. Umar's arrest turns a key Taliban aide into a potential source of information on the militant network operating on the Afghanistan's border.

Mr. Umar, who worked as a spokesman for Tehrik-e-Taliban Pakistan, the group led by Mr. Mehsud, was arrested Monday night, say intelligence sources in Islamabad. He was believed to be traveling to a meeting with Taliban commanders.

As a spokesman for the Taliban insurgency, Mr. Umar maintained a relatively high profile. He frequently called journalists to claim responsibility for terrorist attacks in Pakistan. In recent months, however, he has dodged attention as Pakistani security forces launched an offensive in his home region of Mohamand. His arrest could further weaken the militant outfit following the apparent death of Mr. Mehsud. Pakistan officials are confident that the Taliban commander—who was blamed for the assassination of Pakistani leader Benazir Bhutto—was killed in a U.S. missile strike on Aug. 5. Some Taliban leaders insist Mr. Mehsud is still alive, but the Associated Press cited officials as saying that Mr. Umar acknowledged Mr. Mehsud's death.