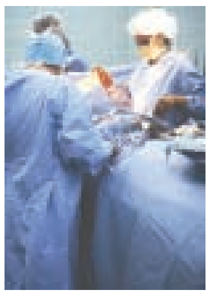
THE WALL STREET JOURNAL.
WSJ.com
DOW JONES Newswires
EUROPE
DOW JONES A News Corporation Company
VOL. XXVI NO. 243 * WEDNESDAY, JANUARY 14, 2009

THE WALL STREET JOURNAL.



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Business & Finance

Top U.S. Fed officials said Obama needs to push forward with the unpopular act of pumping more taxpayer money into ailing financial institutions and may need to buy bad assets from banks. The president-elect faces a big challenge in getting lawmakers to follow his lead. Page 1

■ **The U.K. government will** unveil an expansion of its financial-rescue plan Wednesday, but it faces a problem getting domestic banks to fill the void left by departed foreign lenders. Page 1

■ **Citigroup is planning** to narrow its mission to two areas, in a reorganization that will mark a further step toward dismantling the financial giant. Page 19

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■ **Yahoo is expected** to announce that former Autodesk Chief Executive Carol Bartz has accepted its offer to become CEO. Page 3

■ **Royal Bank of Scotland** is selling its stake in Bank of China, aiming to raise up to $2.37 billion, as Western banks shed Chinese holdings. Pages 19, 32

■ **U.S. blue-chip shares slipped**, while broader indexes had small gains, as investors fretted over coming profit reports. European shares fell. Page 20

■ **Airbus is likely** to report that it signed more orders for new planes than Boeing last year. But the big issue is which will see fewer orders evaporate. Page 3

■ **Germany detailed** $66.89 billion in spending and tax measures to boost the economy, but economists said the benefits will take time to kick in. Page 3

■ **The ECB is** likely to cut rates by a half percentage point on Thursday to stem the risk of a deeper recession. Page 3

■ **Swaths of the EU** were left without Russian gas supplies for a seventh day as a pact to kick-start Russian exports via Ukraine unraveled. Page 32

Markets 4 p.m. ET

MARKET	CLOSE	NET CHG	PCT CHG
DJIA	8448.56	-25.41	-0.30
Nasdaq	1546.46	+7.67	+0.50
DJ Stoxx 600	201.66	-2.87	-1.40
FTSE 100	4399.15	-27.04	-0.61
DAX	4636.94	-82.68	-1.75
CAC 40	3197.89	-48.23	-1.49
Euro	$1.3186	-0.0160	-1.20
Nymex crude	$37.78	+0.19	+0.51

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World-Wide

Israeli forces battled Palestinian militants in southern Gaza City before withdrawing into sparsely populated farmland for the third day in a row, fueling fears that a third phase of the Israeli attack could be imminent. But there were also indications that Israel's and Hamas's resistance to an Egyptian-sponsored cease-fire initiative may be softening. Page 11

■ **Hillary Clinton said** the U.S. should engage hostile powers such as Iran and Syria and pursue partnerships with China and Russia, in her bid to become the next secretary of state. Page 9

■ **Biden told** Iraqi leaders that the coming U.S. administration is committed to a responsible troop withdrawal that doesn't endanger security improvements.

■ **Four Iranians were tried** on charges of seeking to topple Iran's government with alleged U.S. support, and a verdict is due soon, a judicial official said.

■ **Ethiopian forces began** a pullout from Somalia, threatening to leave a power vacuum but also presenting an opportunity for more moderate groups to reclaim the government. Page 11

■ **Zimbabweans are facing** a deepening humanitarian crisis and what appears to be a renewed security crackdown, just weeks before Mugabe plans to form a new government. Page 11

■ **North Korea said** it will keep its nuclear arsenal until it is satisfied the U.S. isn't hiding atomic weapons in South Korea.

■ **A Paris court convicted** 11 men with alleged links to a Kurdish rebel group over firebombing attacks on Turkish cultural sites in southwestern France.

■ **Protesters clashed** with police in Latvia's capital after a demonstration against the government turned violent.

■ **Eight people died** in an explosion at a government building in Russia's Ingushetia province. An initial investigation suggested a gas leak was to blame.

■ **Obama is expected** within his first week in office to issue an executive order to close the U.S. prison at Guantanamo. Page 11

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EDITORIAL & OPINION

German vote engineering
Berlin's stimulus package is curiously timed for the elections. Review & Outlook. Page 13

Fed leaders, Obama back bigger bank-bailout plan

Support sets stage for fight in Congress; accountability push

By Greg Hitt And Jon Hilsenrath

Reuters

Fed Chairman Ben Bernanke discussed the U.S. financial system during a speech he delivered at the London School of Economics on Tuesday.

Top Federal Reserve officials threw themselves into a U.S. political debate, saying the Obama administration needs to push forward with the highly unpopular act of pumping more taxpayer money into ailing financial institutions and might need to buy bad assets from banks.

President-elect Barack Obama visited Capitol Hill on Tuesday to sell a similar message to Senate Democrats. Getting Congress to follow his lead could be the biggest political challenge in his first weeks in office.

Lawmakers are pushing for new conditions on federal money that finds its way to banks. Moreover, lawmakers and Mr. Obama are weighing more popular priorities, including fiscal stimulus and helping homeowners avoid foreclosure.

"A modern economy cannot grow if its financial system is not operating effectively," Fed Chairman Ben Bernanke warned in a speech at the London School of Economics.

Funds from the Treasury Department's $700 billion Troubled Asset Relief Program helped prevent a global financial meltdown last year, he said. But bad assets continue to clog the balance sheets of financial institutions. Fixing that problem, he said, is paramount.

"Fiscal actions are unlikely to promote a lasting recovery unless they are accompanied by strong measures to further stabilize and strengthen the financial system," he said. Donald Kohn, the Fed's vice chairman, delivered a similar message in testimony before the House financial-services committee.

Lawmakers have been highly critical of TARP, arguing that taxpayer

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Swiss bank UBP lost money with Madoff

Name: Union Bancaire Privée

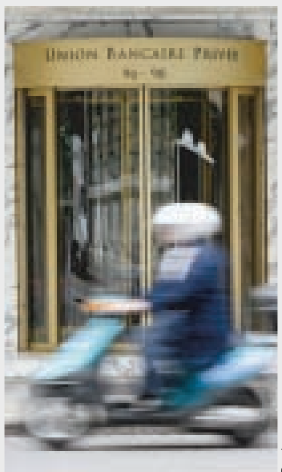
Headquarters: Geneva

Founder: Edgar de Picciotto, 80 years old, a Lebanese-born financier who was among the early hedge-fund investors

History: In 1969, Mr. de Picciotto formed Compagnie de Banque et d'Investissements. It grew rapidly through a series of acquisitions, including a merger with an American Express Co. unit.

Clients: The bank managed about $124.5 billion in assets as of June from wealthy individuals and institutions throughout Europe, the U.S. and the Middle East.

Madoff exposure: UBP says it had $700 million of direct exposure through its funds-of-funds and client portfolios and that its total exposure was less than 1% of its assets.



Reuters

Union Bancaire Privée in Geneva

Swiss bank UBP missed warnings about Madoff

By Cassell Bryan-Low

LONDON—Swiss bank **Union Bancaire Privée** kept hundreds of millions of dollars of its wealthy clients' money in Bernard Madoff's alleged Ponzi scheme despite warnings from its own research team, according to people familiar with the matter.

While others in the investment community had questioned Mr. Madoff's strategy and chosen to stay away, the instance offers a rare sign that red flags were raised within one of the large institutions that actually invested with Mr. Madoff.

Union Bancaire Privée, known as UBP and one of the largest investors in hedge funds globally, was part of an international network of so-called feeder funds that channelled money into Mr. Madoff's investment firm. The Geneva-based bank has said it has about $700 million in Madoff-related investments through its funds-of-funds and client portfolios.

By early 2007, though, UBP's research department had raised various concerns about Mr. Madoff's business, and later recommended that he be stricken from a list of fund managers approved for its clients' investments, according to people familiar with the matter and internal emails reviewed by The Wall Street Journal. The people say that some of the bank's most senior exec-

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Hurdles rise as U.K. widens stimulus plan

By Carrick Mollenkamp, Alistair MacDonald And Sara Schaefer Muñoz

The United Kingdom government is racing to expand an ambitious financial-rescue plan that so far has failed to spark economic revival. But it faces a tough new problem: getting its domestic banks to fill the huge lending void left by foreign firms that have fled the market.

British Prime Minister Gordon Brown and Treasury chief Alistair Darling are preparing an enhanced lending plan that will be announced Wednesday, the government said. A key part of the new package is expected to be a £20 billion ($29.65 billion) loan-guarantee program aimed at small- and medium-size companies, according to people familiar with the situation.

Messrs. Brown and Darling, however, face a tough reality as they seek to amend the original rescue package: no matter much they pressure U.K. banks to lend, it won't make up for the gap left by the financial damage to lenders in places like Iceland, Ireland and Belgium. The U.K. banks are also hampered by their own growing corporate losses, as well as the fact that there still is no market for securities made up of pools of consumer loans.

As they launch the revised plan, U.K. leaders, hailed in the fall as architects of a smart bank-rescue plan, now will face tough questions

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LEADING THE NEWS

Trade decline adds to the global slowdown

Major nations post big export retreats as demand falls off

Trade among nations is declining sharply in many regions around the world, adding another brake on a global economy that's already slowing dramatically.

*By **Kelly Evans** in Washington, **John W. Miller** in Brussels and **Mei Fong** in Yiwu, China*

The U.S., the world's biggest economy, had a combined $326 billion in trade activity in November, down 18% in just four months from its peak in July, when activity totaled $397.8 billion. Compared with November 2007, total trade in the U.S. sank 7%. In November 2008, U.S. exports fell 5.8% from October, the Commerce Department said, while U.S. imports sank 12% to $183.2 billion due to the weakening economy and falling oil prices that helped to lower the nation's energy bill. Overall, the trade gap narrowed to $40.4 billion from $56.7 billion in October; it was the smallest deficit in five years.

Some of the world's other largest trading nations, including China, Japan and Germany, also are reporting declines in exports in part because U.S. appetite is slacking. In the case of China, the decline was the most severe in at least a decade.

The contraction intensifies pressure on businesses around the world to find new customers and raises calls for government to spend and intervene to help revive growth—and to block imports from competitors.

The largest global economies—the U.S., Japan, and the euro zone—are already in recession and the red-hot growth seen in emerging countries last year is cooling rapidly.

While the growth of trade generally slows during recessions, it doesn't usually contract. In December, the World Bank projected global trade would decline by 2.1% this year, the first decline since 1982, and topping the 1.9% decline in 1975.

Declining trade is hurting the European Union's efforts to limit the depth of Europe's recession. Exports from the EU's four biggest economies—Germany, Italy, Spain and France—fell a combined 10.9% in November to $188.3 billion, according to a Wall Street Journal calculation, compared with $211.4 billion in October.

In Germany, the region's largest economy, exports fell 11.8% in November from the previous year to $102.7 billion—the biggest drop this decade. Don Brasher, founder and owner of Geneva-based Global Trade Information Services, said he expects the downward trend in global trade activity to continue for at least the next six months. In 15 years of running his company, he says, "I've never seen this before."

"We think this will end up being the worst global recession since the second World War," said Nigel Gault, chief U.S. economist at IHS Global Insight in Lexington, Mass.

Meanwhile, Japan which has the world's second-largest economy and is heavily dependent on exports for growth, posted a record decline in exports for November as its trade surplus fell for the ninth month in a row, its Ministry of Finance reported Tuesday.

"With the U.S. economy unlikely to pick up anytime soon, despite President-elect Barack Obama's planned economic-stimulus measures, the Japanese economy will keep facing very severe conditions at least until June," said Norio Miyagawa, an economist at Shinko Research Institute.

A.P. Moller-Maersk A/S, the world's biggest container shipping company, announced last month it is laying up eight huge vessels on a drop in demand due to the current global economic uncertainty. Group Chief Executive Nils Andersen on Tuesday said he doesn't expect a speedy recovery in freight rates and that the container shipping business will remain depressed for the next two years.

"If improvement comes at the end of 2010, we will be pleasantly surprised," Mr. Andersen told reporters during a visit to Singapore. "Nobody expected such a deterioration in the United States. The next couple of years, we will be on a very tough track."

But the downturn in trade is hitting U.S. companies hard. **Galkin Automated Products** Corp. saw exports of its machinery used to make bed mattresses start to drop abruptly in October, just after the global meltdown hit. Since then, the slowdown has spread to all its markets, including Indonesia, Australia and the Middle East.

"Nobody's immune," says Paul Block, chief executive of the closely held West Babylon, N.Y., company. "The fist has just continued to clench itself and it's happening everywhere."

Galkin has shed workers down to a staff of 25 from 30 before the slowdown, and cut back everyone's hours by 15% to try to preserve jobs.

The woes of the world's biggest economies are especially worrisome to developing nations, whose cheaper labor and raw materials helped them become production centers and whose rising prosperity cultivated their own domestic demand.

China, for example, is buying less now from other countries even as it has more trouble selling to them. Exports from China in December fell 2.8% from a year earlier, extending the 2.2% decline in November, China's Customs agency said Tuesday. China's imports fell even more sharply, dropping 21.3% in December after a 17.9% fall in November.

Exports have contributed around 20% of China's economic growth since 2005, up from a single-digit share in previous years. That boost from overseas demand helped charge China's five-year run of 10%-plus economic growth. It won't be easy to replace that quickly, one reason why China's growth rate is expected to slow this year to 8% or lower.

Those strains are on display in Yiwu, a city four hours' drive southwest of Shanghai. It's often called the dime-store capital of the world, thanks to its Yiwu International Commodity Trade City, a 370-acre market with more than 60,000 stores selling everything from Valentine's Day decorations to socks to glittering costume jewelry.

In good times, Yiwu is overrun with buyers from U.S., Europe and the Middle East snapping up things like zippers and notebooks in bulk. But with new orders from the U.S. and Europe dropping recently, merchants are trying to make up the shortfall by cultivating new markets from Latin America and Russia, as well as domestic Chinese consumers—with lukewarm results.

One of the center's more ambitious ventures was the opening of a new wing in late 2007 that was intended to lure Chinese consumers with South Korean child seats, Californian wines, Japanese ceramics and Italian shoes. Over a year later, traders in that section report hardly any business at all.

—Andrew Batson and Timothy Aeppel contributed to this article.

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.

THE WALL STREET JOURNAL EUROPE (ISSN 0921-99)
Boulevard Brand Whitlock 87, 1200 Brussels, Belgium
Telephone: 32 2 741 1211 Fax: 32 2 741 1600
SUBSCRIPTIONS, inquiries and address changes to:
Telephone: +44 (0) 207 309 7799 Calling time from 8am to 5.30pm GMT
E-mail: WSJUK@dowjones.com Website: www.services.wsje.com
Advertising Sales worldwide through Dow Jones International. Frankfurt: 49 69 971428 0; London: 44 207 842 9600; Paris: 33 1 40 17 17 01
Printed in Belgium by Concentra Media N.V. Printed in Germany by Dogan Media Group / Hürriyet A.S. Branch Germany. Printed in Switzerland by Zehnder Print AG Wil. Printed in the United Kingdom by Newsfax International Ltd., London. Printed in Italy by Telestampa Centro Italia s.r.l. Printed in Spain by Bermont S.A. Printed in Ireland by Midland Web Printing Ltd. Printed in Israel by The Jerusalem Post Group. Printed in Turkey by GLOBUS Dünya Basınevi.
Registered as a newspaper at the Post Office.

Editeur responsable: Daniel Hertzberg M-17936-2003

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

CORRECTIONS & AMPLIFICATIONS

Chrysler vehicles sold in December 2007 had been on dealer lots for 82 days, according to J.D. Power & Associates. A Corporate News page article Monday incorrectly said the vehicles had been on dealer lots for 70 days last year.

LEADING THE NEWS

Airbus likely topped Boeing in '08

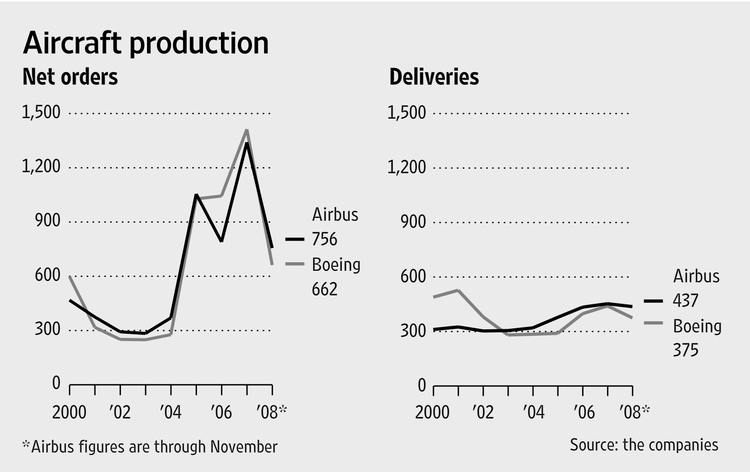
Orders for new planes are expected to hit stiff winds this year

By Daniel Michaels

European plane maker Airbus is expected to announce Thursday that it signed more orders for new planes than rival **Boeing** Co. in 2008. But with the global economy struggling, this year's winner is likely to be the one seeing fewer existing orders evaporate.

John Leahy, Airbus's top airplane salesman and a chief operating officer, said in an interview that airlines—which are facing dwindling passenger counts—will be ordering fewer new planes this year. The issue for both manufacturers, he said, "is whether people ask to defer or reschedule orders" that are set for delivery this year or next. So far, customers are keeping their commitments, he said.

Access to funding will be a key factor. The global financial crisis has dried up ready sources of capital. Banks that recently lent to airlines have cut back, leasing companies have limited cash and financial markets that airlines routinely tapped for aircraft funding have all but disappeared.



Airbus, a unit of Franco-German **European Aeronautic Defence & Space** Co., and Boeing say most 2009 delivery plans are on track because most customers arranged funding for this year's purchases before financing dried up.

Still, aircraft financiers predict that both companies will need to help many carriers arrange financing. They may also have to park new jetliners outside the factories until money becomes available for the industry.

"There's going to be a pretty big funding gap," said Christian McCormick, chief executive of Natixis Transport Finance, a division of French investment bank Natixis SA and a major underwriter of aircraft purchases.

The total financing needed for planes to be delivered this year could reach $70 billion, bankers and analysts say. Some estimate the liquidity crisis could create as much as a $20 billion gap because sources of funding have all but disappeared.

Bob Genise, chief executive of aircraft lessor DAE Capital, a division of **Dubai Aerospace Enterprise**, notes that leasing companies in recent years have accounted for up to 35% of deliveries from Airbus and Boeing, either through planes they bought directly or ones they helped airlines to finance. "The leasing industry is not going to be there" this year, Mr. Genise said. "I have concerns about the ability of the market to fund all those deliveries."

If funding isn't found, Airbus and Boeing may need to cut production levels over the next two years, financiers said.

Airbus and Boeing plan to keep production roughly stable. Both have been aggressively juggling production schedules, allowing stronger customers take planes sooner and urging weaker ones to delay.

Airbus's 2008 lead in jetliner deliveries has been expected. Boeing last week announced that in 2008 it booked orders for 662 new jetliners and delivered 375 planes. Airbus had topped both those figures through November.

Boeing failed to meet its 2008 sales target of roughly 475 planes due to a 58-day strike by factory workers and manufacturing snags that forced dozens of planes to be repaired. Boeing's sales number was a 53% drop from 2007's industry record of 1,413 net orders.

Airbus posted 756 net orders through November and delivered 437 planes. Results through December will be updated on Thursday.

—J. Lynn Lunsford contributed to this article.

Effectiveness of German stimulus is criticized

By Andrea Thomas

BERLIN—Germany presented its €50 billion ($66.89 billion) package of spending and tax measures to support its ailing economy, calling it the biggest fiscal-stimulus effort in Europe, but the plan got a mixed reception from economists and business groups, especially as many of the benefits will take time to flow through.

The stimulus program for 2009-2010 was agreed on late Monday and follows a first stimulus package adopted in November, which economists said would boost the economy by €12 billion through 2010.

The new plan boosts investment in public infrastructure by €18 billion, which could take months to be implemented, and from July 1 cuts income taxes and the payroll-tax burden by about €18 billion. The program also encourages companies to retain workers by putting them on short shifts rather than laying them off.

The coalition government parties also backed plans for a €100 billion fund to provide credit guarantees to help companies struggling with tight credit-market conditions.

Not all were happy with the package, with some criticizing the late timing of reducing the income-tax and payroll-tax burden.

Angela Merkel

"What is problematic about this package is that most of the stimulus will only become effective in the second half of this year. With respect to the infrastructure measures, it seems even reasonable to assume that any significant impact will materialize only by the end of 2009," said Dirk Schumacher, an economist at Goldman Sachs.

Some business groups were also disappointed. "The agreed cut in taxes and [social security] contributions are too little and come too late to give a noticeable boost to consumption," said Stefan Genth, managing director of German retailers association HDE. He said a big tax cut and infrastructure package would have been better than the bundle of different measures.

But the Federation of German Industry said the second stimulus plan comes at the right time. "It's sensible that the government fights the recession with higher investments and higher net income," said the group's managing director, Werner Schnappauf.

The two stimulus programs announced since November, plus other tax and benefit changes in recent months, add up to about €80 billion in higher spending and lower taxes through 2010.

Deputy Chancellor Frank-Walter Steinmeier said that shows that Germany is doing more to fight the crisis than any other European country.

As part of the deal, the coalition parties agreed to cut mandatory health-care premiums by 0.6 percentage point to 14.9% of gross income and cut the income-tax rate for lower-income earners by one percentage point to 14%. They will also pay a bonus of €100 per child and help the car industry by providing financial incentives to buy new cars.

Finance Minister Peer Steinbrück said the stimulus "won't prevent the recession but will help contain it."

Germany's budget deficit is likely to stay below the European Union's threshold of 3% of gross domestic product this year, but it probably won't stay below that level in 2010, Mr. Steinbrück said.

Steffen Kampeter, a lawmaker and budget spokesman for the ruling conservative parties, has said new government borrowing might hit a record of around €60 billion this year.

ECB expected to cut rates as inflation worries ease

By Nina Koeppen

FRANKFURT—Most economists say they believe the European Central Bank will continue with its monetary easing campaign and cut interest rates by half a percentage point Thursday to stem the risk of a deepening recession in the euro zone, although policy makers have given no clear signal about their decision.

Thirty-four of 42 private-sector banks polled by Dow Jones Newswires expect the ECB to cut the key policy rate to 2% from 2.5% currently. The ECB has already lowered interest rates by 175 basis points, or hundredths of a percentage point, since October, and rates are expected to drop to historic lows of around 1% by this spring.

The downturn is challenging policy makers, European Central Bank President Jean-Claude Trichet told the European Parliament Tuesday. "This is no time for complacency. Current challenges are pressing, and new challenges shall arise," said Mr. Trichet, speaking at a ceremony in Strasbourg, France, for the euro's 10th anniversary.

Six private-sector banks predict a quarter-point rate cut; only Merrill Lynch forecasts that the members of the ECB's Governing Council will make no change.

"Recent miserable economic data don't allow for a break in the recent rate-cut cycle, unless the ECB wants to run a significant risk of three-month Euribor rising again, and the euro spiking to $1.45," said Aurelio Maccario, chief euro-zone economist at UniCredit.

French Finance Minister Christine Lagarde urged the ECB to take into account the recent fall in euro-zone inflation, and the rapid deterioration of the economic environment. "I am confident that the ECB will appreciate that inflation is under control and that growth in the euro zone is key and vital for employment," she said.

Euribor rates—the Euro interbank offered rates, at which banks lend funds to each other—have been nudging lower, with the benchmark three-month rate falling to 2.612% from 2.653% Monday. Banks' continuing reluctance to lend to one another has pushed up interbank lending rates—a benchmark for some consumer and business loans across the euro zone, though some rates have been easing recently.

A steep decline in the euro zone's inflation rate and a benign price outlook also support the case for a January rate cut, economists said.

The euro zone's annual inflation rate dropped to 1.6% in December from 2.1% in November, preliminary estimates show. The ECB's medium-term goal is for an inflation rate just below 2%. Falling energy prices helped push German wholesale prices down by 3.3% in December 2008 from the year before, official figures showed Thursday.

Yahoo to name Carol Bartz as next CEO

By Jessica E. Vascellaro And Joann S. Lublin

Yahoo Inc. is expected to announce that Carol Bartz, former chief executive of software company **Autodesk** Inc., has accepted an offer to become the Internet company's next CEO, according to people familiar with the situation.

A spokesman for Yahoo, of Sunnyvale, Calif., declined to comment. Ms. Bartz couldn't be reached to comment.

The offer caps Yahoo's two-month search for a leader to succeed Jerry Yang, its co-founder and former CEO who oversaw the company through an acquisition offer from **Microsoft** Corp. Mr. Yang stepped down in mid-November after a short and tumultuous tenure at the helm in which he tried to save the struggling Internet firm, only to see it continue to flounder.

Ms. Bartz, 60 years old, will face a number of challenges as she tries to turn around Yahoo's flagging performance and stock price. Some investors have been lobbying for a breakup of the Internet giant, for instance.

Ms. Bartz still serves as executive chairman of Autodesk, of San Rafael, Calif., which she ran as chief executive from 1992 to 2006. Autodesk is about half the size of Yahoo, with approximately 7,000 employees world-wide.

Ms. Bartz was also an executive at Sun Microsystems Inc., and she sits on the board of Cisco Systems Inc. with Mr Yang. She is also a member of the Intel Corp. board with Yahoo President Susan Decker, who was also interviewing for the CEO job.

Ms. Bartz's appointment will likely reopen questions of Yahoo's strategic direction, potentially clearing the path for the company to restart negotiations with Microsoft over a sale of its search business. Microsoft CEO Steve Ballmer has publicly said in the past few weeks that a search deal with Yahoo should be made when there is a management transition at both companies. Microsoft late last year hired a Yahoo executive Qi Lu to lead its Internet business.

Ms. Bartz and Yahoo's board will also have to turn to other ways to right the business, which is being hurt further by the down economy. That could include striking a deal with another partner like **Time Warner** Inc.'s AOL or divesting of smaller business units.

With these major strategic questions in mind, Yahoo's board focused its CEO search on experienced executives with deal and operating experience, according to people familiar with the search. A few board members also raised their hands, according to people familiar with the matter.

Ms. Bartz has a track record of helping young companies grow and mature. She professionalized management practices at Autodesk and helped tame the eccentric culture set by the company's founder John Walker. Autodesk, which makes design software used in engineering, produced less than $350 million in revenue a year in the early 1990s when Ms. Bartz became CEO there but generated more than $1.5 billion in revenue by the time she stepped down in 2006.

Gas engines get fuel-savings boosts

Hybrids generate the hype, but new technology means traditional engines will dominate car market for years

By Matthew Dolan

Hybrids and electric cars are generating the buzz this week at Detroit's North American International Auto Show. But thanks to new technology, the century-old internal-combustion engine appears poised to make a significant leap in fuel efficiency.

While car makers are showcasing gas-electric hybrids, plug-in hybrids and concept cars powered by fuel-cell batteries, they also are rolling out new vehicles whose gasoline engines boast advances such as direct fuel injection.

Auto analysts say sales of vehicles with advanced gas engines will far exceed those of hybrids and electrics for years to come.

Sales of hybrids in the U.S. will rise to 578,000 by 2014 from 353,000 this year, according to CSM Worldwide. But the forecasting firm projects that sales of vehicles using more-efficient gas engines will jump to 5,082,000 by 2014 from 585,000 this year.

World-wide, electric vehicles, including plug-in and battery-only technology, will capture not much more than 10% of the global automotive market by 2020, according to a report by Roland Berger Strategy Consultants released this week.

"Leaping to a new technology is really a big risk," said Eric Fedewa, CSM's vice president of global powertrain forecasting. "It's much more cost effective and much less risk to do something to an existing, proven technology."

All auto makers are under pressure to boost fuel economy to meet stricter governmental standards. But consumers are fickle when it comes to buying superefficient vehicles.

Sales of **Toyota Motor** Corp.'s Prius, the best-known hybrid, zoomed last year when gas prices hit \$1.05 a liter in the U.S. But now, with gas costing less than half that, Toyota has seen Prius sales slow dramatically and it recently mothballed a U.S. factory slated to build the model.

Associated Press

The Ford Explorer America concept car at this year's Detroit show, where fuel efficiency ideas generated most of the buzz.

One big hurdle hybrids face is higher sticker prices, often thousands of dollars more than the same model with a traditional engine. It takes years for a customer to earn back this cost through gas savings.

The internal-combustion engine "will likely remain the backbone of mobility for the foreseeable future," said **Daimler** AG Chief Executive Dieter Zetsche. He said his company has been able to improve the efficiency of gas and diesel engines by about 23%. "There is still further to go."

At the car show, **BMW** AG displayed hybrid concepts of its 7-Series and X6 models that combine V8 engines with a two-mode hybrid to deliver a 20% improvement in fuel economy. But the German maker also predicted it could still squeeze out as much as 10% improvement in fuel economy with tweaks to its existing lineup of gasoline engines, said Klaus Draeger, a member of BMW's executive board.

Leading the way are direct-injection engines, which take highly pressurized fuel and thrust it squarely into the combustion chamber of each cylinder. By contrast, traditional engines mix fuel with the incoming air in the inlet port, which is less efficient. Car maker say the advantages are lower emissions, better performance and greater fuel efficiency.

Ford Motor Co. rolled out its EcoBoost technology, which promises greater performance while offering as much as a 20% increase in fuel economy over the same-size traditional engine. It will first be available later this year in the Ford Flex seven-passenger crossover wagon. By 2012, Ford expects to produce 750,000 EcoBoost vehicles annually, said Derrick Kuzak, Ford's global vice president for product development.

At **General Motors** Corp., 38 of its models will use direct-injection engines by next year, totaling about 10% of its global production. "On the journey to electrification of vehicles, we think we're going to need to make significant improvements in gasoline engines," said Sam Winegarden, GM's executive director of engineering.

GM and other makers are also racing to develop a viable gas engine using a technology called homogenous-charge compression-ignition, or HCCI. The technology is believed capable of providing as much as a 30% boost in economy by burning fuel faster at lower temperatures and reducing some of the energy lost during the combustion process.

"HCCI would be the next logical extension of improving the gas engine," Mr. Winegarden said, adding that HCCI is likely to hit the market within the next 10 years.

Major auto makers expect to present a varied lineup of vehicle technologies, but offer most with gasoline engines. "I don't think one technology will outdate another. They'll layer," said Jim Lentz, president of Toyota Motor Sales USA.

Much of the electrification strategy touted by auto makers counts on hefty incentives, including tax breaks to make buying a hybrid or battery-powered car easier on consumers' wallets. Without such incentives, the costs of creating a robust electric- and hybrid-car market will be prohibitively high, according to a new report from Boston Consulting Group.

Even environmentalists agree that improving the gas engine is a good, near-term solution. "There is no silver bullet, we need a silver buckshot," said Luke Tonachel, vehicles analyst with the Natural Resources Defense Council. "We need cars that go further on less gas. We'll need to embrace all of the technology."

—Kate Linebaugh and Jeff Bennett contributed to this article.

Toyota banks on retooled Prius

By Kate Linebaugh And John Murphy

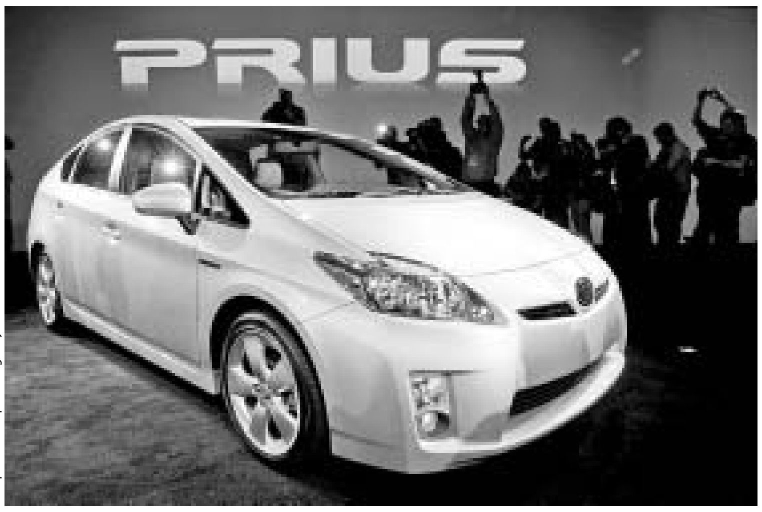
DETROIT—**Toyota Motor** Corp. is banking that its newly upgraded Prius will help lift its sagging global sales even as the hybrid market is becoming crowded, falling fuel prices have damped consumer interest in green cars and the world economy is expected to shrink.

In the U.S., Toyota aims to sell as many as 180,000 of the third-generation Prius vehicles in 2010, about the same volume sold in 2007.

Depending on the pace of a global economic recovery, the company seeks to sell 400,000 vehicles worldwide as it expands the number of countries in which the top-selling hybrid is offered to 80 from 44.

Toyota executive Bob Carter said the new midsize sedan would get a combined 21 kilometers a liter, compared with 19 on the current model. "We will continue to expand our hybrid line," Mr. Carter said in an interview at the North American International Auto Show.

Auto makers including **Ford Motor** Co. and **Honda Motor** Co. are bringing new hybrid vehicles to market as sales are taking a hit. Hybrid sales fell by half in December from a year earlier, according to Autodata



European Pressphoto Agency

A new Prius was displayed this week at the North American International Auto Show in Detroit. Toyota hopes this upgraded version of the hybrid will bolster sales.

Corp., while the overall market declined by more than a third. Sales of the Prius in the U.S. dropped 45% in the month from a year earlier and sank 12% over the year.

Last summer, when gasoline prices soared to \$1.05 a liter, Toyota struggled to keep pace with demand. Today, the company has 50 days' supply of the hybrid vehicle, more than what Toyota would like, according to Jim Lentz, president of Toyota Motor Sales U.S.A. The company expects to sell as many Prius cars in the U.S. as it did last year at about 160,000 vehicles, Mr. Carter said.

The new Prius that Mr. Carter said would be available in May has an expanded interior, a more aerodynamic exterior and a host of options, including a solar roof that powers the ventilation system.

Peugeot-Citroën sales declined 4.9% last year

By Geraldine Amiel

PARIS—**PSA Peugeot-Citroën** SA underlined the woes of the auto sector as it reported a 4.9% decline in sales for last year, although it maintained its global market share of 5%.

The French auto maker, which sells most of its cars in Western Europe, sold 3.26 million vehicles last year. Sales of assembled vehicles, which exclude kits that are exported and assembled elsewhere, dropped 8.7% to 2.95 million vehicles.

"These numbers are clearly terrible, but they should not come as a major surprise to anyone," Merrill Lynch said in a research note Tuesday. The bank noted that the French government is working on further support for car makers and said it expects Peugeot-Citroën to take more aggressive restructuring measures next month.

Peugeot-Citroën fared worse that local rival **Renault** SA, which last week said its global vehicle sales fell 4.2% last year. Peugeot shares closed at €14.30 (\$19.13), down 1.7%, in Paris on Tuesday.

In Western Europe, Peugeot-Citroën's sales of cars and light commercial vehicles dropped 11% last year. However, the company noted that even as sales collapsed in Western Europe, it maintained its 13.8% market share. Market-share gains in France and Germany were offset by declines in the U.K. and Spain.

Renault's European sales fell 7.2% last year, while its market share rose to 9% from 8.8%.

The Peugeot 308 and 308 SW models were key sales drivers, while the Citroën C5 helped beat its sales target in a segment under pressure, the company said.

The auto maker's range of ecofriendly vehicles also supported sales. For the third consecutive year, global sales of vehicles emitting less than 140 grams of carbon dioxide per kilometer were well above 1 million.

Peugeot-Citroën didn't provide an outlook for the current year. It is scheduled to report full-year earnings Feb. 11.

Over the past year, Peugeot-Citroën shares have tumbled more than 70% because of the steep drop in car sales and the global economic slowdown. *—William Horobin contributed to this article.*

CORPORATE NEWS

Retailers warn of trouble

Tesco and Metro expect a rough year as sales growth ebbs

By Cecilie Rohwedder

Associated Press

The U.K.'s Tesco and Germany's Metro Group said retail-sales gains slowed in the fourth quarter. Discounting, including at this central London store, cut results.

LONDON—Two of Europe's biggest retailers, **Tesco** PLC and **Metro Group** AG, predicted a tough year ahead as they reported a slowdown in sales growth over the holiday period and grappled with worsening economies in their home markets.

Tesco, the largest retailer in the U.K. by revenue, posted the slowest year-end sales growth in its British home market since the early 1990s. Metro, Germany's biggest retailer by revenue, said fourth-quarter sales rose significantly less than those in the first nine months of last year.

This year "will be a very difficult year," Eckhard Cordes, Metro's chief executive, said in a statement. "Customers will think twice where and for what they spend their money."

Both companies are changing in response to the slowdown, cutting costs and putting off expansion plans in an effort to protect their profit margins. Metro plans to curtail its international expansion to give itself "entrepreneurial flexibility," Mr. Cordes said. Tesco said in December that it would open fewer new stores in the U.K. this year, and has expanded its offerings aimed at cash-strapped consumers.

"There were challenging trading conditions in all our markets," said Lucy Neville-Rolfe, Tesco's corporate- and legal-affairs director.

The actions by Tesco and Metro—the world's biggest retailers after **Wal-Mart Stores** Inc., **Carrefour** SA and **Home Depot** Inc.—illustrate how the global economic and financial crisis is forcing retailers to abandon long-held growth strategies. Mergers and acquisitions in the retail sector have all but disappeared, while store renovations, development of new formats and real-estate deals have slowed sharply.

"The recessionary environment has completely changed retailers' attitudes and plans," said Simon Chinn, an analyst with retail consultancy Verdict Research in London.

Tesco, Metro and other grocery-store operators are performing better than many other retailers. On Monday, British sofa retailer **Land of Leather Holdings** PLC entered administration, a form of bankruptcy protection, joining music-store chain Zavvi, fashion chain USC and general retailer **Woolworths Group** PLC.

At Tesco total sales rose 11.6% in the seven weeks to Jan. 10, compared with a year earlier, boosted by sales outside the U.K. In the U.K., sales at stores open at least a year increased 2.5% over the same period, although the figure was skewed by the British government's recent cut in value-added tax. Without the tax cut, sales would have increased 3.5%—exceeding last year's gain of 3.1%.

Metro, meanwhile, said fourth-quarter sales rose 3%. Year-end sales benefited from international operations. For all of last year, sales rose 5.9% to €68 billion ($91 billion).

Elan reviews options, possible sale

By Jeanne Whalen

Irish biotech company **Elan** Corp., facing pressure from big shareholders unhappy with its performance, said it has started a "strategic review" that could lead to a sale of the company, a merger or an alliance.

Tuesday's announcement, however, frustrated some major investors, who said they would rather see the company cut spending and boost sales of its drugs.

Elan, based in Dublin, derives most of its sales from the multiple-sclerosis drug Tysabri, which it markets in partnership with U.S. biotech firm **Biogen Idec** Inc. It is also developing a closely watched drug for Alzheimer's with U.S.-based **Wyeth**.

Concerns about Tysabri's side effects and questions about the efficacy of the Alzheimer's drug caused Elan's shares to fall about 70% last year. Tuesday, the shares rose about 14% on the Irish Stock Exchange to €6.76 ($9.04), giving Elan a market capitalization of about €3.2 billion ($4.28 billion).

Elan said it has hired **Citigroup** to review its options, which "could include minority investment or strategic alliance, a merger or sale." It said its goal was to gain the money and commercial infrastructure it needs to get the drugs it has under development to market. Elan, which isn't profitable, needs to pay for costly studies of its experimental drugs, and to pay off its $1.8 billion in debt, $1.2 billion of which is due in November 2011.

A spokeswoman for Elan said it would prefer to avoid a full sale or merger. Any move could be complicated by Elan's partnerships with Biogen and Wyeth.

Some big shareholders expressed disappointment with the company's plans. Reached by telephone, Jack Schuler, who owns about 1% of Elan's stock and has lobbied for the removal of Kelly Martin as the company's chief executive, said he is against Elan selling stock "at this very low price." He said he also would oppose it selling the rights to some of its experimental drugs, because the company is in a weak position and wouldn't get good value for them.

"The company can clearly maneuver through their debt position in 2011 by just cutting expenses and improving the sales of Tysabri," he said.

Infosys cuts sales outlook, sees a tough year

Infosys Technologies Ltd. cut its revenue forecast for the current fiscal year and warned it could be 2010 before the struggling Indian tech sector gets back on its feet.

*By **Niraj Sheth** in New Delhi and **Rumman Ahmed** in Bangalore*

Infosys's results are the first released by an Indian technology company since **Satyam Computer Services** Ltd. co-founder and former chairman B. Ramalinga Raju was jailed last week after admitting to falsifying Satyam's accounts.

Bangalore-based Infosys, India's second largest tech company by sales, posted a 33% year-on-year rise in net profit to 16.41 billion rupees ($338 million) in the fiscal third quarter ended Dec. 31, partly on the back of a weakening rupee.

Quarterly revenue was 57.86 billion rupees, up 36% from a year-ago. But the company recorded its first-ever sequential decline in dollar revenue, which fell to $1.17 billion in the December quarter from $1.22 billion in the September quarter.

Infosys also lowered its revenue forecast for the fiscal year ending March 31 to $4.69 billion from its earlier guidance of $4.77 billion, which was issued in September.

The once-booming Indian tech industry has hit a sharp slump as the global economic slowdown makes companies more hesitant to sign multi-year outsourcing contracts.

Infosys Chief Executive Kris Gopalakrishnan said he expects the difficult business environment to continue until "the end of 2009 or beginning of 2010."

But Mr. Gopalakrishnan indicated that Infosys may stand to benefit from the accounting scandal at Satyam. In an interview, he said some Satyam customers have approached Infosys about transferring outsourcing work away from the company, now the target of a fraud investigation.

German discounter Aldi invades Wal-Mart's turf

By Cecilie Rohwedder And David Kesmodel

German store chain **Aldi** is so cheap that **Wal-Mart Stores** Inc. closed its discount outlets in Germany two years ago partly because shoppers found the U.S. giant too expensive in comparison.

Now, the U.S. arm of Aldi is cranking up expansion in Wal-Mart's home turf and seizing on the economic downturn to lure consumers to its Spartan stores and cheap groceries. The discount chain will open at least 75 U.S. stores this year, well above its typical pace, including its first Aldi store in New York City.

The company is counting on the economic downturn to crash a traditional barrier to the U.S. grocery business: Americans tend to be loyal to big-name brands.

Store-brand goods generally make up 22% of U.S. food sales in terms of unit volume, according to research by Nielsen Co., while in some European markets, they account for about 30%. At Aldi, 95% of the goods are the retailer's own brands.

Aldi's expansion shows how the tough economy is changing the competitive landscape across industries. Aldi first arrived in America in 1976 cramped. It is adding more fresh produce, designed to lure middle-class shoppers. And it is running television commercials, a change for the company whose marketing was long limited to a weekly newsletter highlighting low prices.

But the essence of the business is low prices through store-brand foods. It buys in bulk from suppliers and commissions them to make its own store brand of groceries cheaper than rivals. In the U.S. Midwest, for example, its prices are between 15% and 20% less than Wal-Mart and 30% to 40% cheaper than regional chains, said David Livingston, a supermarket analyst with DJL Research in Waukesha, Wis.

The chain locates new stores near Wal-Mart Supercenters, to draw customers, he says.

Aldi has been able to grow quickly under the radar, in part, because the company is so private. The two branches of the family-owned company, Aldi Süd and Aldi Nord, are controlled by a series of Albrecht family trusts. They don't report results, but consultancy Planet Retail estimates $66.38 billion in combined annual sales. Aldi Nord owns California-based Trader Joe's specialty food stores.So far, the group's biggest U.S.

Aldi

Aldi's U.S. push relies on new layouts, with higher ceilings and more windows, along with abundant produce. A Geneva, Ill., store showed the changes last spring.

and began opening what has now become a collection of 1,000 U.S. stores, mostly in the Midwest and Northeast.

"This is the perfect confluence of factors for us," says Jason Hart, president of Aldi's U.S. division. He is charting a push into the Dallas-Fort Worth area next year with 25 new stores and a $40 million distribution center that will serve stores planned for Texas and Oklahoma, prime Wal-Mart territory.

A Wal-Mart spokeswoman said Aldi's plans wouldn't affect its price strategy or operations.

Supermarket chains such as **Safeway** Inc. and **Kroger** Co. are reporting higher sales of store-branded products. Mr. Hart and other Aldi executives say they had planned to expand before the downturn, but the moves have new urgency.

The push comes as the retailer is running out of room to grow in its German home market, where an estimated 90% of households shop at its stores, and Aldi and other deep discounters account for 40% of all grocery sales.

For expansion in the U.S. and Britain, where it is also building new stores, Aldi tweaked its retail formula. New stores have higher ceilings and more windows to make the 17,000-square-feet outlets feel less market is the Chicago area, where it has 157 stores.

With the latest expansion, Aldi is correcting its past mistakes in the U.S. and U.K. In the years after its launch in the U.S. and 1990 arrival in Britain, Aldi opened unattractive stores in low-income areas and sold very few products with hardly any fresh food, for instance.

In Germany, Aldi eventually improved its food ranges and offered more upscale products in its twice-weekly non-food promotions. The changes brought in middle-class shoppers with more disposable income.

The retailer aims to repeat this strategy in the U.S. and Britain. But Aldi has a long way to go to attain the type of influence it does in Continental Europe, where it has shaped shopper habits. Planet Retail expects Aldi's U.S. 2008 sales climbed 21% to $7 billion. Wal-Mart has $374.5 billion in U.S. sales, although much of that business comes from nonfood items. Kroger, the largest grocery store chain in the U.S., has $70.2 billion.

"If you asked me to list our top 10 competitors in the U.S., Aldi wouldn't be on it," said John Rishton, chief executive of Dutch retailer **Ahold** NV, which owns Stop & Shop and Giant-Landover grocery chains in the U.S.

CEO firings are on the upswing as economy heads down

U.S. companies sack six chiefs in a week; more turmoil ahead

BY JOANN S. LUBLIN

A deepening labor market downturn that cost 524,000 Americans their jobs last month is even swelling the jobless rate for chief executives.

William Watkins, ousted Monday at **Seagate Technology** LLC, is the sixth CEO of a publicly held company to be replaced in just the past eight days. His exit follows the departures last week of CEOs at **Tyson Foods** Inc., **Borders Group** Inc., **Orbitz Worldwide** Inc., **Chico's FAS** Inc. and **Bebe Stores** Inc.

Many experts view the changes as harbingers of more turmoil in executive suites this year. Like other companies, these six corporations have been grappling with poor financial results, slumping stock prices and, in some cases, investor criticism.

An informal survey of management consultants, recruiters, investors and governance specialists pointed to several other CEOs whose jobs may be vulnerable: Rick Wagoner of **General Motors** Corp.; Vikram Pandit of **Citigroup** Inc.; Jonathan Schwartz of **Sun Microsystems** Inc.; Steve Odland of **Office Depot** Inc.; and Kenneth Lewis of **Bank of America** Corp. Officials at those companies said their CEOs retain the board's support or declined to comment.

CEO turnover "doubles in bad times," said Dirk Jenter, an assistant finance professor at Stanford University's business school, who recently analyzed 1,627 CEO changes between 1993 and 2001. Mr. Jenter found that CEOs are most vulnerable in a downturn when their employers' shareholder returns lag rivals.

Last year, 61 companies in the Standard & Poor's 500-stock index changed CEOs, up from 56 a year earlier, according to executive search firm Spencer Stuart. The number of such switches may increase this year, Mr. Jenter predicted. Boards typically oust CEOs a year or two after relative shareholder returns start to slip, he said.

"As bad times drag on, you begin to examine the leader's response," observed Charles Elson, a director at HealthSouth Corp. and head of the Weinberg Center for Corporate Governance at University of Delaware's business school.

Executives of corporations based outside the U.S. are leaving as well. Anglo-Australian mining company **Rio Tinto** PLC on Monday said Dick Evans, chief executive of its aluminum division, plans to retire and will leave the board on April 20. Norwegian electric power and aluminum producer **Norsk Hydro** ASA also said its CEO is stepping down.

Seagate removed Mr. Watkins at the same time it announced plans to eliminate 10% of its workforce. The maker of computer disk drives warned of disappointing sales in December, and its shares have lost 80% of their value in the past year.

Borders and Tyson also had sharp share losses under their old CEOs. Borders shares fell about 97% under George Jones, who took over in July 2006.

The turmoil extends to senior executives below the CEO. New chief executives often replace top lieutenants to create their own team. With the recession, "this is the most volatile environment I've seen in 30 years," observes Peter D. Crist, head of Crist|Kolder Associates, a search firm in Hinsdale, Ill.

Harry Pearce, chairman of **Nortel Networks** Corp. and a retired vice chairman of GM, also expects more CEO departures. Mr. Pearce thinks many of these changes will be ill-advised. "It's probably the worst time to make a change," Mr. Pearce said. Hiring a leader during crisis "almost invites bad decisions" because a newcomer must act fast before fully grasping the business, Mr. Pearce said. He declined to comment on the future of Nortel Chief Executive Mike Zafirovski, who has been running the troubled telecommunications equipment maker since 2005.

Switching CEOs is rarely a panacea. A June 2008 Wall Street Journal survey of 30 big companies that removed CEOs between January 2005 and June 2007 revealed that the shares of those companies had declined far more often than they had increased. (The survey excluded financial-services CEOs who had lost jobs amid the credit crisis.)

Several of the CEOs considered vulnerable this year are relative newcomers who have been unable to halt declines in their employers' fortunes. Mr. Pandit was named CEO at Citigroup in December 2007, amid multibillion dollar losses tied to the mortgage crisis. But Citigroup remains unstable.

Federal officials discussed removing Mr. Pandit as part of the second bailout, but decided that his ouster could destabilize the company, people familiar with the talks have said. Citigroup's lead independent director, Richard Parsons, said Sunday the board retains confidence in Mr. Pandit and is not considering his removal.

Bank of America's Mr. Lewis won praise last year for steering the bank through the worst of the mortgage mess, while acquiring Countrywide Financial Corp. and this year Merrill Lynch & Co. at bargain prices.

Now, some analysts question whether those deals will ultimately hurt the bank, which halved its dividend in October. B of A shares have fallen more sharply than other banks in the past month. Mr. Lewis "is under a lot of pressure," Mr. Elson said.

Sun has struggled to find a formula for consistent growth since the Internet boom. Mr. Schwartz replaced Sun co-founder Scott McNealy in 2006, but Sun continues to lag behind bigger rivals such as **Hewlett-Packard** Co. Sun's shares fell about 75% last year. H-P's slid about 25%.

Other potentially vulnerable CEOs face longer-standing problems. Mr. Wagoner has led GM since 2000, a period in which its market share has shrunk and its shares have fallen about 94%. Some members of Congress urged Mr. Wagoner to resign when GM sought a federal bailout last fall. GM directors have backed him publicly.

Office Depot lags larger rival **Staples** Inc., and recently halved plans for new store openings this year. Last year, dissident shareholders threatened a proxy fight, claiming that management used economic weakness as an excuse for its "persistent underperformance."

Neil Austrian, the board's independent lead director, said in a statement that Mr. Odland "is doing everything possible" to improve performance.

Seagate shakes up top management

BY DON CLARK

Disk-drive giant **Seagate Technology** Inc. announced a surprise management shake-up that replaced the outspoken Chief Executive William Watkins with Chairman Stephen Luczo.

The company also said David Wickersham had resigned as chief operating officer, effective immediately.

Seagate confirmed Monday that it plans to reduce its work force by about 10%, a move discussed by Mr. Watkins and another Seagate executive at the Consumer Electronics Show last week.

Mr. Watkins's high visibility at the trade show made the timing of his replacement seem abrupt. Asked to explain the changes, a Seagate spokesman said only that "the board just felt that at this time Steve Luczo was the right guy to take the company forward."

Mr. Watkins and Mr. Wickersham couldn't be reached for comment.

William Watkins

Mr. Luczo, 51 years old, first became CEO after the sudden firing in 1998 of Chief Executive Alan Shugart, the company's maverick co-founder. Mr. Luczo, who had been president and chief operating officer, helped take Seagate private in a leveraged buyout and then go public again.

Mr. Watkins, who succeeded Mr. Luczo as CEO in 2004, had previously helped oversee a restructuring that took Seagate's work force from about 111,000 people to 35,000, and made Seagate's factories much more flexible and efficient, said John Monroe, an analyst at Gartner.

Mr. Watkins, 56, became rich enough to buy several homes—including a posh beach house near Santa Cruz, Calif., with a stretch of private beach. He often dressed in blue jeans and had a reputation for candor that sometimes caused public-relations problems.

More recently, Seagate and its rivals were whipsawed by excess manufacturing capacity, followed by a slump in demand. In December, the company warned that its revenues in the second period would be lower than expected.

—Jerry Dicolo contributed to this article.

CORPORATE NEWS

Harley stock skids further

Goldman downgrade, woes at finance unit weigh on share price

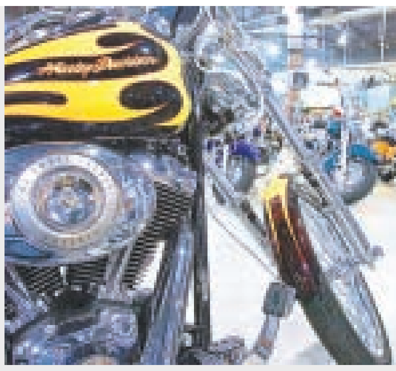
By Susan Carey

Investors continued to steer clear of **Harley-Davidson** Inc. in the wake of Goldman Sachs Group Inc.'s "sell" recommendation.

On Monday, Goldman cut its investment rating on Harley to "sell" from "neutral" amid flagging demand for motorcycles and rising credit costs. Goldman estimated that retail motorcycle sales in the U.S. will be down 30% this year and predicted a 95% year-to-year decline in operating profit at the financial-services unit because of higher funding costs and declining credit quality.

The company declined to comment on the Goldman report.

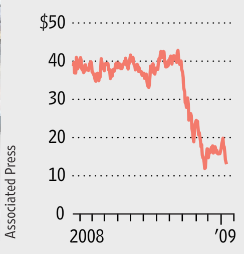
Separately, Harley said last week that Sy Naqvi, president of the company's finance unit since February 2007, decided to resign, effective immediately. Mr. Naqvi, 59 years old, joined Harley from DeepGreen Financial Inc. Harley Chief Financial Officer Tom Bergmann, 42, will assume Mr. Naqvi's post while the company embarks on an external search for a successor.



Harley-Davidson motorcycles on display at a dealership in Omaha, Nebraska.

Downhill ride

Harley-Davidson's daily share price



Source: WSJ Market Data Group

Harley-Davidson Financial Services helps consumers finance their motorcycles and independent dealers their inventory. In the third quarter, the finance unit's operating income declined 28% to $35.6 million from $49.5 million a year earlier. Due to turmoil in the credit markets, the unit failed to book any income from selling loans to third parties in the period. A year earlier, the unit completed a $782 million securitization transaction, with a gain of $3.5 million.

In October, Harley said it hoped to access the debt market in the fourth quarter to raise between $300 million and $500 million for the financial-service unit, which faced a payment of $400 million of debt due in December. In a Dec. 12 federal filing, Harley said it raised $500 million in a short-term loan backed by motorcycle-sales receivables.

The company, citing plans to release its fourth-quarter results on Jan. 23, declined to comment beyond the news release about Mr. Naqvi's departure.

The Milwaukee-based company's stock slipped to $13.75, down 38 cents, or 2.7%, in mid-afternoon composite trading Tuesday on the New York Stock Exchange. On Monday, the shares had sunk 12%, or $1.87, to $14.13 in 4 p.m.

Air France CEO hails Alitalia deal

By Daniel Michaels

The chief executive of Franco-Dutch airline **Air France-KLM** SA said its acquisition of a minority stake in Italy's **Alitalia** SpA, which has recently been recreated through a bankruptcy proceeding, was "nearly an ideal case."

Alitalia's Italian managers had the advantage of "defining the company at the bottom of the market," said Air France-KLM CEO Pierre-Henri Gourgeon. The two carriers announced on Monday that Air France-KLM would invest €323 million ($432 million) for 25% of the new Alitalia.

"We picked the assets, we didn't take the debt. The cost of redundancies is covered by the government, and we have new employment contracts," Mr. Gourgeon said in an interview. He added that by establishing the new airline now, amid a deep industry crisis, the operation should be well positioned for growth.

The agreement will give Air France-KLM "the best possible access to the Italian market," Mr. Gourgeon said.

He acknowledged that Alitalia, which has recently been merged with Italian rival Air One SpA, faces a challenge in regaining its footing after foreign rivals invaded the rich Italian market over recent years. He added that labor strife, long a problem for Alitalia, could still hurt the operation. "I hope that staff will concentrate for a while on rebuilding Alitalia," Mr. Gourgeon said.

Separately, Air France-KLM Chairman Jean-Cyril Spinetta said in a radio interview that the company may consider increasing its stake further, but only once a four-year shareholder pact ends.

A lockup agreement will be in place through January 2013, stipulating that no Italian shareholder will be able to transfer shares externally to Air France-KLM or the group of Italian shareholders financing Alitalia's reflotation.

—Geraldine Amiel contributed to this article.

Green group buys plot near Heathrow

Associated Press

LONDON—An environmental coalition led by Greenpeace announced Tuesday it had purchased a plot of land on ground earmarked for a proposed third runway at London's chronically congested Heathrow Airport.

The group, which includes Oscar-winning actress Emma Thompson, said it bought the land, roughly half the size of a football field, for less than £25,000 ($37,000) in the village of Sipson, where hundreds of family houses will be destroyed if the runway project goes forward.

Greenpeace director John Sauven said the new owners will never sell the property, roughly half the size of a football field, to the government or airport operator BAA Ltd., a unit of **Grupo Ferrovial** SA.

"The legal owners of the site will block the runway at every stage through the planning process and in the courts," he said. "And if it comes to it many thousands of people will be prepared to peacefully defend their field in person, standing in front of bulldozers and blocking construction."

A much-delayed decision on the runway plan will be announced this month, said Prime Minister Gordon Brown's spokesman. He added that the government has already agreed in principle to add capacity at Heathrow as long as it doesn't lead to Britain violating European air-pollution targets.

The prime minister's cabinet appears divided over the issue, which pits environmental concerns—and Britain's commitment to controlling climate change by reducing carbon emissions—against economic growth and job creation. Some supporters believe the runway would help create 65,000 new jobs.

Ms. Thompson, one of Britain's best-known actresses, said she had joined the group that purchased the land because it was "hypocritical" for the government to promise to reduce greenhouse gases while greatly increasing air-traffic capacity.

The expansion plan has also sparked fierce opposition from legislators representing towns and villages that would be adversely affected by the increased air traffic. One of the new land owners, Conservative Party environmental adviser Zac Goldsmith, said the coalition hopes to use the land to slow down and ultimately kill Heathrow expansion.

"Eventually the government will probably be able to buy the land through compulsory purchase, but the question is how long it will take them," said Mr. Goldsmith, who plans to run for Parliament from Richmond Park, one of the affected districts. "I think this one single act will prevent anything from happening before the next election."

He said that could effectively end the expansion plan since the Conservative Party, which enjoys a healthy lead in opinion polls, opposes construction of a third runway. Britain's next general election must be held by the middle of next year.

GLOBAL BUSINESS BRIEFS

Aegon NV

Ernst executive is proposed as successor to finance chief

Dutch life insurer and pension provider **Aegon** NV said Chief Financial Officer Jos Streppel is retiring April 22 and Jan Nooitgedagt will be proposed as his successor. Mr. Nooitgedagt, 55 years old, is chairman of Ernst & Young's Benelux operations. "Although the retirement of Mr. Streppel doesn't come as a surprise, we believe the current turmoil demands predictability and confidence," said SNS Securities analyst Maarten Altena, adding that Mr. Nooitgedagt "has the required capabilities and experience to successfully guide Aegon through the current difficult circumstances." Mr. Streppel has been Aegon's finance chief since 1998. Mr. Nooitgedagt's appointment is subject to approval by the Dutch central bank.

EADS

Louis Gallois, chief executive of **European Aeronautic Defence and Space** Co., said the company pulled out of a "significant" acquisition of a U.S. defense company after the board decided protecting cash is a bigger priority. The Airbus parent was "on the way to send the check" at the end of last year when the board intervened, Mr. Gallois said at a news conference. He declined to name the target, saying it has since had "fantastic success" with a big order from the Pentagon, but stated that it wasn't Lockheed Martin Corp. EADS had cash reserves of €9 billion ($12 billion) at the end of last year. "We need this cash to protect the company and we need this cash to support our customers and, sometimes, our suppliers" who are struggling to raise funds, he said.

Volvo AB

Swedish truck maker **Volvo** AB said Tuesday it will lay off more than 1,600 employees in Sweden as it slows production amid falling demand. The layoffs will be in addition to more than 2,000 job cuts announced by the truck unit last year, Volvo spokesman Stefan Karlsson said. He said the new cuts involved about 1,020 workers at two production plants in Sweden and 600 workers at Volvo's Powertrain unit, which makes engines, gear boxes and rear axles for trucks. "The reason for this is primarily a weak order intake right now and that there are no real signs of improvement," said Mr. Karlsson. In the last few months, Volvo has laid off several thousand workers in its trucks, heavy machinery, Powertrain and information-technology divisions.

Beiersdorf AG

German cosmetics company **Beiersdorf** AG, maker of the Nivea brand, Tuesday said its 2008 net profit rose 25% amid robust demand for its hair and skin-care products, but it missed its 2008 sales target because of weakness in its adhesives unit, Tesa. Net profit rose to €553 million ($740 million) from €442 million a year earlier, while sales increased 8.3% to €5.97 billion. However, organic sales—stripping out currency fluctuations and acquisitions—rose just 7.5%, missing the company's target for growth of more than 8%. The adhesives unit, Tesa, recorded a slight decline in sales to €845 million from €846 million last year, partly because of the slowdown in the automotive industry. Beiersdorf's shares declined about 20% in value in 2008.

Eurostar Group Ltd.

Eurostar Group Ltd., the high-speed passenger-train service linking Britain to mainland Europe, said ticket sales rose 11% last year, boosted by shoppers from Europe looking to cash in on the pound's weakness. Eurostar said it carried 9.1 million passengers last year, up 10% from a year earlier. Ticket sales reached £664 million ($984 million) and would have been higher were there not a Sept. 11 fire in the rail line's tunnel, the company said. Eurostar is still operating at only 90% of capacity because a 16-kilometer section of the tunnel is under repair, adding an extra 20 minutes to travel time. Full service is expected to be restored in the spring. Chief Executive Richard Brown said the outlook for this year is "optimistic" compared with most businesses but that growth won't be as strong as last year.

Pernod Ricard SA

French spirits company **Pernod Ricard** SA Tuesday said sales in its fiscal first half were "satisfactory" and in line with its forecast, thanks to good holiday sales. In a statement ahead of releasing full earnings on Feb. 13, the owner of brands such as Beefeater gin and Mumm champagne said it still expects sales to have grown about 5% organically in the six months ended Dec. 31 and that it now sees double-digit growth in net profit from recurring operations. "Most emerging markets have continued enjoying strong growth, particularly China, India and Eastern Europe," the company said. Countries such as France and Germany showed good growth, while Spain, South Korea "encountered difficulties" and U.S. retailers cut inventories, Pernod Ricard said.

Taylor Wimpey PLC

U.K. house builder **Taylor Wimpey** PLC said Tuesday that it will have to make further write-downs when it reports full-year results unless market conditions improve. The company said it continues to believe the U.K. and U.S. housing markets won't recover in the short term. U.K. house builders have been struggling amid some of the worst market conditions in decades, with a squeeze on mortgage availability and low investor and customer confidence. Taylor Wimpey has been hit harder than rivals as its debt weighs on its balance sheet. Its net debt as of Dec. 31 stood at £1.55 billion ($2.3 billion), reduced by £300 million since June 30 as a result of cost cutting and a reduction of levels of work in progress. Taylor Wimpey shares were down 20%.

The Washington Post Co.

The Washington Post Co. on Tuesday named Elizabeth Spayd and Raju Narisetti as managing editors under the paper's new executive editor, Marcus Brauchli. Ms. Spayd, 50 years old, and Mr. Narisetti, 42, succeed the top two lieutenants Mr. Brauchli inherited when he joined the Post in September. Those editors, Washingtonpost.com Executive Editor Jim Brady and Managing Editor Philip Bennett, resigned recently. As expected, Mr. Brauchli has redefined those roles. Ms. Spayd will oversee political, general, business, foreign and local news. Mr. Narisetti will assume responsibility for day-to-day operations of the paper's Web site and also oversee the Style and Weekend sections, The Washington Post Magazine and video, design and photography.

—Compiled from staff and wire service reports.

FOCUS ON ENERGY

Pickens's windmills tilt against realities

Billionaire's plan for renewable energy faces tall hurdles

BY NEIL KING JR.

WASHINGTON—He boasts his own self-declared army and the support of 13 U.S. governors, 53 congressmen and 180 mayors, along with the Sierra Club and the American Lung Association. He has plugged his cause on countless news shows and spent $60 million of his own money on a massive ad spree.

Now T. Boone Pickens is about to find out which has more oomph: all of the above, or a $100 drop in the price of oil.

The flinty Dallas billionaire is going all out to sell American lawmakers and the next administration on his plan to wean the U.S. off Middle East oil by ramping up the use of wind power and natural gas.

Trouble is, energy markets, and a fair share of skeptics, keep tilting against him.

When the 80-year-old oil magnate launched his vaunted Pickens Plan on July 8, crude oil was at $136 a barrel and rising. Crude has since slumped to below $40 a barrel, as have public concerns over oil supplies and the urgent need for alternatives.

"Cheap oil doesn't help," says Mr. Pickens, who predicted in July that oil would never again dip below $100 a barrel. "It just means we have to work harder."

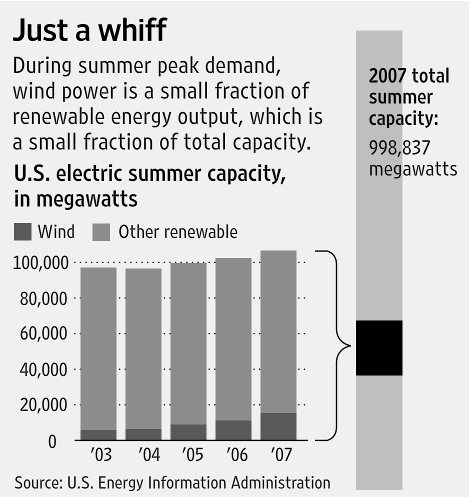
Not since fellow Texas oilman H. Ross Perot dropped $65 million on his 1992 presidential quest to block the North American Free Trade Agreement and rid the country of its national debt has any lone U.S. citizen thrown similar cash and zeal into a public cause.

"This to me is like a war without guns," says Mr. Pickens between a flurry of meetings one recent morning in his hotel suite across from the White House.

The folksy Oklahoma native and his much-touted energy plan have hit some rough spots recently. Mr. Pickens now hopes that a last burst of advertising, plus grass-roots help from his growing legion of volunteers, will get the new Congress to turn at least parts of his plan into law. He was in Washington Tuesday to meet with lawmakers, including House Speaker Nancy Pelosi.

Mr. Pickens's original vision had something for everyone. First he would build a wind farm in Texas with 2,700 turbines costing upward of $10 billion. That would pump power into the national grid, allowing huge amounts of natural gas to be diverted from power plants to newly equipped cars and trucks.

Getty Images



The result, he promised, would be a sharp reduction in the country's dependence on Middle East crude.

But the credit crunch gutted the wind project's financing, putting all those turbines on hold. "The wind stuff is deader than hell right now," he concedes.

By October, the value of Mr. Pickens's own equity hedge fund, BP Capital, fell by around 60% from its peak in late June.

Mr. Pickens suffered another jolt in November, when California voters resoundingly defeated a ballot measure he supported to put $5 billion in bond money into promoting natural-gas vehicles in the Golden State. Mr. Pickens's own company, **Clean Energy Fuels** Corp., the largest owner of natural-gas filling stations in the U.S., sponsored the plan and put up $19 million to back it.

Then there was the long swoon in oil prices, which have now driven fuel costs down to their lowest level in years. Mr. Pickens pitched his plan as the best way to slash America's foreign-oil tab by a third within 10 years. Plunging prices managed to do that work, it turns out, in less than six months.

A rangy man who still works out almost every morning, Mr. Pickens banks heavily on his own mystique for bucking adversity and making vast fortunes. "I have lived through 14 presidents, one Depression and as many booms and busts as you can imagine," he says in his most recent TV spot, set to air extensively in the Washington area this month.

A lifelong Republican who helped fund the Swiftboat attacks on Sen. John Kerry during the 2004 presidential campaign, Mr. Pickens took his plan first to President George W. Bush. The two men met in the Oval Office in April.

"The president sat and listened for an hour and a half," Mr. Pickens says. "And then nothing happened. No call back. Nothing. So I decided to do it myself."

He didn't fare much better with the two presidential nominees. When he sat down with Sen. John McCain in August, the Arizona Republican chastised him for "trying to pick winners" by so openly favoring natural gas. President-elect Barack Obama seemed more amenable when the two met in a hotel conference room in Reno, Nev., a few weeks later.

Mr. Pickens sketched out his plan in series of pie charts on a white board. "He didn't do any back flips or anything but he did seem to like what I was saying," Mr. Pickens says.

Mr. Pickens hasn't been shy about tweaking his plan to keep abreast of critics and the collapsing market. He first proposed that Congress mandate that all new fleet vehicles run on natural gas. That went down with a loud thud among critics such as Fred Smith, chief executive of FedEx Corp., whose massive fleet includes 672 aircraft and more than 80,000 motorized vehicles.

Mr. Smith, who declined to comment, argues that the best way to curb America's oil use is to convert to electric cars and delivery trucks. He opposes the Pickens plan's heavy focus on natural gas, saying it would require onerous additions to the country's infrastructure and deepen the reliance on fossil fuels. An influential group of corporate CEOs and former generals that he is co-chairman of, called Securing America's Energy Future, is of the same view.

So Mr. Pickens shifted his focus to the country's truckers, saying that all new long-haul trucks should be required to run on natural gas. That didn't sit well with former Kansas Gov. Bill Graves, who heads the American Trucking Association.

The son of a truck operator, Mr. Graves laid out his objections over breakfast recently in Mr. Pickens's suite. Many U.S. companies, he noted, are already turning to diesel hybrids. Natural gas-run trucks are about a third more expensive than traditional diesel trucks. Nationwide filling stations for natural gas don't exist.

"How do you just airlift in the infrastructure to make this happen?" he said.

Mr. Pickens has recently taken to labeling his critics as un-American. Mr. Graves got the full dose.

"Bill, I just want to warn you on this," Mr. Pickens said, putting down his fork. "I'm going to make you look unpatriotic for supporting foreign oil. I just want to make sure you understand that."

Taken aback, Mr. Graves pointed out raspberries and croissants arrayed before them. The foreign oil helped deliver the food, he said. "We wouldn't have any of this here if our trucks hadn't delivered it," he said. "So what's more patriotic, Boone?"

Since July, Mr. Pickens has logged more than 300 hours aboard his personal jet and spent five days a week outside of Dallas. His office says that, to date, word of his plan has reached 1.8 billion U.S. newspaper readers and TV watchers—every American, that is, six times over.

Mr. Pickens is also amassing a nationwide cadre of supporters, including a "Pickens Army" of 1.3 million online adherents. One such foot soldier is Ryan Jones, a 32-year-old automation student at Idaho State University in Pocatello. The goal is to have one designated foot soldier in all 435 congressional districts. Mr. Jones, who helped convert Pocatello's mayor, is now planning a recruitment party at the local brewery to "get some people signed up," he says.

Still, for all his labors, Mr. Pickens appears likely to fall short in his quest to force some mass conversion to natural gas-fueled transportation in the U.S. anytime soon. Legislation now in the works, top congressional aides say, will probably include some tax incentives to get companies to reduce their oil consumption, but not much more.

Mr. Pickens promises to push on. "We've been on this energy yo-yo for 40 years," he says. "We are going to pay an unbelievable price if we don't get this right."

Green companies grow, counting on Obama

BY SIMONA COVEL

While many small businesses continue to struggle with tight credit and declining sales, one fledgling industry is seeing a boom in investment and sales growth: alternative energy.

Alternative-energy firms are reporting an influx of inquiries and business from a wide range of companies looking to increase their energy efficiency, especially from those that believe the Obama administration will impose stricter regulations requiring them to conserve energy. President-elect Barack Obama has spoken often of the importance of alternative energy, also known as clean technology, and his federal stimulus package is expected to include plans to beef up alternative-energy infrastructure and improve energy efficiency in government buildings. In a speech last week, he called for the U.S. to double the production of alternative energy in three years.

So start-ups across a variety of areas—solar power, biofuels and energy conservation among them—are getting increased financing from venture capitalists and lenders at a time when other small companies are cutting back and being turned away by investors. And many are hiring more staff, boosting marketing efforts and expanding geographically.

Alternative energy "has been the brightest sector in venture capital over the last year," says Brian Fan, research director at Cleantech Group, a San Francisco company that provides information and research about the industry. "Everyone is thinking it's going to be a big priority of the incoming administration."

While the overall volume of venture-capital deals sank last year, investments in clean-technology companies totaled $8.4 billion, up nearly 40% from 2007, according to Cleantech Group. In the third quarter alone, venture capitalists poured $2.6 billion into clean technology, a quarterly record. In the fourth quarter, they invested $1.7 billion.

Some venture capitalists think clean technology is the next big thing—the innovation that will drive the economy, much as Internet-related ventures did a decade ago. "Anytime big innovation comes along, it brings the chance to build big companies," says Erik Straser, general partner at venture-capital firm Mohr Davidow Ventures in Menlo Park, Calif., which has investments in several alternative-energy start-ups.

But whether the administration will turn to energy initiatives quickly enough for all these companies to reap the rewards remains to be seen. And unlike with other new types of technology companies, the growth of clean technology "depends on the right kind of government policies and incentives," Mr. Fan says, because implementation requires a certain amount of infrastructure and tax credits to offset the expense for users.

Just the anticipation of a new administration has been enough to spur interest among companies. **Green Panel** Inc., a solar technology and installation company in Brighton, Mich., is planning to add four employees to the 14-person, two-year-old firm over the next few weeks to handle new business that has come in since the election. Even though no new energy regulations are in place yet, big companies are starting to take a look at alternative-energy options, says Adam Harris, Green Panel's chief executive. He says one industrial firm held off on an order of solar panels until after the election. And he has heard from firms whose executives want to have systems in place ahead of any regulations for big companies.

The firm expects to double its revenue this year to nearly $4 million.

Executives at venture-capital-backed **Greenline Industries** Inc., a Larkspur, Calif., maker of biodiesel production equipment, believe the Obama administration will create a huge demand for biodiesel and other advanced biofuels. The president-elect has said he'll require that 60 billion gallons, or some 227 billion liters, of advanced biofuels are produced by 2030, spurred by tax incentives and government spending.

Greenline, which has 35 employees, declines to offer specific projections but plans to triple its sales staff in the coming weeks.

"It's a reaction to the administration change and to changes we expect as a result of the people [Mr. Obama] has picked—the policies that will be happening and the growth in demand we expect," says Donn Tice, Greenline's chief executive. The company's latest round of venture-capital financing was in March, for $20 million.

Clinton calls for 'smart power'

Obama pick for secretary of state, at hearing, says U.S. should engage with Iran and Syria

By Patrick Yoest

WASHINGTON—Sen. Hillary Clinton called for the use of "smart power" in her bid to become the next secretary of state, arguing Tuesday that the U.S. should engage hostile powers such as Iran and Syria, and pursue partnerships with China and Russia.

"I believe that American leadership has been wanting, but is still wanted," Sen. Clinton said in remarks at her confirmation hearing in the Senate Foreign Relations Committee.

With daughter Chelsea in attendance, Sen. Clinton appeared to sail smoothly through her hearing before the Senate panel, despite concerns among some lawmakers that the global fund raising of her husband, former President Bill Clinton, could pose ethical conflicts for her as secretary of state.

During the hearing, Sen. Clinton, 61 years old, emphasized areas of foreign policy in which she and President-elect Barack Obama think alike, including their conviction that in order to make gains abroad the U.S. needs to strengthen its domestic economy.

Like Mr. Obama, Sen. Clinton has said the U.S. should make a more focused commitment to stabilizing Afghanistan and pushing Pakistan to eliminate the havens al Qaeda terrorists have found on its territory. Both favor closing the prison for terrorist suspects at Guantanamo Bay, Cuba, and support the continued expansion of the Army and the Marine Corps, and they share the view that the Bush administration undervalued international diplomacy.

Sen. Clinton said military action—a hallmark of the Bush administration—"will sometimes be necessary," but that the administration "will rely on it to protect our people and our interests when and where needed, as a last resort."

The New York senator called for the use of "smart power," saying the U.S. "cannot solve every problem," and "we certainly don't face the best of circumstances today, with our economy faltering and our budget deficits growing."

Associated Press

"I believe that American leadership has been wanting, but is still wanted," Sen. Hillary Clinton said in remarks at her confirmation hearing in the Senate Foreign Relations Committee.

She assured the committee that if confirmed, the State Department "will be firing on all cylinders"—applying pressure when needed and looking for opportunities to advance U.S. interests.

The senator credited Secretary of Defense Robert Gates with stimulating debate about the role of diplomacy and civilian institutions in the global war on terror, endorsing his call for providing the State Department with more resources.

While offering no specific new peace proposal, Sen. Clinton spoke confidently of Mr. Obama's intentions to renew U.S. leadership in the world and to strengthen U.S. diplomacy.

"As intractable as the Middle East's problems may seem, and many presidents, including my husband, have spent years trying to help work out a resolution, we cannot give up on peace," she said.

Pointing to recent bloodshed in Gaza, Sen. Clinton called for a peace pact "that brings real security to Israel; normal and positive relations with its neighbors; and independence, economic progress and security to the Palestinians in their own state."

She said the new administration would pursue a broader approach to the problem of Islamic extremism in Afghanistan and Pakistan.

Sen. Clinton called China "a critically important actor in a changing global landscape," but warned that "much of what we will do depends on the choices China makes about its future at home and abroad."

Sen. Clinton said she and Mr. Obama "seek a future of cooperative engagement with the Russian government on matters of strategic importance, while standing up strongly for American values and international norms."

On climate change, Sen. Clinton pointed to the coming United Nations Copenhagen Climate Conference as an opportunity to "lead abroad through participation."

"We can lead at home," Sen. Clinton said, "by pursuing an energy policy that reduces our carbon emissions while reducing our dependence on foreign oil and gas—which will benefit the fight against climate change and enhance our economy and security."

The selection of Sen. Clinton, which has prompted bipartisan praise in Congress, saw some notes of caution from a senior member of the Foreign Relations panel. Indiana Sen. Richard Lugar, the top Republican on the panel, called attention to Mr. Clinton's fund-raising activities as head of the Clinton Foundation. Recent disclosures show President Clinton raised money from several foreign governments.

—The Associated Press contributed to this article.

Geithner faces queries on taxes and housekeeper

By Jonathan Weisman

U.S. Sen. Charles E. Grassley, ranking Republican on the Senate Finance Committee, is raising questions about a housekeeper who worked briefly for Treasury Secretary-nominee Timothy Geithner without proper immigration papers, and multiple years when Mr. Geithner didn't pay Social Security and Medicare taxes for himself.

Committee Chairman Max Baucus (D., Mont.) summoned panel members to his office Tuesday afternoon to discuss the matter ahead of any public confirmation hearing.

According to people familiar with the matter, Mr. Geithner employed a housekeeper whose immigration papers expired during her tenure with Mr. Geithner, currently president of the Federal Reserve Bank of New York. The woman's papers were expired for three months, then she got a green card to work legally in the U.S., and federal immigration authorities didn't press charges against her, these people said.

The second issue involved taxes due while Mr. Geithner worked for the International Monetary Fund between 2001 and 2004. As an employee, Mr. Geithner was technically considered self-employed and was required to pay Social Security and Medicare taxes for himself as both an employer and an employee.

He apparently failed to do so, resulting in Internal Revenue Service audits his last two years at the IMF. As soon as the IRS brought the issue to his attention, he paid the taxes with interest, these people said.

Timothy Geithner

Mr. Geithner wasn't available to comment. Sen. Grassley declined to comment.

It is unclear whether these issues will be an impediment to the nomination of Mr. Geithner, whose ascension has been widely praised. Mr. Geithner spent most of his career managing government responses to financial crises, from the 1990s bailouts of Mexico, Indonesia and Korea to the current market meltdown that has brought Wall Street to its knees.

At the same time, similar issues have derailed nominations in the past. Former President Bill Clinton's first and second choices for attorney general both withdrew amid allegations that they failed to pay taxes for household help. President George W. Bush's first choice for Labor secretary withdrew after it emerged that she had employed an illegal immigrant.

Obama aides said they didn't think these issues would present a problem, given the minor nature of the infractions and the gravity of the role Mr. Geithner has been nominated to take.

On the tax front, Mr. Geithner's oversight is not uncommon. The IRS has mandated loose rules for U.S.-born IMF employees unaware of their obligations to pay payroll taxes.

Mr. Baucus nonetheless decided to hold a closed-door meeting to allow the two matters to be aired before Mr. Geithner's public confirmation hearing.

Obama team reconsiders tax credit for new hiring

By Greg Hitt
And Jonathan Weisman

U.S. President-elect Barack Obama's proposed tax credit for new hiring is likely to be scaled back—and could be jettisoned from his economic-stimulus plan altogether—in favor of new and bigger tax breaks for renewable-energy development and production, said individuals familiar with the situation.

During the campaign in October, Mr. Obama had proposed a tax credit of $3,000 for each new hire made by businesses, in response to mounting job losses. Transition aides were determined to keep that promise in his economic-recovery package, but the proposal has come under strong criticism on Capitol Hill, with many members of Mr. Obama's own party raising concerns about its effectiveness.

Economists of all political stripes have said businesses would likely claim the credit for hires they would have made anyway, or worse, lay off workers simply to rehire them and claim the tax break.

"That's one that gets a lot of opposition," said Sen. Charles Schumer, a New York Democrat.

Obama transition spokeswoman Stephanie Cutter declined to comment on what she described as continuing negotiations between Obama officials and lawmakers over the issue.

Haggling over the stimulus package, now estimated to cost $800 billion over two years, is heating up, as Obama aides and top Democratic lawmakers seek to hammer out final details later this week. The goal is for Congress to pass the plan by the Presidents Day recess in mid-February.

Associated Press

U.S. Sen. Charles Schumer, left, with New York Gov. David Paterson on Monday. Sen. Schumer said a proposed tax credit for hiring has drawn opposition.

Obama economists over the weekend released specific job projections by category, and suggested that the overall stimulus plan could save or create 3.7 million jobs.

ECONOMY & POLITICS

Silver lining in jobs data

Companies in U.S. might be improving their productivity

By Jon Hilsenrath
And Brian Blackstone

There may have been a silver lining for the U.S. economy in the horrific December job losses reported Friday by the Labor Department. Companies are cutting back so aggressively that they actually might be increasing their productivity even in the face of a wrenching economic shock.

The contraction in the number of hours worked might have been greater than the contraction in overall economic output for the quarter, which will be reported later this month. In other words, businesses appear to have squeezed more out of the workers they kept on staff, increasing business productivity—a measure of the nation's output per hour worked by the work force—even though the economy was going through its most severe contraction in decades.

In the long run, strong productivity growth should drive profits, and, potentially, real wages higher.

In the final three months of 2008, U.S. employers reduced the number of hours that workers logged at a 7.7% annual rate, through a combination of layoffs and cutbacks in overtime and manufacturing production shifts. It was the largest quarterly contraction in hours worked since 1975, according to Macroeconomic Advisers LLC, a St. Louis research firm.

More labor
Change from a year earlier in nonfarm business output per hour worked; quarterly data

Sources: U.S. Labor Department; Macroeconomic Advisers LLC (fourth quarter 2008 estimate)

The government's estimate of productivity growth comes out in early February. Most economists focus on productivity growth among nonfarm businesses—excluding agriculture, government and parts of housing. Macroeconomic Advisers estimates that output in the nonfarm business sector contracted at an 8.25% rate for the quarter, while hours worked contracted at an 8.6% annual rate.

"Nowadays, [companies] seem to anticipate a decline in output and lay off workers ahead of time," said Barry Bosworth, a productivity expert at the Brookings Institution, a Washington think tank.

Mass layoffs, fewer overtime hours and eliminated production shifts are fundamentally bad news because they mean workers are suffering. But it also means the economy is adjusting to the shock of the financial crisis—and the crisis can't end until an adjustment has taken place.

Of course, economic problems persist: Banks still sit on large losses from bad assets. The job losses tied to strong productivity means further strain on millions of households. And the good productivity news could be revised away by statisticians.

U.S. productivity trends have changed dramatically in the past decade. The U.S. experienced a productivity boom in the late 1990s, and it has proven surprisingly enduring. Productivity hasn't declined on a year-over-year basis since 1995. In the 1970s and 1980s, it experienced long contractions around recessions.

Chris Varvares, a Macroeconomic Advisers economist, says many companies entered this downturn with inventories relatively lean, meaning companies haven't been caught on their heels by the collapse in consumer demand. The expanded use of temporary workers also has made it easier for businesses to adjust their work force as the environment changes. Technology has made it easier to manage both inventories and employment levels.

A rise in productivity would be a potentially positive mark on the economic record of President George W. Bush, who has presided over two recessions, a dismal stock market and a housing bust. In the 30 full quarters that Bush has been president, through the third quarter of last year, nonfarm business productivity grew on average 2.6% at an annual rate. That is compared with 2% for Bill Clinton and 1.6% for Ronald Reagan.

Japan moves on budget plan

By Takashi Nakamichi

TOKYO—Japan's lower house of parliament passed a 4.786 trillion yen ($53.72 billion) extra budget to fund some of the government's promised economic stimulus measures, but the fate of the spending plan is far from certain after one representative quit the ruling party.

Prime Minister Taro Aso's cabinet compiled a stimulus package in October to try to jump-start an economy that is slowing in tandem with the global slump. Japan's real gross domestic product contracted an annualized 1.8% in the July-September quarter. The extra budget is designed to pay for the stimulus package.

The budget will now move to the upper house, which is controlled by opposition parties led by Democratic Party of Japan. All of them are likely to reject the plan, meaning that some of the government's stimulus steps may not be implemented as initially scheduled.

Mr. Aso's ability to push through his stimulus plan is limited by the opposition party control of the upper chamber and his own diminishing public support, which has also damaged his standing in the ruling Liberal Democratic Party.

Lower-house LDP representative and former bank minister Yoshimi Watanabe defected from the ruling LDP earlier in the day, partly to protest the lack of action by the Aso administration against the practice of guaranteeing private sector jobs for retired top bureaucrats. Local media reported that Mr. Watanabe abstained from the budget vote.

Mr. Watanabe, 56 years old, has served as a minister in charge of financial services and administrative reform. He has been among LDP politicians who have sought to carry on the policies of economic overhaul initiated by former Prime Minister Junichiro Koizumi. Mr. Watanabe has advocated policies that would deregulate Japan's financial-services industry further or limit the influence of bureaucrats in the government. For example, in early 2008, Mr. Watanabe led a group of policy makers who called for managing Japan's huge foreign-exchange reserve more actively so it would look more like a sovereign-wealth fund.

The Japanese public is unhappy about Mr. Aso's policies as the country's export-dependent economy slides deeper into recession amid the global economic slump, and a greater number of jobs are lost.

One of the main measures in the stimulus plan—cash handouts to households totaling around two trillion yen—has been criticized by the opposition and even some ruling party politicians as a waste of money that will do little to support the economy.

A public poll in the Yomiuri newspaper on Monday showed that 78% of those surveyed were opposed to the cash handout plan. The poll also showed an Aso cabinet support rate of only 20.4%, and a disapproval rate of 72.3%.

Under Japan's Constitution, the main budget legislation is enacted 30 days after the lower chamber approves it, regardless of what the upper house decides. But the same doesn't apply to other relevant bills needed to execute measures included in the planned budget, meaning it will be difficult for the ruling LDP and New Komeito coalition to swiftly pass the whole set of budget bills.

To be sure, there is a way to work around that legislative roadblock. If the upper house rejects those relevant bills or lets 60 days pass without voting on them, the coalition can put the legislation to a second vote in the more powerful lower house and enact it through their two-thirds majority.

However, even if any bills are put to a second lower-house vote, the ruling coalition won't receive the two-thirds vote it needs if 16 of their lower-house party members revolt due to discontent with Mr. Aso.

The bills that passed the lower house on Tuesday are for the second supplementary budget put together for the fiscal year ending in March. In October, the government approved a 1.81 trillion yen extra budget.

In addition to the controversial cash benefits, the second supplementary budget will allocate 755 billion yen toward revitalizing rural economies and 505 billion yen toward supporting small companies. Bills linked to the extra budget also include those that would raise the limit on injecting public funds into ailing banks to 12 trillion yen from two trillion yen, and enable a government body to buy up to 20 trillion yen in bank-held stocks.

—Yuka Hayashi contributed to this article.

Risks seen in slowdown in China, bank bailouts

By Tomas Bielskis

A drop in China's growth below 6% this year would be a major risk to the global economy, the World Economic Forum said in its annual Global Risk report.

The forum also warned that government bailouts of banks were "dangerous ... without remedying the root causes of the problem," and strongly increased the risk of fiscal crisis in developed economies that are running high deficits.

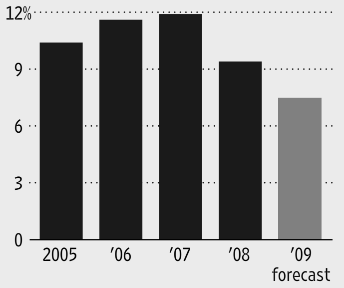
The annual report, released Tuesday, said China's size and role as the main creditor to the U.S. meant a slowdown in its growth rate would inflict significant damage on the world's economy, as well affecting the strength of the dollar and commodity prices.

The World Bank said China's gross domestic product last year grew 9.4% and projects that the decline in export demand will to drive growth down to 7.5% this year, "increasing the risk of a hard landing that would stress the financial system and could generate social tensions in China and beyond."

Unprecedented government spending in support of troubled financial institutions is also threatening to worsen the stretched fiscal positions of many countries, the report added, pointing to the U.S., U.K., France, Italy, Spain and Australia as vulnerable. Developed economies such as these already face fiscal strains from rising health-care and pension costs for aging populations, the report said.

Elsewhere, even though equity markets have already lost 50% of their value, further asset-price declines are expected this year as a vicious cycle of falling asset prices, write-downs and deleveraging by companies "appears to be unbroken," the report said.

Losing steam
China's gross domestic product, annual percentage change



Note: Inflation-adjusted GDP in Chinese yuan
Source: World Bank

"The global economy is still not in the clear," said Daniel Hoffman, chief economist at Zurich Financial Services AG, in a release accompanying the report, adding that "one of the biggest risks is that short-term crisis fighting may induce businesses and governments to lose the long-term perspective on risk."

One example is concern over developing water shortages, though they haven't featured prominently in the global financial crisis that is absorbing the attention of governments right now. Water is critical to generating energy, the report said, noting that 50% of water costs are energy related.

The report contained a nugget of optimism, describing this year as an "opportune moment to strengthen global governance and build the political will to restore global financial stability."

The report's release precedes the World Economic Forum's meeting of financial and political leaders in Davos, Switzerland, from Jan. 28 to Feb. 1.

Financial crisis, oil's plunge cause record Russia outflow

By Lidia Kelly

MOSCOW —Russia saw a record $130 billion in net capital outflows last year, data from the central bank showed Tuesday, reversing the inflows of 2007 and revealing some of the strain the global financial crisis has placed on Russia.

The outflows contrast with the $83.1 billion of capital that flowed into a booming Russia in 2007. The fourth quarter alone saw an outflow of $130.5 billion, which followed an outflow of $17.4 billion in the third quarter.

Capital flight from Russia started late in the summer and was initially spurred by Russia's military conflict with Georgia. Then late last year, Russia's authorities began admitting the severity of the financial fallout and its spread to the real sectors of the economy that had boasted a growth rate of 7% or higher in gross domestic product terms in recent years.

Most economists, who have followed the Kremlin's efforts to support the ruble even as the price of oil, Russia's chief export, has tumbled, had expected heavy outflows. The central bank has been dipping into the country's gold and foreign exchange reserves, which fell by more than $150 billion from a peak of nearly $600 billion in the last four months of 2008. In December alone, the central bank spent $70 billion trying to prop up the ruble and avoid the panic among the population that a currency collapse, akin to 1998, would cause.

The data from the central bank includes transfers of ruble assets into foreign currencies by both corporations and individuals. The central bank has been weakening the ruble gradually, with nearly two mini-devaluations a week that have led to the ruble shedding 18% of its value in the past two months.

Traders have estimated that despite allowing the ruble to weaken slightly twice this week, the central bank has spent more than $12 billion in the past three days defending it. Tuesday, the ruble closed unchanged from Monday at the upper limit of its trading band against a basket of dollars and euros.

"We're approaching a point where there must be a fundamental reconfiguration of macroeconomic policy," said Neil Shearing, an emerging Europe economist at Capital Economics in London. "Up till now we have been left with a situation where interest rates are very low and the ruble is overvalued."