News In Depth: Iraq's reluctant leader emerges as an unlikely force

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Breaking news at europe.WSJ.com

Behind the podium, on a shaky platform

Agence France-Presse/Getty Images

WANT TO HIDE? Expectations of a Conservative victory in the next election and an uncertain economy have vexed U.K. Prime Minister Gordon Brown, seen at a Wednesday news conference. **Pages 2, 32.**

Intel appeals EU fine, cites human rights

By Charles Forelle

BRUSSELS—**Intel** Corp. appealed a billion-euro antitrust fine Wednesday. That was expected. But among the chip giant's arguments is an unlikely complaint: Its human rights were violated.

Intel isn't alone. A growing list of companies are raising the charge that the EU's vigorous antitrust watchdog is running afoul of protections afforded by European human-rights law.

The maneuver is something of a Hail Mary pass—no EU antitrust appeal has won on the argument. But it reflects the frustration of companies faced with ever-mounting fines from the EU's antitrust watchdog.

Intel's precise legal arguments aren't known; under EU procedure, court case files are closed to public inspection. A company spokesman confirmed the company is raising human-rights issues, though he didn't provide details. It will be more than a year before the Court of First Instance in Luxembourg rules.

Also among those trying the human-rights move are **Saint-Gobain Glass France** SA, a big glass maker that swallowed an €899 million ($1.3 billion) fine last year, and **Schindler Holding** Ltd., fined €147 million for coordinating bids for elevators. Rulings are pending in the cases.

The argument raises a fundamental question: As the EU regulator ratchets up fines, does it cross the line from an administrative organ to a criminal court?

EU courts have long said no, but some think it now has. "There is no doubt that antitrust proceedings are criminal in nature," says Arianna Andreangeli of the University of Liverpool, who cites the size of the fines and their "deterrent and punitive" character.

The issue calls into question the EU's practice of having a politically appointed bureaucrat—the current antitrust commissioner is Neelie Kroes of the Netherlands—in the role of prosecutor, judge and jury.

Mrs. Kroes supervises investigations, and then decides whether the target is guilty and what the punishment should be. Her decisions are formally approved by all the 27 EU commissioners, but in practice they are rarely questioned.

That kind of administrative procedure was appropriate four decades ago, when the EU began handing out relatively small fines, defense lawyers say, but outmoded in an era in which Mrs. Kroes has made nine-figure penalties

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Morgan Stanley loss comes with pay rises

By Joe Bel Bruno And Jessica Papini

NEW YORK—**Morgan Stanley**'s strategy of dialing down risk to pull itself out of the financial crisis is coming at a steep price.

The investment bank, which narrowly averted a collapse at the height of Wall Street's meltdown, reported a third straight weak quarter. Losses in all three of its major business lines in the second qurrter came in sharp contrast to the rebounds playing out for rivals such as **Goldman Sachs Group** Inc. and **J.P. Morgan Chase** & Co.

Morgan Stanley's expenses rose faster than some analysts expected, as the firm paid up for employees it feels it can't afford to lose. Overall compensation and benefits rose 25% from last year's first quarter, to $3.9 billion, or 72% of Morgan's quarterly net revenue of $5.4 billion.

So far this year, Morgan Stanley has paid or set aside pay of $5.9 billion, about 70% of revenue. That compares with the $11 billion set aside or paid at Goldman Sachs, which last quarter bounced back to record profit and revenue thanks to strong trading results. Because Goldman's revenues have been stronger, it hasn't set aside as big a portion of revenue for compensation and benefits.

In the broad realignment of the financial industry, Morgan Stanley risks falling be-

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	CLOSE	PCT CHG
DJIA	8881.26	-0.39
Nasdaq	1926.38	+0.53
DJ Stoxx 600	215.65	+0.29
FTSE 100	4493.73	+0.28
DAX	5121.56	+0.54
CAC 40	3305.07	+0.07
Euro	$1.4207	-0.15
Nymex crude	$65.40	+1.05

LEADING THE NEWS

U.K. investors delay action until elections

Decisions are put off as businesses await Conservative victory

BY ALISTAIR MACDONALD AND NEIL SHAH

LONDON—The U.K. faces a vexing problem as it battles the recession: Many investors, companies and individuals are convinced the opposition Conservatives will win the next election—and they are delaying crucial decisions until a new government takes over, expected by June.

The Tories are as much as 17 percentage points ahead of Labour in some opinion polls, and many investors are already looking beyond Prime Minister Gordon Brown's Labour government. Nearly everyone in the U.K.—except Mr. Brown and the Labour Party—expects a Conservative Party victory. In a preview of the 2010 vote, the Conservatives are expected to win Thursday's special election for a parliamentary seat vacated by a Labour lawmaker who resigned over accusations that he had abused the parliamentary expense system.

Stimulus on the table

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The notion that big institutions are waiting around for an inevitable Conservative government is causing uncertainty—and in some cases gridlock—in boardrooms, markets such as currency exchange, and other areas where key players are wary of making a big move while Labour is still in power.

Adding to the uncertainty, mystery remains about what exactly the Conservatives and their leader, David Cameron, would do with a win in the elections, which must be held by June. The Tories have kept mum about details of their plans for areas such as budget cuts and taxation because they don't want to give their opponents too much time to attack.

When the Conservatives do make a detailed policy pronouncement, it has an impact. Earlier this week, the party said it would kill the Financial Services Authority and shift many of its responsibilities to the Bank of England. In the eyes of many, that statement rendered the FSA a lame duck—just as it is supposed to be engaging in the global debate over regulatory reform.

As Parliament went home for the summer this week, hopes diminished that the government will be able to tackle any big issues over the next year. The coming year will be mostly about politics, analysts say.

"The general election is making it almost impossible for people in politics to be frank about the need to respond to the fiscal crisis," says Patrick Dunleavy, a professor of political science and public policy at the London School of Economics. "And that's making it hard for other people to make decisions."

Mr. Brown on Wednesday brushed aside suggestions that his party would lose. "People have to know that what we are doing [to help the economy] has results, and it takes time for these results to come through," he said. "Then people will see very clearly the choice between the parties."

Pundits have called British elections before, only to be proved wrong. "Businesses I speak to, though well aware of the opinion polls, are certainly not assuming a Conservative victory," argues Stephen Timms, a government Treasury minister. "The Tories have strikingly failed to articulate a vision for Britain, or a coherent set of policies," he says.

Bloomberg

The Conservative Party's leader, David Cameron, is widely assumed to be the prime minister in waiting. What his party will or can do with a victory is less clear.

But bond and currency traders are watching Tory announcements closely when weighing investment decisions.

"We're assuming that [the Tories] are going to be the next government, so you have to listen to what they're saying," says Russell Silberston, head of global interest rates at Investec Asset Management in London.

People like Mr. Silberston are foraging for clues to what Conservative pronouncements mean. Last week, his team heard reports that the Conservatives were studying both Tory budgets from the early 1980s and the large cuts in Canadian public spending in the mid-1990s. They began to look at those periods to see by how much deficits were reduced, and how that was achieved.

Some markets fear a "hung Parliament," in which the Conservatives win, but lack enough political support to push through a bold agenda. If doubts increase about the next government's ability to tackle the ballooning budget deficit, the British pound and prices of U.K. government bonds could be in for a nasty spill.

"What really matters from here is whether the next government is strong or weak," says Steven Pearson, a currency analyst at Bank of America Merrill Lynch in London. In a sign of worry over Britain's finances, the gap between the yield on U.K. government bonds and relatively safe German debt has been widening lately. On Wednesday, the spread stood at 0.48 percentage point, close to its high for the year of 0.51 percentage point on Feb. 27.

Fears of legislative deadlock come at a dangerous time for the U.K.'s finances. In May, Standard & Poor's Ratings Services warned Britain it could lose its triple-A credit rating if it didn't soon make efforts to address its fiscal problems. S&P said it will revisit the rating issue after the general elections, effectively tying sterling's fate to the vote in the minds of many investors.

For many businesses, especially small firms, the lack of clarity makes planning harder. "We are in limbo," says Tracy Hoather, managing director of Sameday PLC, a courier service based in Cheshire, in northwest England. Ms. Hoather mentions both Labour's and the Conservatives' lack of clarity on environmental policies such as charges on waste and use of the roads, areas that would hit her business.

The pound's volatility is making it more costly and harder to plan for customers of South African wine producer Jordan Wine Estate. Chief Executive Gary Jordan recently set up a London restaurant, but says he is holding back on further investment in Britain because he doesn't know where he stands on issues such as tax incentives. "If the world wants to recover you can't have political parties holding their cards to their chest," he says.

The Conservatives did spell out their plans this week in one crucial policy area, financial regulation. The party said it would give the FSA's banking oversight to the Bank of England and merge its consumer-protection duties with another body.

That will "create a planning blight on new regulatory initiatives and a career blight for those employed at the FSA, with the uncertainty increasing the rate of attrition," says Chris Rexworthy, an expert in regulation at London-based IMS Consulting and a former FSA regulator.

The move has caused anger at the FSA, where some believe their ability to make Britain's voice heard at international forums discussing the future shape of regulation has been hurt by their status as a potentially dead institution.

Some individual investors are frozen too. "Where there is any uncertainty, people are usually happier to delay than take some action, particularly when it concerns investing or spending money," says Jason Witcombe, who advises individuals on issues such as investments, pensions and tax. His London-based firm, Evolve Financial Planning, has seen an increase in customers who are putting planning on hold amid uncertainty about what a future government might do.

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INDEX TO PEOPLE

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

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LEADING THE NEWS

Glaxo's profit rises 12%

Drug maker expects to supply flu vaccine by first part of 2010

By Jeanne Whalen And Jason Douglas

GlaxoSmithKline PLC hopes to supply swine-flu vaccine to all of the governments it is in discussions with by the first part of 2010, but that will depend on some quirks in the production process, the company's chief executive said Wednesday.

So far, 16 governments have ordered 195 million doses from Glaxo, but the company is talking to 50 governments at the moment and expects total orders to be "substantially" higher, Chief Executive Andrew Witty said. Mr. Witty's remarks came as the company reported a 12% rise in second-quarter profit.

Andrew Witty

How quickly Glaxo can deliver will depend on how much active ingredient, or antigen, it can produce, Mr. Witty said. But the H1N1 virus being used for swine-flu vaccine is so far yielding a low level of antigen, he said, echoing comments made by other vaccine makers and the World Health Organization in recent days.

If production levels remain roughly where they are now, "we believe we could meet the kind of demands we're being told [governments] want" by "the first part of 2010," he said.

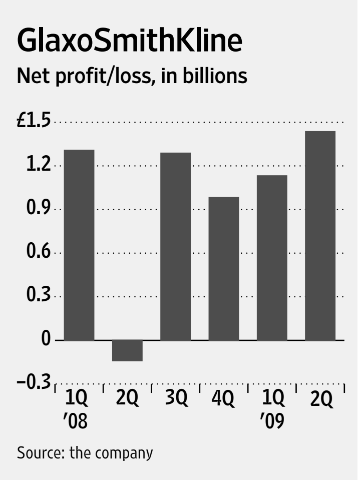
Glaxo's second-quarter profit rose to £1.44 billion ($2.37 billion) from £1.29 billion a year earlier, helped by the British pound's weakness against other currencies. Sales rose 15% to £6.75 billion.

The company's most important business—prescription drug sales in the U.S.—fell 15% in the quarter when measured at constant exchange rates, hit by generic competition for several Glaxo drugs. Sales in Europe and in emerging markets grew 1% and 14%, respectively. Most drug companies are pinning their growth hopes on emerging markets as sales in the U.S. market are threatened by cheaper generics, frugal insurers and a lack of new products.

In addition to the vaccine, Glaxo is increasing production of an antiviral medication, Relenza, that is being prescribed by some doctors to relieve the symptoms of swine flu.

Mr. Witty said he expects the pandemic to make a "significant contribution" to Glaxo's profit, which he said is justified given the company's investment over the years in developing Relenza and flu vaccines.

Glaxo is charging wealthy nations €7 (about $10) a shot for the H1N1 vaccine and developing countries less, he said. It is also donating



50 million doses to the WHO.

Governments buying H1N1 vaccine from Glaxo are agreeing to indemnify the company against some legal liabilities that may arise from a mass vaccination program, Mr. Witty said. "I think the governments completely understand that what you're asking the companies to do is manufacture vaccine for use against a virus which we haven't seen before...which may get used on a scale not seen before," he said. "And it's unreasonable to expect private institutions to take whatever risk" that might bring, he said.

He added that he expects regulators including the U.S. Food and Drug Administration and the European Medicines Agency to sign off on the vaccine before it is used in any consumers.

Iberdrola sees demand for electricity picking up

By Bernd Radowitz

MADRID—Spanish electricity company **Iberdrola** SA on Wednesday posted a 5.5% decline in second-quarter net profit but said a pick-up in electricity demand could boost results later this year.

Net profit fell to €713.5 million ($1.01 billion) from €755 million a year earlier as revenue dropped 4.4% to €5.47 billion from €5.72 billion. The consolidation of U.S. energy company Energy East and a €112 million gain from the sale of a 10% stake in wind-turbine maker Gamesa Corporación Tecnológica SA in June couldn't compensate for lower electricity prices in Spain and lower output volumes in Spain, Latin America and Britain.

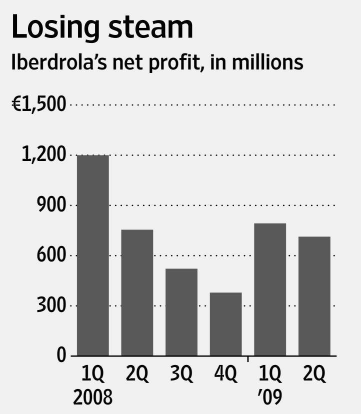
Electricity demand in its core markets of Spain and the U.K. fell 7.1% and 5.6% respectively in the first half. The company didn't provide demand figures for the second quarter.

However, Chairman Ignacio Galán said the decline in Spanish energy demand has tapered off over the past six weeks. This is likely to translate into higher electricity prices toward the end of the year, Mr. Galán said. Output from wind power, which usually slows down during the Spanish summer, is also expected to increase by year-end.

"We expect [2009] results without extraordinary gains in line with last year, maybe slightly better," Mr. Galán said. Yet he cautioned that the results will also depend on how the company's divestment program proceeds and the strength of sterling and the Brazilian real compared to the euro. The pound's decline against the euro had dragged on first-half results of Iberdrola's U.K. unit Scottish Power PLC.

Iberdrola has sold €1.3 billion in nonstrategic assets so far this year, but plans to divest an additional €1.2 billion in assets by the end of the year. These divestments, together with a recent €1.33 billion capital increase, helped Iberdrola reduce its net debt to €29.32 billion at the end of the second quarter from €31.18 billion at the end of the first quarter.

Asked whether the company's 9.5% stake in Portuguese energy firm Energias de Portugal SA could be the next asset to be sold, Mr. Galán said the stake "is currently in our fridge." The chairman didn't elaborate further, but an Iberdrola spokeswoman said the chairman's comment didn't mean the company is preparing for a sale of the stake. No decision on a possible stake sale has been taken yet, she added.



Sources: the company; Bloomberg News (photo)

◀ José Ignacio Sánchez Galán, chief executive officer of Iberdrola

Pfizer's earnings decline 19%

By Peter Loftus

Pfizer Inc.'s second-quarter profit dropped 19%, hurt by a strong dollar and lower sales of its blockbuster cholesterol drug Lipitor.

Smaller rival **Eli Lilly** & Co., meanwhile, posted a 21% rise in its quarterly profit, thanks in part to higher sales of antidepressant Cymbalta and cancer drug Alimta.

Both drug makers boosted their 2009 earnings forecast. Several major drug makers may see improved second-half results as the effects of unfavorable currency rates dissipate, though challenges such as generic competition will continue.

New York-based Pfizer saw sales of some its top drugs decline because of generic competition and unfavorable currency rates. Generic competition and drug-research setbacks were among the factors that drove Pfizer to agree earlier this year to acquire Wyeth. The deal is expected to close by year end.

Pfizer, the world's largest drug maker by sales, Wednesday reported earnings of $2.26 billion, or 34 cents a share, down from $2.78 billion, or 41 cents a share, a year earlier. Excluding acquisition and restructuring-related charges, earnings came to 48 cents from 55 cents.

"Our initial impression is that the company exhibited good cost control," said Miller Tabak analyst Les Funtleyder.

Revenue fell 9.4% to $10.98 billion, hurt by unfavorable foreign-exchange rates.

Sales for Lipitor, the top-selling prescription drug in the world, declined 9.8% to $2.69 billion, with U.S. sales falling 6%.

Pfizer raised its adjusted 2009 earnings forecast a nickel to between $1.90 and $2 a share.

Indianapolis-based Lilly reported quarterly earnings of $1.16 billion, or $1.06 a share, up from $958.8 million, or 88 cents a share, a year earlier. Excluding items, including a six-cent charge related to litigation involving the antipsychotic Zyprexa in the latest quarter, earnings rose to $1.12 a share from 94 cents.

Lilly's total revenue rose 2.8% to $5.29 billion.

Lilly raised its projected 2009 earnings range to between $4.20 and $4.30 a share from $4 to $4.25.

Genzyme cuts earnings, revenue view

By Thomas Gryta

Genzyme Corp.'s second-quarter profit more than doubled on solid sales growth, as the anticipated revision to its 2009 earnings forecast that reflects a temporary plant shutdown came in below already reduced Wall Street estimates.

The biotechnology company said the plant shutdown had minimal impact on the latest quarter's results but will pressure results for the rest of the year. It said the facility should resume production of its top-selling drugs—Gaucher disease treatment Cerezyme and Fabry disease treatment Fabrazyme—later this month, with shipments expected by year end.

Genzyme shut down production at its Allston, Mass., plant in June after discovering a virus in one of six bioreactor vats used to develop drugs at the plant, which is the only facility that makes Cerezyme and Fabrazyme, enzyme replacements for rare genetic disorders.

The company is now targeting 2009 earnings, excluding items, of $2.35 to $2.90 a share on revenue of $4.6 billion to $5 billion. Analysts expected 2009 earnings of $3.31 a share on revenue of $4.96 billion, according to Thomson Reuters. Previously, the company projected earnings of $3.52 and revenue of $5.15 billion to $5.35 billion.

Due to product shortages, Genzyme cut its revenue projections for Cerezyme to $750 million to $1 billion for the year, down from $1.25 billion to $1.28 billion. Genzyme now expects Fabrazyme revenue between $510 million and $520 million for 2009.

For the second quarter, the company posted earnings of $192.2 million, or 70 cents a share, from $69.6 million, or 25 cents, a year earlier. Excluding acquisition and other costs, profit rose to 85 cents from 38 cents.

Revenue rose 4.9% to $1.23 billion, or 11% excluding foreign-currency impacts. The company noted that the shutdown of the Allston facility cut revenue by $13 million during the latest quarter.

In afternoon trading Wednesday, shares of Genzyme were down $4.53, or 8%, to $51.38 on the Nasdaq Stock Market.

P&G drug-unit sale close; price tag may hit $3 billion

By Jeffrey McCracken And Ellen Byron

Procter & Gamble Co. is getting closer to a possible sale of its prescription-drug business, and several parties, including specialty drug maker **Warner Chilcott** Ltd., and private-equity firm **Cerberus Capital Management LP**, are engaged in later-stage discussions, according to people familiar with the matter.

The unit could fetch about $3 billion, these people say.

An acquisition of the P&G business would substantially boost the profile of Warner Chilcott, a New Jersey-based company that focuses on women's health care and dermatology products. Folding in the division would triple Warner's revenue and give it access to drugs that focus on a wide range of women's health concerns.

Warner Chilcott didn't return calls seeking comment.

Cerberus, which proposes acquiring the division and turning it into a stand-alone company, is more circumspect about the transaction, according to people familiar with the situation. But it has lined up preliminary financing from some Wall Street banks, a small sign that banks are getting comfortable financing acquisitions, albeit ones with low amounts of debt financing and very steady cash flows.

"Cerberus can't get it if the strategic buyers are serious. They will pay more than Cerberus for it," said one person familiar with the situation.

The unit—which earns roughly $800 million in operating profit—was put on the auction block late last year, in a sales process led by **Goldman Sachs** & Co. A deal could be wrapped up by the end of summer, according to the people familiar with the discussions, though they warned final discussions could still falter.

CORPORATE NEWS

Pricing dispute boosts China's iron costs

Miners try to isolate Beijing as it demands discounts on ore amid soaring demand; Rio detentions are a factor

By Shai Oster

BEIJING—China's decision to hold out for lower iron-ore prices in negotiations with the world's biggest mining companies is forcing its steel mills to pay far more than competitors around the globe.

China's own rising demand, plus tremors from Beijing's detention of four employees of Anglo-Australian mining company **Rio Tinto** PLC, have helped to send spot prices for iron ore soaring past $90 a metric ton. That is the highest level since late last year, according to Chinese steel consultancy Mysteel, and about 20% higher than the long-term contracts agreed to by Japanese, South Korean and European buyers earlier this year.

Late Monday, Brazilian miner **Vale** SA said it agreed to supply iron ore to **ThyssenKrupp** AG on similar contract prices—about a third less than last year's prices, on average—deepening China's isolation in this year's round of negotiations. Vale had already concluded negotiations with other steelmakers at the same global benchmark that China is so far refusing to follow.

The China Iron & Steel Association, which is leading the Chinese side of negotiations with miners, says its contract negotiations are continuing. But prospects for this year's talks, which failed to conclude by a June 30 deadline, have been clouded since then by China's accusation that Rio Tinto employees used bribes to procure "state secrets" related to iron-ore price negotiations. Rio was the lead negotiator for the mining companies.

Workers sweep iron-ore powder at the port in Rizhao, China.

Analysts say the detentions—along with speculation by iron traders that Rio has stopped shipments to China—have helped to drive up prices. Rio denies the allegations about its employees, and says it continues to import ore into China.

China imported 297 million tons of iron ore in the year's first half, nearly 30% more than in the year-earlier period. Without long-term contracts, Chinese steel mills have to buy more ore on the spot market, without discounts—which in turn drives up the spot price even more.

"Whether key industry secrets have been leaked or not also matters little, as it is an open secret that China's insatiable demand for growth will continue to fuel ever-growing demand for iron ore," said Ren Xianfang, an analyst with IHS Global Insight, a commodities consultancy. Ms. Ren added, "This fact alone will undermine China's bargaining power in any resource-related negotiations."

Beijing has said little about the Rio case since detaining Stern Hu, an Australian citizen, and three Chinese colleagues at Rio. People knowledgeable about the annual talks say that much of the information most useful to mining companies would be data on steel prices, inventories and corporate profits. Those are all either publicly disclosed or available through legal means.

The case could involve corporate data that had yet to be publicly disclosed, or Rio executives may have had assembled a breadth of data that alarmed officials. "There's plenty of data that iron-ore companies would love to have. It's the sort of thing you get drinking with people late at night, establishing good working relationships," said Alan Heap, an iron analyst at Citigroup Inc. But, he said, "It's different in China where those things can be state secrets."

Mr. Hu was in charge of Rio's China iron-ore department, and oversaw the company's ore sales to Chinese steelmakers. The key issue for Rio and other miners would have been gauging future Chinese demand.

Analysts say the miners could have had a pretty good indication that demand would rise as a result of China's $585 billion economic-stimulus package, which includes about $220 billion in spending on highways, bridges and other infrastructure.

Iron-ore sellers also may have been seeking deeper information about factors such as production costs and inventory. That is routinely sought out during negotiations in developed countries, say analysts and people who have been involved in similar negotiations.

"You can find such data on any Chinese steel Web site," said IHS's Ms. Ren. The problem could come, she said, with trying to obtain "more specific information, particularly with respect to individual companies," that might not be public.

Spending cuts by clients delays an ad-industry recovery

By Suzanne Vranica

Big marketers, including **American Express**, **General Motors** and **Royal Dutch Shell**, have cut back on the fees they pay ad firms, a shift that could dash recent predictions that an advertising recovery is in the offing.

ADVERTISING

Second-quarter results due out Thursday from ad giants **Omnicom Group** and **Publicis Groupe** are likely to underscore the trend. "We think investors should brace for a steep decline in organic revenue," says Deutsche Bank analyst Matt Chesler.

Some analysts suggest organic revenue, which excludes the impact of foreign-currency conversions and recent acquisitions, will be off almost 8% at Omnicom and 6.3% at Publicis. Those would be far steeper declines in the closely watched industry benchmark than the two companies reported for the first quarter.

Interpublic Group, which is set to report results next Tuesday, is likely to come in below its peers because of a falloff in its events business and cuts made by its largest client, GM, according to a person familiar with the matter.

While ad companies have historically lagged behind in economic recoveries, this time their rebound may come even later, and be less convincing. Not only have marketers slashed what they spend on ad time and space, but many companies have also significantly reduced what they pay their agencies for ad services, such as creating TV commercials.

"The reality is that clients want more for less," says Maurice Levy, chief executive of Paris-based Publicis. "It's something that is unfortunately becoming quite common."

Ad executives say marketers have slashed the fees they pay by 5% to 30%. Some companies have even asked that fees be reduced retroactive to Jan. 1, meaning firms are paid less for work they have already completed, according to two ad executives.

Earlier this year, **Anheuser-Busch InBev** reduced what it pays some of its ad firms by shifting away from retainer relationships. American-Express has cut the fees it pays to its agencies by as much as 20%, say two people familiar with the matter.

"Our companywide re-engineering plan did include reducing staffing levels, cutting operating costs and scaling back investment spending, including marketing," says an American Express spokeswoman.

Kraft Foods is currently negotiating with some of its agencies to reduce its fees by as much as 10%, says a person familiar with the matter. Kraft didn't respond to requests for comment.

Over the past few years, companies have begun to get their procurement departments involved in efforts to cut the costs on a wide range of marketing activities, including ad production. The recession has fueled the trend, ad executives say.

"There is no one in the industry whose clients haven't said, 'We are under pressure, so you have to cut fees,' " says David Sable, vice chairman and chief operating officer of Wunderman, a big direct-marketing firm owned by Dublin-based **WPP**.

The cuts will likely hold up a recovery for the ad industry, say ad executives and analysts. "We should be seeing the effect of the renegotiation of fee arrangements for the next 12 months," says Deutsche Bank's Mr. Chesler.

Mr. Levy of Publicis says the large ad-holding companies won't see much in the way of increased organic revenue before the second half of 2010, when results will get a boost from favorable comparisons with this year's slump. Real growth, he adds, will come in 2011.

One producer of TV spots is using its creative firepower to express its displeasure. Scofield Editorial, a small shop in Indianapolis, crafted a video, called "Vendor Client Relationship—in Real World Situations," composed of comic vignettes in which ordinary people ask for price breaks on products such as a filet mignon dinner, a hairdo and even a movie.

In one scene, a woman seated in a hair salon tells the stylist, "I'd like the highlights, but I can only pay for a trim." The video, which has received almost one million views since being posted on YouTube in May, has been making the rounds on Madison Avenue, and some agency chiefs have sent it to their clients. "We hit a nerve," says Brian Boak, an editor at Scofield Editorial.

Diners try to haggle over a restaurant bill in a video by TV-commercial producer Scofield Editorial that spoofs marketer's efforts to negotiate fee cuts for ad services.

Scofield Editorial

The global ad firms have tried to offset declines in compensation by cutting staff. The ad industry frequently reacts to downturns by paring jobs because salaries typically represent about 55% to 65% of an agency's expenses. The industry has shed tens of thousands of jobs so far during this recession.

WPP's head count fell by almost 4,300, or 3.7% of its current work force, during the first four months of the year. New York-based Omnicom laid off about 3,000 people at the end of last year. Interpublic, also based in New York, cut a total of 2,800 jobs in the fourth and first quarters. The pink slips are expected to keep coming.

Wall Street will be paying close attention during the big ad companies' conference calls on earnings for any signs that the slide in ad spending has hit bottom. Lately some media executives have expressed optimism. Others aren't convinced the spending cuts are over.

Publicis expects the market to hit its lowest point in August, while WPP Chief Executive Martin Sorrell has been less optimistic. Several weeks ago, Mr. Sorrell said marketers are showing some confidence, but that it hasn't yet translated to spending. Indeed, toy makers **Hasbro** and **Mattel** said this week that they both had scaled back on advertising during the second quarter.

FOCUS ON AUTOMOBILES

Fiat posts loss despite incentives

Government program spurs sales, but firm still can't turn profit

BY STACY MEICHTRY AND GILLES CASTONGUAY

Government incentives to scrap old cars helped buoy **Fiat** SpA's sales in Europe in the second quarter but couldn't stop the Italian auto maker from incurring a loss for the second consecutive period.

Fiat posted a net loss of €179 million ($254 million) for the three months ended June 30, compared with a net profit of €646 million in the same period a year earlier.

The loss came despite incentives by governments in Europe and elsewhere that allow consumers to trade in old cars for credits on certain new ones.

A Fiat 500 sits in the showroom at a dealership in Epping, U.K.

Bloomberg

Although the measures helped stabilize sales in some European countries, they also have raised concerns about how the auto industry will be affected if governments try to unwind the assistance as early as next year.

In June, Fiat finalized an alliance that will give it a 35% stake in **Chrysler Group** LLC if targets, such as technology upgrades for the U.S. car maker, are met. Fiat also will have the right to take a majority interest in Chrysler once U.S. government loans have been repaid.

Fiat Chief Executive Sergio Marchionne said it was too soon to predict when Chrysler would return to profitability, and what its profit margins would be when it does.

He said new management installed by Fiat and the impact of Fiat's technology will start showing results at the end of next year.

Fiat, which produces vehicles ranging from trucks to tractors, saw overall revenue decline 23% to €13.2 billion during the second quarter from the previous year. However, its car unit, Fiat Group Automobiles, saw some signs of improvement as government incentives began to kick in.

Fiat's passenger-car deliveries rose 7.2% from the same period the previous year in Italy, its biggest market, which introduced a scrapping program in February. Deliveries doubled in Germany, where Fiat's small, fuel-efficient cars took market share from higher-priced German makes that use more fuel.

Sales continued to slide, however, in markets such as the U.K. and Spain, where government help came too late to affect second-quarter results.

Fiat's lackluster finances have at times hindered its growth. Mr. Marchionne's refusal to include cash in its bid for **General Motors** Co.'s Opel appears to have put the German auto maker out of reach.

Mr. Marchionne has offered to spin off Fiat's passenger car unit and merge it with Opel, an offer that remains on the table. On Wednesday, however, Mr. Marchionne said his company would forge ahead with the "inevitable" spin-off, with or without Opel.

GM says global car market is starting to bounce back

BY SHARON TERLEP

General Motors Co. on Wednesday said that global auto sales are starting to rebound and that it is outperforming rivals in emerging markets such as China.

The U.S. auto maker's second-quarter global sales fell 15% from a year earlier but rose 20% from the first quarter. Industrywide, global sales were down 13% year-over-year but up 12% from the first quarter, GM said.

"This global great recession is approaching an end," GM sales analyst Mike DiGiovanni said on a conference call.

Mr. DiGiovanni said that while some of the global increases are driven by government stimulus programs, both rising populations and wealth in emerging markets promise to deliver long-term growth.

The auto maker faces a balancing act with global investments after a federal bailout and bankruptcy that has left the U.S. government as its majority owner.

China, growing at an "alarmingly, surprisingly excessive rate," will drive a global recovery, Mr. DiGiovanni said.

Underscoring China's dramatic growth, the country last quarter outsold the U.S. by 29%. A year earlier, the U.S. outsold China by 57%.

Reuters

As a result of growth in China and declines in the U.S., 72% of GM's sales were outside its home market in the second quarter. Above, vehicles at a GM factory in Shanghai.

As a result of growth in China and steep declines in the U.S., 72% of GM's sales were outside its home market in the second quarter, compared with 65% a year ago.

Mr. DiGiovanni forecast that over the long term, non-U.S. sales will comprise 60% to 65% of GM's global business.

GM, however, tempered optimism by warning that temporary stimulus programs drove much of the second-quarter growth and may take away from future sales. Stimulus programs in China, Brazil and Germany are expected to generate about 2.5 million sales, Mr. DiGiovanni said.

GM said economic troubles, especially in mature markets such as the U.S., Japan and Western Europe, dragged down sales. Steep production cuts in the U.S., where GM recently emerged from bankruptcy, added to the decline.

GM sales in North America fell 32% in the second quarter. For the year's first half, GM sales were down 22% from a year ago to 3.55 million vehicles.

The strength of U.S. sales for all of 2009 will depend in part on the success of the "cash for clunkers" program set to launch this month. The federal program gives consumers up to $4,500 to trade in aged gas-guzzlers for new, more fuel-efficient vehicles.

—Kerry Grace Benn contributed to this article.

EU aims to increase competition in car-repair, used-vehicle markets

BY PEPPI KIVINIEMI

BRUSSELS—Europe's car-repair and secondhand markets need extra rules to increase competition, the European Commission said Wednesday.

Competition in the secondhand-car and repair markets, which make up 40% of consumer car spending, isn't as good as it could be, said the commission. The European Union's executive branch is especially concerned that independent repair shops can't compete with dealerships and repairers that are tied to particular brands.

Currently Europe's car sector is exempted from some aspects of competition law. This means car manufacturers, distributors and repair shops are allowed to enter into certain agreements, which might otherwise be considered illegal.

The commission is currently reviewing this "safe harbor" legislation, which is set to expire at the end of next May.

The commission wants to have rules in place which ensure equal access to technical information for all retailers and repair shops, said Marc Greven, director of legal affairs at the European Automobile Manufacturers Association.

Competition in the market for new cars, however, appeared to be healthy, the commission said. As a result manufacturers and dealerships can continue setting up exclusive contracts until May 2013, after which normal competition rules will apply, said the commission's competition spokesman, Jonathan Todd.

The three-year extension of the exemption will allow car makers and retailers to adjust to the new marketplace and won't hurt the already stricken car European car industry, market analysts say.

Interested parties are invited to comment on the commission's proposal, after which the competition authority will decide how to regulate the secondhand-car market to foster competition, Mr. Todd said.

GM, Germany remain at odds over Opel bids

BY ANDREA THOMAS

BERLIN—**General Motors** Co. and the German government failed to agree on a preferred buyer for Adam Opel GmbH, setting the stage for a standoff between the two sides over the German car maker's future.

At a meeting with GM representatives in Berlin on Wednesday, German officials reiterated the government's preference for a bid from a consortium led by Canadian-Austrian car-parts maker **Magna International** Inc., which Germany believes would safeguard local factories and jobs.

GM has yet to declare its preference, but people close to the company say it sees a number of advantages in a deal with **RHJ International** SA, a Brussels-based holding company whose largest shareholder is U.S. financier Timothy Collins, founder and head of buyout firm **Ripplewood Holdings**. GM would likely have a better chance of buying back Opel in the future, should it so desire, from a financial buyer such as RHJ than from Magna, which has long aspired to become a full-fledged auto maker.

German officials 'made clear that we have a preference for Magna.'

A third bidder, China's **Beijing Automotive Industry Holding** Co., isn't in serious contention, according to people close to the talks.

A sale would require the approval of the Opel Trust, which holds a 65% stake in the car maker. GM, which still holds a 35% stake in Opel, and the German government are equally represented on the trust's board. That means the two sides would have to broker a settlement to reach a deal.

At Wednesday's meeting, German officials "made clear that we have a preference for Magna," Deputy Economics Minister Jochen Homann told reporters afterward. He added that the government's endorsement is conditional on further concessions, in particular an increased capital commitment by Magna and its Russian partners, auto maker OAO **GAZ Group** and Russian state-controlled OAO **Sberbank**.

Magna and the Russians have offered to invest €500 million ($711 million) of their own money in Opel, with €100 million to be paid by the signing of the deal and €400 million in loans, which would gradually be transformed into equity. The consortium is seeking a 55% stake in Opel.

Germany has pledged to support Magna's plan with €4.5 billion in loan guarantees and has signaled that those funds may not be available if GM selects another bidder.

RHJ has offered to invest €275 million for a 50.1% stake in Opel, requesting €3.8 billion in government funding.

Mr. Homann said that GM expressed concerns about the government's preference for Magna but didn't endorse one bidder over another during Wednesday's talks, which lasted four hours. The discussions are expected to resume in the coming days, he said.

Boeing's profit rises 17%

Aerospace firm says it has technical fix for delayed 787 jet

By Ann Keeton
And Kerry Grace Benn

Boeing Co.'s second-quarter profit rose 17%, reflecting a year-earlier charge and strength at its defense business, but the aerospace company didn't deliver an update on when the much-delayed 787 Dreamliner will make its first flight.

Chicago-based Boeing said Wednesday it has identified a technical solution to the problem that caused a delay last month in the 787's inaugural flight. The company said it is studying ways to implement the solution and will provide an update, along with a revised financial outlook, in the third quarter.

The company has come under renewed fire after it again postponed the 787 flight, because of a structural problem that executives deemed small but that further damaged Boeing's credibility. At the time it announced the delay, Boeing said it would take a few weeks to assess the situation. Pressure on the 787 comes as Boeing faces shrinking cash on its balance sheet.

"Second quarter cash flow was better than expected, but this was purely due to timing of tax/pension payments, and we still expect the company to have to raise cash by the end of next year," J.P. Morgan analyst Joseph Nadol wrote in a report Wednesday. A revised schedule for the 787 will likely result in a lower forecast for 2009 earnings, Mr. Nadol said.

For the second quarter, Boeing posted net income of $998 million, or $1.41 a share, up from $852 million, or $1.16 a share, a year earlier. The prior-year results included 22 cents a share in charges. Revenue increased 1.1% to $17.15 billion. Analysts surveyed by Thomson Reuters expected earnings of $1.21 a share.

About half of the company's revenue comes from commercial airlines, which have been hurt by a falloff in air travel. In the second quarter, Boeing's commercial-aircraft sales fell 1.6% but profit increased 5.1% because of lower research-and-development costs. At Boeing's defense business, operating earnings grew 38% and revenue rose 9%.

The company's total order backlog was down 6.9% at $327.8 billion.

Italian broadcasters set satellite-service launch

By Giada Zampano

ROME—Italy's state-owned **RAI** SpA and commercial broadcaster **Mediaset** SpA said Wednesday that their new satellite platform will be launched July 31, a move expected to increase competition in a market now dominated by **News Corp.**'s satellite-TV unit Sky Italia.

Sky Italia has been luring advertisers and viewers away from Mediaset and RAI's free channels with its pay-TV satellite service, which offers more content. Sky surpassed Mediaset in terms of overall revenue for the first time in 2008, Italy's telecommunications regulator said this month. Mediaset, Italy's dominant private free-to-air broadcaster, is owned by the family holding company of Italian Prime Minister Silvio Berlusconi.

Mediaset and RAI's new platform, called TivuSat, will be free and will host about 22 channels, the companies said.

TivuSat users won't pay for content but will need to buy a decoder and smart card, for a total cost of less than €100 ($142). RAI and Mediaset each own 48.25% of the new venture, Tivu, with **Telecom Italia** SpA's media arm holding the remaining 3.5%.

Sky Italia wasn't immediately available for comment Wednesday. News Corp. also owns Dow Jones, publisher of The Wall Street Journal.

—Liam Moloney contributed to this article.

Delta Air Lines, AirTran sound new warnings

By Paulo Prada
And Mike Esterl

Delta Air Lines Inc. on Wednesday offered a grim outlook for the industry and said it doesn't expect a profit for 2009, even as lower fuel prices compared with a year ago enabled the carrier to narrow its loss in the second quarter.

Meanwhile, **AirTran Holdings** Inc., despite posting a profit for the period, said it expects the sector as a whole to struggle for the foreseeable future. "Our industry likely faces a slow recovery," said Bob Fornaro, chairman and chief executive of AirTran.

Adding to the bleak picture, Moody's Investors Service lowered the credit rating of discount giant **Southwest Airlines** Co. two notches to Baa3, just one notch above speculative grade. Moody's cited "continuing weak fundamentals of the domestic airline sector" in its downgrade of Southwest.

Carriers of all sizes have bemoaned the sharp drop in demand for air travel as consumers and corporate customers fly less amid the recession. While business travelers, their biggest source of revenue, try to avoid travel, vacation passengers early in the summer season were lured mostly by low fares that filled planes but generated few profits. Airlines, such as Delta, with big foreign networks are also grappling with sagging demand for travel overseas.

Atlanta-based Delta posted a loss of $257 million, or 31 cents a share, for the quarter, compared with a loss of $1.04 billion, or $2.64 a share, in the 2008 second quarter. The results included a $390 million loss from costly fuel-hedging contracts made last year, when many carriers locked in portions of this year's fuel supply at prices that have since proved to be higher than market rates.

Slumping demand prompted revenue at the post-merger Delta, including a pro-forma comparison that includes earnings at Northwest, to fall 23%.

AirTran, based in Orlando, Fla., posted earnings of $78.4 million, or 56 cents a share, for the period. It booked a loss of $14.8 million, or 14 cents a share, a year earlier. Revenue fell 13% to $603.7 million.

CORPORATE NEWS

Indian mogul blasts taxes

HCL head warns recent increase opens door to rival nations

BY PAUL BECKETT


Agence France-Presse

HCL's Shiv Nadar, shown in 2005, warned that the Indian government's increasing taxation of the tech industry threatens to curb its cost advantage.

NEW DELHI—One of India's leading technology entrepreneurs warned that rising taxation in India threatens to undermine gains that the information-technology industry could reap as the global downturn prompts multinationals to outsource more.

Shiv Nadar, founder and chairman of HCL Technologies Ltd., said in an interview that in the wake of the downturn large clients are reassessing which functions they need to keep in-house and what can be moved elsewhere to raise money and reduce head count.

"When the economy is hurting they are going back to say, 'What is our core, what is the purpose for which we exist?' " said Mr. Nadar, 64 years old. "They've started saying, 'Why not raise some cash and reduce some people and somebody else can look after this.' "

But he warned that the Indian government's increasing taxation of the industry threatens to curb its cost advantage and boost smaller-country competitors trying to challenge India's dominance.

Since 1999, the Indian government has given the tech industry an income-tax holiday to foster growth. The holiday was scheduled to end this year until the government, in its new budget unveiled earlier this month, extended it for one year—a move widely welcomed by the industry.

Separately, however, the government last year introduced a new tax called the minimum alternative tax that, in effect, imposed a 10% tax on profits in cases where companies were paying no taxes under India's income-tax regulations. In the recent budget, that tax rate was increased to 15%. Mr. Nadar said the increased burden would give countries such as Egypt, Sri Lanka, South Africa and the Philippines an advantage. "On the side there are a bunch of alternative countries that are waiting," he said.

Mr. Nadar has been a pioneer in India's technology industry since 1976, when he founded Hindustan Computers Ltd. HCL Technologies has since grown into one of India's largest tech companies. In the quarter ended March 31, it reported net income of $43 million, down 50% from a year earlier, largely because of a $39.7-million foreign-exchange loss. Excluding that loss, net income fell 2.4% to $82.7 million. Revenue increased 18% to $564.4 million.

India's technology industry, which has become a major driver of India's economic success over the past decade, hasn't escaped the downturn unscathed. Many big companies rely heavily on the global finance industry for clients, and the financial crisis has curtailed spending on new initiatives at many banks.

A key question for the future is whether the industry can pick up enough new work either from other industries looking to rationalize their operations or from existing clients outsourcing more functions to offset a prolonged financial-services slump. Mr. Nadar said he is optimistic: "For IT services in India, the environment will be good."

Mr. Nadar said big, international clients would drive consolidation in India's IT industry by demanding that tech companies handle an ever-greater number of tasks. Technology companies that don't have those capabilities, or the geographic spread required by multinationals, either have to acquire them or be acquired.

Big clients are saying, "Look, we are not going to sit here and cut this into pieces of contracts [for] 10 different people," Mr. Nadar said. "They are going to give it to one organization, and that one organization should have at least 70% to 80% of what the services are."

He added: "If you are not able to do it in 20 to 30 countries yourself, in 20 to 30 U.S. states directly, and in every country in Europe, then you won't qualify."

Earlier this month, Mr. Nadar named his daughter, Roshni, 27 years old, as executive director and chief executive of **HCL** Corp., the holding company that controls HCL Technologies and another publicly listed company, HCL Infosystems Ltd., which focuses on the Indian market.

In the interview, Mr. Nadar said her role would include treasury functions at the holding company but not company operations. "The operations companies have their executive boards, they have their executive management, they have their succession plan," he said.

Ms. Nadar, a graduate of the Kellogg School of Management at Northwestern University, noted in a statement that she has been making investment decisions for the company's treasury department since last September and is involved in the company's philanthropic investments and activities.

Gdansk shipyard shrinks in return for its state aid

BY ADAM COHEN

The European Commission on Wednesday cleared €251 million ($356.4 million) in Polish government support for the Gdansk Shipyard, ending a long-running legal battle.

Since 2004 the commission, the European Union's executive arm, has been investigating state subsidies for the historic shipyard, where the Solidarity trade-union movement was born. Much of the state aid cleared by the commission has already been paid to the shipyard.

The commission said in its ruling that the state subsidies gave the shipyard an unfair advantage over rivals. However, it allowed the state assistance after the Polish government and the shipyard's owner, Ukraine-based **Industrial Union of Donbass**, or ISD, submitted a restructuring plan. The measures include a commitment to reduce the shipyard's production capacity, including closing two of the yard's three slipways.

Under EU rules, state aid to companies generally is prohibited. Exceptions are made for businesses that boost employment in impoverished regions or those with restructuring plans in place that will ensure they can be weaned from state help.

The commission's decision authorizes the funding provided since Poland joined the European Union in 2004, as well as an additional €35 million to further restructure the yard.

Poland has been trying to prop up the shipyard since 2002, providing capital injections, guarantees, loans and tax write-offs valued at about €130 million.

EU Competition Commissioner Neelie Kroes said: "This has been one of the longest and most difficult cases I have had to deal with. We have made a tremendous effort to make sure that the yard will be viable for many years to come."

Ms. Kroes said that genuine restructuring was the only way to secure jobs for the workers.

The issue was particularly sensitive in Poland as the docks in Gdansk, on the Baltic coast, are an important part of the country's history. In 1980, 17,000 striking shipyard workers led by electrician Lech Walesa started the Solidarity movement, the first independent trade union in the Soviet bloc.

The Gdansk strikes were followed by similar strikes across Poland and ultimately helped end communism in Poland. Mr. Walesa won a Nobel peace prize in 1983 and later became Polish president.

—Carolyn Henson contributed to this article.

TomTom to cut costs anew as quarterly profit declines

BY ROBIN VAN DAALEN

AMSTERDAM—Dutch navigation-equipment maker **TomTom** NV posted a 62% drop in second-quarter profit Wednesday and said it will further cut costs.

Profit fell to €19.8 million ($28.1 million) from €51.8 million a year earlier, as sales declined 19% to €368.1 million from €453.4 million.

TomTom, along with rival Cayman Islands-based Garmin Ltd., has been hit by a sharp decline in consumer spending on electronic goods amid the economic slump and the increasing prevalence of location-based services available on mobile phones.

As a result of these pressures, TomTom said Wednesday it now aims to cut operating cost by €90 million this year, up from a previous target of €60 million in cost savings.

"In the first six months of 2009 we've realized €64 million in cost savings," Chief Financial Officer Marina Wyatt told reporters. Nearly half of those cuts came from marketing, research and development costs.

In the second quarter, TomTom sold 2.5 million personal navigation devices at an average price of €112, a 20% volume decline and a 14% price drop from a year earlier. In Europe, the company raised its market share from 44% to 45%, but its share of the U.S. market, where Garmin is dominant, fell one percentage point to 18%.

While revenue from personal navigation devices declined by over 30%, revenue from other products rose over 30%. TomTom also sells products and services such as traffic information, fleet-management tools and in-car navigation. Revenue at digital-map maker TeleAtlas was flat.

So far trading has been in line with expectations given at the beginning of the year, Ms. Wyatt said, but she refrained from reiterating the outlook, saying the company needs to see how markets develop in the second half.

In February TomTom said it expects to sell between 11 million and 12 million personal navigation devices this year, generating full-year revenue of between €1.4 billion and €1.6 billion.

Nortel auction process irks RIM

BY SARA SILVER AND STUART WEINBERG

The auction for **Nortel Networks** Corp.'s most profitable assets is giving off sparks, with at least one rival exceeding the minimum bid and BlackBerry maker **Research in Motion** Ltd. urging the Canadian government to intervene, saying it was blocked from bidding.

Final bids were submitted Tuesday for a planned Friday auction, guided by rules meant to ensure that the assets fetch the highest price as Nortel sells off pieces of itself in bankruptcy court.

An affiliate of MatlinPatterson Global Opportunities Partners III LP, which is among Nortel's largest bondholders, on Tuesday bid $725 million for the Toronto telecom gear maker's declining but still highly profitable CDMA voice unit, and for a team of researchers developing a broadband technology known as LTE. Nokia Siemens Networks, a joint venture of **Nokia** Corp. and **Siemens** AG, has offered $650 million for the assets.

MatlinPatterson, an investor in distressed assets being advised by former Nortel managers and wireless executives, said it can generate higher returns for Nortel's creditors by restructuring the units and taking them out of bankruptcy court than by letting Nortel sell them off under Chapter 11. "We will pursue opportunities to acquire additional Nortel assets as they become available," MatlinPatterson said in a statement.

On the eve of the deadline to submit bids, Research in Motion released a statement blaming Nortel, its advisers and the monitors overseeing the bankruptcy process for preventing it from bidding for the wireless assets. RIM says it would have been willing to pay $1.1 billion for those units plus unspecified assets including patents.

"Pending due diligence, RIM believes that Nortel's wireless business and certain [patents] have significant value and that Nortel has strong engineering talent in key areas, including the emerging technology of LTE, that would be beneficial to RIM," RIM said in a statement on Tuesday. "In addition, it appears that the business is profitable, and RIM may also be able to access certain tax benefits as a Canadian corporation."

RIM said it was told it couldn't bid for another set of assets within a year of bidding for the CDMA and LTE units. RIM said Nortel knew it planned to purchase patents "as part of a solution to retain key portions of Nortel's business under Canadian ownership," RIM said Monday.

Nortel said RIM refused to comply with court-approved procedures. Nortel's standard nondisclosure agreement includes a provision that requires parties reviewing its assets not to bid for other company assets within a year without the company's consent, spokesman Jay Barta said.

Norsk Hydro earnings drop 73%

BY ANNA MOLIN

Norwegian aluminum and power supplier **Norsk Hydro** ASA on Wednesday posted a 73% decline in second-quarter profit, despite a rise in demand for aluminum in China, and said it saw further cutbacks in the second half.

The company faces mounting pressure from weak aluminum prices and poor demand, and has already shut down capacity to address oversupply in the industry.

Excluding China, Chief Executive Svein Richard Brandtzaeg said he expects full-year primary aluminum consumption to decline by as much as 15% to 20% from 2008 levels. Norsk Hydro said second-quarter net profit fell to 211 million Norwegian kroner ($33.5 million) from 786 million kroner a year earlier, as revenue dropped 29% to 17.12 billion kroner from 23.98 billion kroner.

It sold more than 90% of its third-quarter primary aluminum production at about $1,475 a ton by June 30.

CORPORATE NEWS

Pepsi profit edges down

Gatorade feels heat, but Frito-Lay brand enjoys growth in Asia

BY ANJALI CORDEIRO

PepsiCo Inc.'s second-quarter earnings slipped 2% due to currency fluctuations and pressures in the North American beverage business, but the company's Frito-Lay snacks drew more cash-strapped consumers and its volumes rose in Asian markets.

PepsiCo's revenue came in lighter than analysts' forecasts, falling 3% to $10.59 billion. But excluding foreign-exchange effects, it rose 5.5%.

The North American beverages business was hurt by continued declines in its Gatorade sports drink, despite recent efforts to revive growth in that key brand.

PepsiCo International results were mixed,with declines in Europe but growth in Asia, the Middle East and Africa.

Still, Chief Executive Indra Nooyi struck a more optimistic note on global economic trends. Ms. Nooyi said cautious consumers are slowly starting to spend and that she was hopeful some signals are pointing to "green shoots" of economic recovery. Ms. Nooyi said some of the company's businesses had done a little better in June.

Pepsi

Pepsi's results were hurt by continued declines in its Gatorade sports drink.

To revive growth in Gatorade, the company said it will launch new products next year. Gatorade dominates the sports drinks category, but sales have come under pressure amid tough competition from brands such as Coca-Cola Co.'s Powerade and VitaminWater. Consumers have also migrated to cheaper options, including tap water, during the recession.

Pepsi reported its second-quarter profit slipped to $1.66 billion from $1.7 billion a year ago. But per-share figures rose to $1.06 from $1.05 as shares outstanding fell 2.5%. Excluding mark-to-market gains and restructuring expenses, earnings dipped to $1.02 from $1.03.

Analysts polled by Thomson Reuters had been, on average, looking for earnings of $1 on revenue of $10.99 billion.

At its Pepsi Americas beverage business, volume fell 6% and revenue was down 7% in constant currency as customers opted for lower-priced offerings. At its Frito-Lay snacks division in North America, volume rose 3% and revenue was up 8% on a constant-currency basis, amid strong sales of Lay's and Doritos.

PepsiCo offered no updates on its bottler bids. In April, the company made an acquisition bid for bottlers **PepsiCo Americas** and **Pepsi Bottling Group**. The bottlers have so far rejected the bid, calling the offer prices too low.

Japan firm sues Cerberus officer

BY TOR CHING LI

TOKYO—**Kokusai Kogyo Holdings** Co. is suing **Cerberus Capital Management** LP's Chief Operating Officer Mark Neporent and two former directors of a transport firm the companies jointly own for a violation of fiduciary duties that resulted in losses of 52.6 billion yen ($561.4 million).

The lawsuit is the latest tussle between private-equity firms and Japanese companies they have interests with, and adds to Cerberus's portfolio of troubles in the country—such as its investment in unprofitable Japanese bank Aozora Bank.

U.S. investment firm Cerberus, which took a 55% stake in Kokusai Kogyo KK in 2004, had appointed the three defendants to the board of the bus, hotels and property company. Japanese conglomerate Kokusai Kogyo Holdings owns 45% of Kokusai Kogyo KK.

The three Kokusai Kogyo KK directors being sued are Mr. Neporent, Toshikiyo Shimizu, who resigned in June 2008, and Kazuhiko Kawai, who left in April, according to a statement that Kokusai Kogyo Holdings issued on Tuesday.

Kokusai Kogyo Holdings said "further despotic governance could severely decrease the corporate value of the company," adding that its employees and labor unions have also voiced their disapproval with Cerberus.

Cerberus said Wednesday the suit was "entirely without merit" and conducted in "bad faith." Cerberus said it will contest the case in court, alleging that Kokusai Kogyo's lawsuit is "the latest in a long series of efforts to compel Cerberus to sell its majority stake in the company to the founding [Osano] family."

Contact details for Messrs. Shimizu and Kawai, who was vice-president of Kokusai Kogyo KK, weren't immediately available. But lawyers for the three defendants—Messrs. Kawai, Shimizu and Neporent—said in court filings that they are calling for a dismissal of the lawsuit and will respond to the charges in court.

Kokusai Kogyo Holdings is seeking to recover 52.6 billion yen in losses allegedly incurred by the three directors from actions such as the sale of a 33.16% stake in Teikoku Hotel in Tokyo for 86.2 billion yen. At the time of the sale in October 2007, the hotel was Kokusai Kogyo KK's most valuable asset. The suit alleges losses were incurred due to the decision to use the sale's proceeds for the redemption of preferred shares issued to Cerberus, rather than for paying off a 200 billion yen loan that Cerberus had extended to Kokusai Kogyo KK.

Kokusai Holdings said the "hasty" sale of the hotel stake resulted in the lost opportunity to sell the shares to another prospective buyer at a higher price, leading to a loss of 12.3 billion yen. In addition, Kokusai Holdings said, the interest rate chalked up by the group's loan was higher than the dividend yield of the preferred shares, incurring an opportunity cost of 14.8 billion yen.

The directors also led Kokusai Kogyo KK to replace loans from Cerberus by obtaining a 200 billion yen loan from Wachovia Corp. at a substantially higher rate, incurring total losses of 25.5 billion yen in increased payments and other expenses, Kokusai Holdings said.

Kokusai Holdings singled out Mr. Kawai for leading the group to sell around 98,000 square meters of land in Otonecho, Saitama Prefecture, at about half the market price, resulting in a loss of 450 million yen.

Cerberus says it "acquired a controlling stake in Kokusai Kogyo (KK) when the company was on the brink of bankruptcy and returned it to profitability." Also, "Cerberus has consistently advised the Osanos that it has no intention [to sell its stake in Kokusai Kogyo KK], and no legal obligation to do so ... ," a spokesman said.

—James Simms contributed to this article.

Tech Mahindra profit falls 49%

BY DEEPALI GUPTA

MUMBAI—**Tech Mahindra** Ltd. said its fiscal first-quarter profit fell 49%, weighed down by the interest costs on the expensive debt it took to buy Satyam Computer Services Ltd.

The software exporter said foreign-exchange losses of about $10 million also pulled down income in the April-June quarter. For the period, profit was 1.32 billion rupees ($27.4 million). Revenue slipped to 11.13 billion rupees from 11.16 billion rupees.

Tech Mahindra raised high-cost debt earlier this year to acquire Satyam, now called Mahindra Satyam, in which it holds 42.7%. Its debt was 23.8 billion rupees at the end of last month. Satyam was plunged into turmoil in January when then-Chairman B. Ramalinga Raju confessed to altering the company's accounts and creating fictitious cash balances.

Tech Mahindra is a joint venture between **Mahindra & Mahindra** Ltd., India's biggest utility-vehicle and tractor maker by sales, and **BT Group** PLC.

GLOBAL BUSINESS BRIEFS

Tele2 AB

Sales rise 3.1% as emphasis shifts to Russia and Baltics

Swedish telecommunications operator **Tele2** AB swung to a net profit in the second quarter, when charges weighed on results. Tele2 posted a net profit of 1.14 billion Swedish kronor ($149 million), compared with a net loss of 54 million kronor a year earlier, when it wrote down 183 million kronor in goodwill and invested 555 million kronor in its joint venture Plusnet. Sales grew 3.1% to 10.13 billion kronor. Along with its Nordic peers, Tele2 has invested heavily in Russia over the past few years, betting that the country will drive sales and earnings as growth in Western European markets slows. In the second quarter, almost half of Tele2's 25.4 million customers were located in Russia. An additional 13% of its customers were from the Baltic countries.

Vodacom Group Ltd.

Mobile-telecommunications operator **Vodacom Group** Ltd. on Wednesday posted a 12% rise in revenue for its fiscal first quarter as it added customers across its operations. Revenue rose to 14.2 billion rand ($1.82 billion) from a year earlier, as a 8.2% increase in revenue in its home market offset an 8.1% decline across the rest of Africa, Vodacom, which is 65% owned by the U.K.'s **Vodafone Group** PLC, said. The company said it had 41.3 million subscribers by the end of June, up almost 20% from the fiscal fourth quarter. It added 1.1 million customers in South Africa during the quarter to bring its base to 28.7 million. However, the pace of subscriber growth is set to slow now that operators must go through the process of registering customers in Vodacom's three largest markets, Chief Executive Pieter Uys warned. Vodacom listed in Johannesburg in May after Telkom SA Ltd. spun off a 35% stake in the company to its shareholders and sold a 15% to Vodafone.

Continental Airlines Inc.

Continental Airlines Inc. Wednesday apologized to India's former president, A.P.J. Abdul Kalam, for frisking him before he boarded a flight to New York. The apology came a day after India's Bureau of Civil Aviation Security filed a complaint with the local police against the Houston-based carrier for "wrongfully" frisking Mr. Kalam on April 21, in contravention of bureau rules that exempt specified VIPs from such body checks. Continental said in a statement that it has formally apologized to the former president for any "misunderstanding and/or inconvenience related to the security screening on April 21."

OAO Aeroflot

Russian flagship carrier OAO **Aeroflot** said Wednesday it will delay the purchase of five A320 and Airbus A321 planes from Airbus, a unit of **European Aeronautic Defence and Space** Co., because of the global economic downturn. The airline said it will buy two A320-200 planes in the first quarter of 2011 and the first quarter of 2012 rather than in the first quarter 2010. The delivery of three A321-200s is being moved to the first and fourth quarters of 2012 from the third quarter of 2010. Airlines world-wide have been struggling with a decline in passenger numbers as business travelers and tourists cut their spending amid the global recession.

LG Electronics Inc.

LG Electronics Inc. posted a record second-quarter profit as robust sales of mobile phones and flat-screen television sets drove sales higher. But the company sounded a cautious note about its third-quarter outlook, saying that margins from mobile phones will likely fall because of stiff competition. LG also expects demand for consumer electronics to remain tepid amid the global economic slowdown. South Korea's second-largest consumer-electronics company by sales after **Samsung Electronics** Co. said second-quarter net profit rose 62% to 1.15 trillion won ($918 million) in the quarter ended June 30, from 707 billion won a year earlier. The net profit also received a boost from 285.7 billion won in foreign-exchange gains. Sales rose 14% to 14.5 trillion won from 12.74 trillion won.

Wipro Ltd.

Wipro Ltd. reported a 12% rise in first-quarter profit, becoming the third major Indian software exporter to beat market estimates as it sounded an optimistic note. Profit at India's third-largest software exporter by revenue rose to 10.16 billion rupees ($209.8 million) in the three months ended June 30, up from 9.08 billion rupees a year earlier. Total revenue—including from IT services, IT products, consumer-care and lighting business—rose 5% to 62.74 billion rupees from 59.67 billion rupees a year earlier, helped by the addition of 26 new IT services new clients. Analysts were expecting a profit of 9.14 billion rupees on revenue of 63.22 billion rupees. "We are starting to see the first signs of stability in the business as ramp downs start to taper off and volumes start to stabilize," Wipro Chairman Azim Premji said.

Reliance Communications Ltd.

India's **Etisalat DB Telecom** Pvt Ltd. and **Reliance Communications** Ltd. said they have signed a deal worth more than 100 billion rupees ($2.07 billion) to share telecom infrastructure in the world's fastest-growing telecom market. Etisalat DB will use infrastructure operated by Reliance Infratel Ltd., the unit that runs the telecom infrastructure business for Reliance Communications, a joint statement said. Reliance Communications is India's second-largest mobile services provider by subscriber base. At the end of March, Reliance Infratel had 48,000 telecom towers. Etisalat in 2008 received spectrum and licenses to offer telecom services in 15 of India's 22 service areas. Reliance Infratel President Inder Bajaj said that under the deal, Etisalat will be offered 30,000 locations, or cell sites, from which it can transmit radio signals over a span of two years.

Avon Products Inc.

Avon Products Inc., giving details of a restructuring plan disclosed in February, said it will realign its global supply chain and streamline operations in key locations to improve efficiency. The changes, which will result in a second-quarter charge of about $77 million, will eliminate about 1,200 jobs when they are fully implemented by 2012-2013, Avon said. Avon will close its facility in Springdale, Ohio, by mid-2012, shifting that production to sites in Morton Grove, Ill., and Celaya, Mexico, and to contract manufacturers.

—Compiled from staff and wire service reports.

Biden faults Ukraine leaders' quarreling

Bickering has held up economic change, moves to end energy dependence on foreign powers, says U.S. vice president

By Peter Spiegel

Associated Press

U.S. Vice President Joe Biden receives an award from Georgia's President Mikheil Saakashvili, background, during a reception in Tbilisi Wednesday.

KIEV, Ukraine—U.S. Vice President Joe Biden chastised Ukraine's political leadership, saying Kiev risks squandering its Orange Revolution through governmental infighting that has stalemated urgently needed economic overhauls, including liberalizing its gas market to end dependence on foreign powers and their suppliers.

As he has throughout his three-day visit to Kiev, Mr. Biden reiterated the Obama administration's commitment to strengthen ties with Ukraine and rejected Russian claims that the former Soviet republic was part of Moscow's "sphere of influence."

But in sometimes harsh tones, he said the 2004 revolution, in which pro-democracy protesters overthrew a Russian-backed leadership accused of electoral fraud, was one "whose promise remains to be fulfilled" by Ukraine's current leaders.

Mr. Biden cited 19th-century Ukrainian poet Taras Shevchenko, whose literary support for Ukrainian independence prompted a Cold War-era monument in his honor in Washington, D.C., arguing that Mr. Shevchenko would today be proud of Ukraine's newfound freedoms but not its political leadership.

"I think he would also be wondering why the government is not exhibiting the same political maturity as the people, why communications among leaders have broken down to such an extent that political posturing appears to prevent progress," Mr. Biden said in a speech billed as an address to the Ukrainian people.

Ukraine's political paralysis has dragged on for months, with former Orange Revolution allies President Viktor Yushchenko and Prime Minister Yulia Tymoshenko trading accusations and preventing major energy and government reform measures from moving through parliament.

Despite the stalemate, the Obama administration has refrained from public criticism in the past, and U.S. experts on the region expected Mr. Biden to address the issue with leaders only behind closed doors.

But in a significant departure reflecting Washington's growing frustration with Kiev, Mr. Biden cast the infighting in both historical and national-security terms, saying future generations will hold the current leadership accountable if it doesn't take needed but painful steps to overhaul an economy and political system sputtering in the wake of a brutal economic recession.

"The time for inertia and neglect has long passed," Mr. Biden said in the 20-minute speech Wednesday at the Soviet-era Ukraine House. "The leaders of this country came together once in 2004 because they knew a free and prosperous Ukraine was more important than any one politician or any one political party. I have no doubt Ukrainians will come together again."

The Ukrainian stalemate has been exacerbated by coming presidential elections in January, in which both Mr. Yushchenko and Ms. Tymoshenko are expected to compete. But U.S. officials insisted the reforms must come before any change in government. "The world doesn't wait for elections," said a senior administration official traveling with Mr. Biden. "These problems are immediate."

Mr. Biden saved his toughest criticism for the government's handling of the energy sector, where the government provides large subsidies on imported natural gas that is sold domestically. Analysts have argued that the disparity between market prices and the cheap government-sold gas has created a black market where corruption is rampant.

In addition, analysts said, the large subsidies have forced Kiev to rely on below-market price imports from Russia, which allows Moscow to directly influence Ukraine's domestic economy. Twice in the past three years, disputes between Russia and Ukraine over gas payments have shut down a major gas pipeline that transits Ukraine to the rest of Europe, leaving parts of Eastern and Central Europe shivering during the winter.

Although he didn't mention Russia by name, Mr. Biden said reform of the energy sector is essential to Ukraine's independence and national security, saying that only if the country liberalizes its gas market will it be free of dependence on foreign powers and their suppliers.

"Your economic freedom depends more, I suspect in this country, on your energy freedom than on any other single factor," Mr. Biden said, urging conservation as well as reform. "That will be a boon to your economy and an immeasurable benefit, I respectfully suggest, to your national security."

Mr. Biden also announced the establishment of a joint U.S.-Ukrainian working group on energy security, which is scheduled to meet later this year.

Ukraine has already implemented some painful economic reforms, including an agreement to gradually increase energy prices, as part of an emergency $16.4 billion aid deal with the International Monetary Fund.

Mumbai gunman tells court he is ready to face execution

The surviving gunman from last year's terrorist assault on Mumbai said he was ready to be hanged and expected no leniency for providing details of the plot and confessing to his role in the attack.

"If I am hanged for this, I am not bothered. I don't want any mercy from the court," Mohammed Ajmal Kasab told a Mumbai court Wednesday, the third day of his trial.

*By **Sonya Misquitta** in Mumbai and **Matthew Rosenberg** in New Delhi*

After entering a plea of not guilty, Mr. Kasab, a 21-year-old Pakistani, stunned the court Monday with a lengthy confession of his part in November's three-day assault on luxury hotels, a train station, a Jewish center and other targets.

"I don't think I am innocent," he told the court Monday, and then proceeded to tell the story of how he went from being a poorly paid shop assistant in small-town Pakistan to the face of the carnage in Mumbai.

At first, he said, all he wanted was to be a bandit. So he and a friend headed for Rawalpindi, a city near Pakistan's capital and the country's military headquarters. They searched for bearded men, figuring Islamist militants could train them to use weapons and fight, according to the court's record of Mr. Kasab's confession.

They were directed to a house on the corner of a narrow lane. A man answered the door. "I told him we had come for jihad," Mr. Kasab said, according to the court record. The man was from Lashkar-e-Taiba, a major Pakistani militant group that has repeatedly launched terrorist strikes in India.

The next day, they were on a bus heading to Muridke, the small town where Lashkar, along with its associated charity, Jamaat-ud-Dawa, were based before a crackdown by Pakistani authorities in the weeks after the Mumbai attack. There, he said, he learned how to pray. Then, in f hills nearby, he and 19 other young men went on a basic training of sorts: they exercised and learned to shoot. After that, Lashkar did some background checks. Then he was taught to use AK-47s, rocket launchers, grenades and mortars.

A few months later, Mr. Kasab found himself in Karachi where he and the nine others selected for the Mumbai mission learned how to navigate a boat and studied their targets. Six weeks later, the 10 men embarked in a small boat to a bigger boat, Mr. Kasab said. The bigger boat's four sailors were sent back to Pakistan, along with some Lashkar operatives, Mr. Kasab said. The navigator remained aboard.

On Nov. 26, Mr. Kasab said he overheard the man who would be his partner during the attack, Abu Ismail, talking on a mobile phone. " 'You ate those four goats?' " Mr. Kasab recalled Mr. Ismail saying. " 'Can I eat the fifth one?' "

The context suggested that Mr. Ismail was discussing killing the sailors of the bigger boat. Some time later, the navigator disappeared and another one of the attackers, a man Mr. Kasab identified as Soheb, emerged from the engine room with a bloody knife. "Soheb was looking little scared," Mr. Kasab told the court.

The following day, Mr. Kasab and the other attackers piled into an inflatable dinghy. Each carried an AK-47, a pistol, eight hand grenades, ammunition, a Nokia mobile phone and dried fruit and bottled water.

They split into pairs after landing in Mumbai. Mr. Kasab said he and his partner hailed a taxi and headed to the Chhatrapati Shivaji Terminus train station.

They ducked when Mr. Ismail threw the first grenade. Then they started spraying bullets into the crowd. A picture of Mr. Kasab moving through the train station holidng a gun at his hip, has become one of the attack's enduring images. Then the pair walked to the nearby Cama Hospital and opened fire again. Soon after, in a stolen Skoda car, Messrs. Kasab and Ismail ran into a police roadblock near Chowpatty Beach. Mr. Ismail was gunned down by the officers, and Mr. Kasab was captured.

During his testimony, Mr. Kasab identified his Lashkar handlers, naming two of the men currently awaiting trial in neighboring Pakistan for their alleged role in the plot.

The judge sealed his testimony Tuesday of how he was indoctrinated by Lashkar and banned news organizations from reporting it for fear it could stoke violence between India's Hindu majority and Muslim minority.

On Wednesday, Mr. Kasab effectively invited India to execute him. "Whatever I have done, I have done in this world. It would be better to be punished in this world. It would be better than God's punishment," Mr. Kasab said.

The judge, M.L. Tahiliyani, has said he will decide Thursday whether to accept the confession . His decision is likely to affect another case being heard in India, the trial of two Indians who allegedly aided the 10 attackers, and the Pakistani case, which is scheduled to begin shortly. Mr. Kasab's attorney, Abbas Kazmi, urged the judge to accept the entire confession, saying there was no point in prolonging the trial.

Darkness and wonder on the edge of Asia

Associated Press

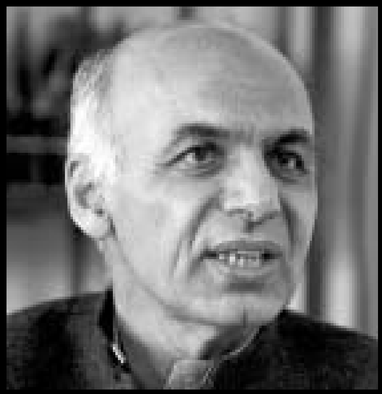
In China, people used welding masks to watch the solar eclipse that crossed Asia Wednesday, leaving some parts dark for more than six minutes. At right, the sun is blocked in the Pacific Ocean, 1,200 kilometers south of Tokyo.

New dawn | Top candidates running for Afghanistan's presidency

Hamid Karzai, 51
AFGHANISTAN PRESIDENT

Graduated from Himachal Pradesh University in India in 1983 with a degree in political science.

A member of a moderate anti-Soviet Mujahedeen group in the 1980s. Spent most of the Taliban years in Pakistan, plotting the regime's overthrow. He was chosen as interim president at a Loya Jirga in 2002 and then elected president in 2004. His popularity declined, due to war and corruption, but he still commands more name recognition and political networks than other candidates.



Ashraf Ghani, 60
FORMER AFGHANISTAN FINANCE MINISTER

Scholar-official who studied anthropology and international affairs, earning his PhD at Columbia University. Worked at the World Bank and the United Nations.

Following the fall of the Taliban in 2001 he returned to Afghanistan and later served as finance minister for Mr. Karzai, but refused to continue in the post after the president's election in 2004.

Dr. Abdullah, 49
FORMER AFGHANISTAN FOREIGN MINISTER

Graduated from Kabul University's Department of Medicine in 1983 as an Ophthalmologist.

Former adviser to military commander Ahmad Shah Massoud; acted as foreign minister for the Northern Alliance during the Taliban reign. Served as foreign minister from 2002 to 2006 in Mr. Karzai's government.

Photos: Reuters (Karzai; Ghani); Agence France-Presse (Abdullah)

Afghanistan plans debate

Young democracy slated for display for the few with TVs

By Peter Wonacott And Anand Gopal

KABUL—Afghanistan is expected to put its rough-edged new democracy on display in a televised debate between candidates vying to lead one of the world's poorest, most turbulent countries.

But only three of the 41 presidential candidates were asked to appear for the event Thursday evening, and only one looked certain to show up, reflecting the disarray of a nascent system that still lacks political parties and general ground rules for debates.

On Wednesday evening, a spokesman for the heavily favored incumbent, President Hamid Karzai, said the president wouldn't participate because he didn't have enough notice and more candidates weren't invited.

Two former senior government officials were slated to take part: Abdullah, 49 years old, an ophthalmologist and former foreign minister, and Ashraf Ghani, a 60-year-old academic and ex-finance minister who has hired U.S. political strategist James Carville as an adviser. Both candidates were expected to lambaste the record of 51-year-old Mr. Karzai, their former boss.

But after Mr. Karzai's pullout, an aide to Dr. Abdullah said the candidate would review his commitment to participate. Mr. Ghani couldn't immediately be reached for comment late Wednesday. In an earlier interview, he said he will direct his criticism to an empty lectern if the president doesn't show.

Under Mr. Karzai's leadership, he says, Afghanistan's development has sputtered, the opium trade has boomed and corruption has spiraled out of control. "President Karzai has been an extremely bad president," says Mr. Ghani. "He hasn't delivered."

The Karzai campaign spokesman, Waheed Omar, said the criticism was typical of candidates who overlooked the progress the country had made in the past eight years. "All they want to do is take credit for the achievements and blame President Karzai for the shortcomings," said Mr. Omar.

Despite the nation's long list of economic and security woes, the debate also is expected to showcase the growth of Afghanistan's young democracy. The election, set to take place Aug. 20, has helped to foster a nascent civil society of political activists and interest groups. Womens and veterans organizations have caught the attention of candidates and elevated their grievances. A raft of presidential challengers—more than 40—has spotlighted other problems, from police corruption to the effectiveness, or lack of it, of billions of dollars in foreign aid.

One of Afghanistan's private television channels will host the broadcast, a first in the country's history, according to the channel, Tolo.

Afghanistan faces the formidable task of holding an election when swaths of the country are at war. This July has been the bloodiest month for foreign troops since the war against Afghanistan's Taliban began in late 2001, with nearly three soldiers dying per day.

Despite a U.S.-led military offensive, Taliban guerrillas continue to operate freely in large parts of the country's Pashtun-dominated south, and there are growing concerns that insurgents will disrupt next month's polls.

Mr. Karzai has led Afghanistan since the U.S. and other North Atlantic Treaty Organization countries toppled the Taliban in late 2001. He was chosen then to head Afghanistan's interim government. In 2004, Mr. Karzai won the first direct presidential elections in the country's history, but the results were marred by allegations of fraud by his opponents, though the charges never went to court.

This time, Mr. Karzai has been able to strike deals with regional commanders who earlier opposed him. Such support has tipped him as the election favorite, but many experts say the race has tightened in recent weeks.

A big question mark is voter turnout, even in areas of relative calm. There have been problems with voter registration. And without paved roads in much of rural Afghanistan, thousands of donkeys will be needed to deliver election materials to polling sites, according to Margie Cook, the chief electoral adviser for the United Nations Development Program. It is also unclear how widely the campaigns of various candidates are followed. Only 7% of rural Afghanistan has electricity, thereby limiting Thursday's debate mainly to an urban minority.

Mr. Ghani says he is targeting young people—about 70% of the country is under 30 years old—and women. He promises programs that will spawn one million jobs and provide wider access to education. He also has used social networking on the Internet to recruit 8,000 volunteers around the country, he says.

For political polish, Mr. Ghani has hired Mr. Carville, the strategist for Bill Clinton's 1992 campaign for the U.S. presidency. Mr. Carville has focused partly on toning down the candidate's intellectually haughty reputation. "He's telling me not to be too smart," says Mr. Ghani, arching a dark eyebrow. "Great advice," he adds.

Mr. Carville says he is urging Mr. Ghani to play to his strengths, including an expertise in development, so he can connect to those who worry about food, electricity and jobs.

Dr. Abdullah, who goes by one name, is taking a different tack. The former diplomat has sought to highlight his Pashtun heritage and his past as a mujahedeen fighting the Soviet Union.

Most of the 40 candidates running against Mr. Karzai—almost double the number that contested the last presidential election—have virtually no chance of winning. The overloaded field obscures the most credible candidates from Afghanistan's voters, and should shrink, argues Peter W. Galbraith, the deputy special representative for Afghanistan at the U.N.

Two big Kurdish parties face election challenge

By Gina Chon

BAGHDAD—The two political parties that have long dominated life in Iraq's semiautonomous Kurdish enclave are facing their first real challenge in years as they head into elections this week.

More than 500 candidates from 24 parties or alliances are running for the Kurdish Regional Government's 111-member parliament, in polls slated for July 25. Residents also will vote for president of the region, with current President Masoud Barzani, running for a second term, being the hands-down favorite.

The parliament represents the three provinces of Iraqi Kurdistan. The region was awarded a measure of United Nations-enforced autonomy from Saddam Hussein in 1991. It held on to its semi-independence after the U.S.-led invasion in 2003 that ousted Mr. Hussein.

The region has long been dominated by the Kurdistan Democratic Party, headed by Mr. Barzani, and the Patriotic Union of Kurdistan, led by Jalal Talabani, president of Iraq. The KDP and PUK run as a coalition called the Kurdistani List. In 2005, the two parties swept area elections, capturing all but seven seats, which two smaller parties and independents share.

Candidates outside the List are trying to change that equation and capitalize on dissatisfaction with the status quo.

"The most important issue for our people is the totalitarian control of the leadership of the two dominant political parties over all sources of the economy, media and government, and all aspects of life in Kurdistan," says independent presidential candidate Kamal Mirawdeli, who is far behind in some polls but is pulling in double-digit rankings.

The biggest threat to the List is a group of former PUK members, fed up with their own party's leadership, who have cobbled together an alliance of candidates to challenge the old guard. Calling themselves the Change slate, they are poised to capture at least several seats, analysts say.

They are attracting those voters who are frustrated with what they say has been corruption, curbs on democracy and the neglect of basic services in recent years.

"They made so many promises and told us so many lies," says Omer Mahmud Salih, a resident of the Kurdish regional capital of Irbil. "Corruption exists in every country, but ours is beyond limits."

Any weakening of the two parties' hold on power could have repercussions beyond the border of the enclave. Tensions between KRG officials and the federal Iraqi government—long a cause for concern in both Baghdad and Washington—have been heating up.

The Kurdish parliament recently approved a draft constitution that has angered Baghdad because it claims several bits of contested land, including the oil-rich Kirkuk region. Kurdish officials had hoped to include a constitutional referendum to the July 25 ballot, but Iraqi federal officials overruled them.

Many Kurdish voters say they are tired of this bickering with Baghdad, too, and blame it for distracting leaders from more-pressing domestic issues, such as developing basic municipal services. President Talabani has tried to play the role of mediator, brokering meetings between the two sides behind the scenes, including a current attempt to get Mr. Barzani sit down with Prime Minister Nouri al-Maliki.

Dependable polling data aren't available, but some recent surveys suggest an opening for the Change slate. A June poll by the Solidarity with Students Organization, an independent nongovernmental group that works with Kurdish youth, suggests the race could be close. The Change slate was polling 29.5% of the vote in the survey, not far behind the Kurdistani List's 32.7% showing.

A KDP spokesman, speaking for the Kurdistani List, acknowledged that the Kurdish region has a problem with corruption and that the government hasn't accomplished enough in providing services. He said the government has done the best it could considering the challenges it faced, such as inadequate infrastructure. The two parties, he said, have been successful in attracting foreign investment to help rebuild Kurdistan and create jobs.

Iraqi Deputy Prime Minister Barham Salih, a senior PUK member, is running at the top of the Kurdistani slate. If he wins he will likely be the KRG's next prime minister. His campaign emphasizes government reforms and promises to improve services. To connect with younger voters, he hikes with groups of 20-something residents, maintains a Facebook page and regularly posts on Twitter.

The Change slate has filed lawsuits against the two main parties for campaign violations. The Kurdish government denies the accusations.

—Zaineb Naji contributed to this article.

Associated Press

A Kurdish poll worker is seen with ballot boxes during a training session ahead of regional elections for local parliament in three provinces in Sulaimaniyah, Iraq.