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What's News

European and U.S. shares gained sharply, as manufacturing data from China, the EU and the U.S. added to hopes the global economy is turning a corner. Emerging economies are driving a rally in commodities, helping shares in developed nations. Page 19

■ **Sterling hit** a seven-month high just below $1.65, but analysts doubt that the 19% rally since mid-March has much more to go. Page 19

■ **Americans' income** unexpectedly surged in April, elevated by the stimulus package, while spending fell and savings increased. Page 8

■ **The Bank of England** should resume oversight of the U.K.'s financial stability, a parliamentary committee recommended. Page 8

■ **Manufacturing activity** in the euro zone last month contracted at the slowest pace since November. Page 8

■ **Officials in Pakistan** said suspected Taliban militants abducted busloads of teenage students and staff near the Afghan border. Page 9

■ **U.K. Treasury chief Darling** apologized for an "expenses mistake" as he scrambled to avoid becoming the most high-profile figure toppled by an expenses scandal. Page 9

■ **The U.S. says** there is evidence North Korea is working on a long-range missile, but it is unclear if the rocket will be fired soon. Page 32

■ **J.P. Morgan is planning** to raise roughly $5 billion in fresh capital as part of its effort to repay $25 billion in government funds. Page 21

■ **Citigroup has told** about five former top executives that it won't pay them tens of millions of dollars in promised severance payouts. Page 25

■ **Citigroup** and Bank of America are trying to become bigger providers of services to hedge funds, even as that industry shrinks. Page 21

■ **Merck and AstraZeneca** agreed to collaborate on testing a potential new cancer regimen composed of two experimental drugs. Page 6

■ **Iraq's self-ruled** Kurdish region officially started pumping crude oil to the international market, a development that should boost the country's cash-strapped economy.

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Prison break
Inspector Clouseau's heirs stage a penal Tour de France. Page 11

Breaking news at europe.WSJ.com

GM files for bankruptcy

Obama defends government's new role, says auto executives will 'call shots'

DETROIT—**General Motors** Corp. filed for Chapter 11 bankruptcy protection early Monday, marking the humbling of an American icon that once dominated the global car industry and setting up a high-stakes gamble for U.S. taxpayers.

By Kevin Helliker, Neil King Jr. and John D. Stoll

The bankruptcy filing, made in the U.S. Bankruptcy Court in Manhattan, marks the climax of a lengthy debate over the auto maker's future after it sought a bailout from the U.S. government in December to stay alive. In the end, GM couldn't complete its restructuring out of court and filed for bankruptcy-court protection to get billions more in aid from U.S. taxpayers.

Engineering change

The question now facing 56,000 auto workers, 3,600 GM dealers and the Obama administration: Will it work?

Monday, U.S. President Barack Obama defended government intervention in GM as the auto maker enters Chapter 11 bankruptcy, saying the actions are part of a "viable, achievable plan that will give this iconic company a chance to rise again."

Under the plan, the government would own 60% of the new GM, but Mr. Obama said auto executives "will call the shots and make the decisions about turning this company around." He said the government would refrain from playing a management role in all but the most critical areas. "Our goal is to help GM get back on its feet...and get out quickly," he said.

In remarks after Mr. Obama's statement, GM Chief Executive Frederick "Fritz" Henderson said New GM will be a leaner and quicker company that is more focused on its customers and its products.

The GM chief said the company will execute changes in leadership over the next 60 days. Much of GM's management team has been in place for years or decades.

In an affidavit filed with the court, Mr. Henderson said the U.S. Treasury won't continue to fund GM's restructuring if the auto maker fails to obtain approval to sell its most valuable assets to a new entity by July 10. He said the "need for speed in approving and

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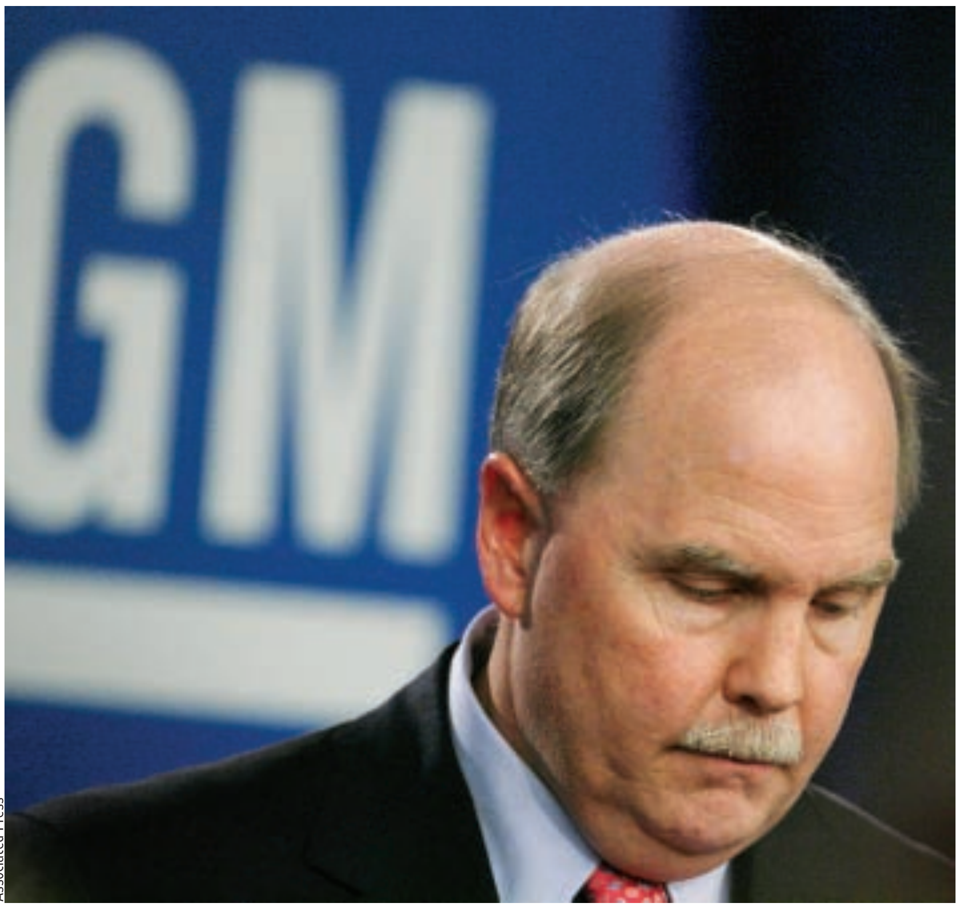

Associated Press

GM Chief Executive Frederick "Fritz" Henderson listens to a question at a news conference Monday. GM filed for bankruptcy protection as part of the U.S. government's plan to shrink the auto maker.

Airbus jet vanishes en route to Paris

By Daniel Michaels And Antonio Regalado

An Air France Airbus A330 plane with 228 people onboard disappeared over the Atlantic Ocean on Monday after suffering an electrical failure while flying through violent storms three hours after taking off from Rio de Janeiro en route to Paris.

Search teams from both sides of the Atlantic were scouring the ocean for Flight 447—which was operated by a four-year old plane that had undergone maintenance last month—according to French and Brazilian officials, while families of the passengers gathered at crisis centers set up at airports in Rio and Paris.

French President Nicolas Sarkozy told reporters at Charles de Gaulle Airport that he had asked U.S. authorities to help look for the plane with reconnaissance satellites. But after meeting some of the passengers' relatives, Mr. Sarkozy said he had "told them the truth.... Chances of finding survivors are very slim."

The Air France flight had left Rio airport at 7:03 p.m. local time (12:03 a.m. Paris time), and contact was lost with the plane around 3:30 a.m. Paris time, according to Air France Chief Executive Pierre-Henri Gourgeon. Brazil's air force said the plane's crew failed to radio in at the scheduled time of 11:20 p.m.

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Fiat, without Opel, still pursues partner

By Stacy Meichtry And Jennifer Clark

ROME—After a failed bid for **General Motors** Corp.'s Opel unit, **Fiat** SpA Chief Executive Sergio Marchionne plans to focus his attention on restructuring the Italian car maker's U.S. partner, **Chrysler** LLC, as it emerges from bankruptcy.

Behind the scenes, however, Fiat is expected to keep hunting for another partner—ideally in Europe—that can give it scale in an industry dominated by bigger rivals and bogged down by an excess of production capacity.

"The Chrysler deal doesn't...give Fiat that immediate boost of scale," says Mark Fulthorpe, a London-based analyst with auto-industry consulting group CSM Worldwide.

Six months ago, Mr. Marchionne set out to double Fiat's production to around 5.5 million cars, compared with the two million it made last year. As part of the strategy, the Italian company forged a deal with Chrysler in April and then spent the past month bidding for Opel.

On Friday, however, the German government brokered a tentative deal for GM to sell Opel to a group of investors led by Austrian-Canadian car-parts maker **Magna International** Inc. Mr. Marchionne said Fiat would focus on Chrysler. "I think we will just keep on focusing on

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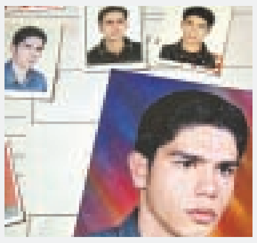

Civil-liberty debate

Juvenile executions emerge as flashpoint in Iran election
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Markets

4 p.m. ET

	CLOSE	PCT CHG
DJIA	8721.44	+2.60
Nasdaq	1828.68	+3.06
DJ Stoxx 600	214.31	+2.93
FTSE 100	4506.19	+2.00
DAX	5142.56	+4.08
CAC 40	3379.49	+3.11
Euro	$1.4158	+0.18
Nymex crude	$68.58	+3.42

THE GM BANKRUPTCY

Pain spreads through a web of companies

Auto maker spent big on IT, sports events, TV ads and lobbying

By Suzanne Vranica

In its 100 years of existence, **General Motors** Corp. hasn't just been an emblem of America's industrial might. It also has supported a nationwide economic ecosystem, from Wall Street to Washington, from Madison Avenue to Silicon Valley, which will be shaken by the third-largest bankruptcy in U.S. history.

"The fallout could be catastrophic for many businesses," says John W. Henke Jr., president of Planning Perspectives Inc., a research firm in Birmingham, Mich. "GM is so integrated into our society—from IT professions, advertising agencies, media companies and even those who provide janitorial services to GM."

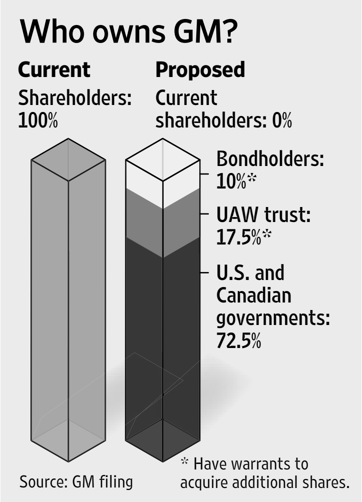
Even if GM speeds through bankruptcy court, as the Obama administration hopes, it will come out the other end a much smaller company than the one that dominated the car industry for decades.

GM is currently the biggest spender on information technology in the country, as measured by the percentage of revenue spent on IT services and software. It accounted for half the $9 billion that auto makers and their suppliers spent last year in this area, according to research firm IDC, a unit of International Data Group.

For example, **Hewlett-Packard** Co. is owed $17 million, according to court documents filed in the auto maker's Chapter 11 filing. H-P said it will continue to work with GM in support of its restructuring in a manner that protects H-P's rights as a GM creditor and supplier.

"There will be a slowing of the growth in IT spending because of GM's bankruptcy," predicts Joe Barkai, the director of IDC's Manufacturing Insights.

GM is a big player in Washington, spending $13.1 million on lobbyists last year on a wide range of issues, including climate-change legislation, renewable-fuels standards and health-care overhaul, according to the nonpartisan Center for Responsive Politics.



The auto maker has spent $169 billion on 668 acquisitions, investments and divestitures since 1985, benefiting a long list of Wall Street advisers, including **Morgan Stanley** and **Bank of America** Corp., according to Thomson Reuters. It has also issued almost $1 trillion in a variety of debt and equity.

Of all the industries to be hit, the media business stands to suffer the most, experts say. Over the decades, American brands have used television ads in particular to solidify their position in the American zeitgeist with catchy slogans such as Chevy's "Like a Rock" and Pontiac's "We build excitement." Dinah Shore helped during the 1950s with "See the USA in your Chevrolet."

It's a striking about-face from the time when GM bought up beachfront media properties at a frenetic pace, including pricey TV events such as the Olympics. TV executives dubbed network TV time as GM's "crack cocaine," while Madison Avenue executives dubbed the company "Generous Motors."

GM, long the second-largest advertiser in the U.S. after **Procter & Gamble** Co., spent $5.3 billion on advertising in 2008, according to its annual report. About $2 billion went directly into the coffers of U.S. media conglomerates, including **CBS** Corp. and **Walt Disney** Co., according to WPP Group PLC's TNS Media Intelligence.

The car maker is also one of the largest sports marketers in the country, spending about $240 million in 2007 on sports and art sponsorships, according to WPP's IEG, a Chicago-based research firm.

"There will be an enormous effect on media, both at the national and local level—we have already begun to see it," says Randy Falco, the former chief executive of Time Warner Inc.'s AOL. Mr. Falco compared the dislocation with the decline of tobacco advertising in the 1970s.

Facing plummeting car sales, GM has over the past 18 months bailed out of premium ad buys such as the Super Bowl and Oscars. It has dropped endorsement and sponsorship agreements with Tiger Woods and filmmaker Ken Burns. The car maker also slashed fees paid to ad shops, causing hundreds of layoffs in the ad business.

Ad and marketing firms were owed at least $167 million, as of May 31, according to court documents.

One of GM's largest creditors, Starcom MediaVest Inc., the media-buying unit of French ad titan **Publicis Groupe**, is owed $121.5 million. Publicis is owed another $25.3 million. The bulk of the money owed to Starcom stems from purchases made on GM's behalf. Executives familiar with the matter say Starcom's contracts stipulate it doesn't have to pay media companies for ad space until it's been paid by the client. A spokeswoman for Starcom declined to comment.

GM owes New York ad titan **Interpublic Group** of Cos. about $16 million. Interpublic's McCann-Erickson ad agency is owed another $4.6 million. GM is Interpublic's largest client, accounting for about 6% of its annual revenues. Several Interpublic units work for GM, including Campbell-Ewald, which has handled Chevy since 1922. In anticipation of the bankruptcy, Interpublic recently signed an agreement with its lenders that will allow Interpublic to draw on a $335 million credit line in the event GM files for bankruptcy.

Interpublic said Monday, "Today marks an important step toward a strong and vital GM, and we look forward to playing our part in that future success."

Interpublic recently said in a worse-case bankruptcy scenario, it has $150 million in exposure in receivables, work-in-progress and committed media. That amount does not include what it would cost Interpublic if it had to close its Detroit offices.

Executives at both ad conglomerates are hopeful each would be given "critical vendor" status, which means it would be eligible to get paid at least a portion of whatever GM owed it before GM filed for bankruptcy protection.

GM, Citigroup to leave DJIA

By Kevin Kingsbury

General Motors Corp. and **Citigroup** Inc. will be replaced in the Dow Jones Industrial Average by **Cisco Systems** Inc. and **Travelers** Co., respectively.

GM filed for bankruptcy Monday as part of a government-aided restructuring effort. Bankruptcy is an automatic disqualifier for membership in the benchmark stock index.

Citigroup is being removed because "the bank is in the midst of a substantial restructuring, which will see the government with a large and ongoing stake," Dow Jones editor-in-chief Robert Thomson said. "We genuinely hope that once the bank has refashioned itself that we will again be able to consider it for inclusion."

GM has been a component of the Dow since 1923. Because of the stock's plunge to below $1, GM makes up just 0.1% of the DJIA weighting. Citi's figure is 0.35%. The component changes take effect June 8.

CORRECTIONS & AMPLIFICATIONS

The European Parliament has the power to vote out the European Commission. A front-page article in some editions of the Friday-Monday paper said the Parliament would acquire this right if all countries ratified the so-called Lisbon treaty.

OAO Gazprom's market capitalization was about $130 billion on May 22. A May 25 Economy & Politics article on demand for natural gas in Europe incorrectly said it was around $85 billion.

The last name of David Zilkha, a former employee of Microsoft Corp. and Pequot Capital Management Inc. who sent emails that are part of a Securities and Exchange Commission investigation into possible insider trading at Pequot, was misspelled as Zikha in a Jan. 9 article on the investigation.

INDEX TO BUSINESSES

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

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INDEX TO PEOPLE

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

For more people in the news, visit CareerJournal.com/WhosNews

THE GM BANKRUPTCY

‘Old GM,’ with cast-off assets, will linger

Restructuring leaves a cleaner, leaner firm and sister with issues

By Jeffrey McCracken
And Mike Spector

The Obama administration bills **General Motors** Corp.’s bankruptcy as a fresh start for an American icon, saying it will unleash a lean competitor from court protection by summer’s end. But the remnants of GM left behind pose financial and operational quandaries that could prove an continuing drain on both taxpayers and the revitalized GM.

The proposed plan will cleave apart one of the country’s oldest and largest companies into, in effect, a “New GM” and “Old GM,” evoking the historic breakup of AT&T Corp. in 1984 into long-distance and local-phone companies. As with the dismantling of Ma Bell, GM will have to meticulously apportion every line-item of revenue and expenses to the two companies, be it employee salaries or the cost of a new wrench.

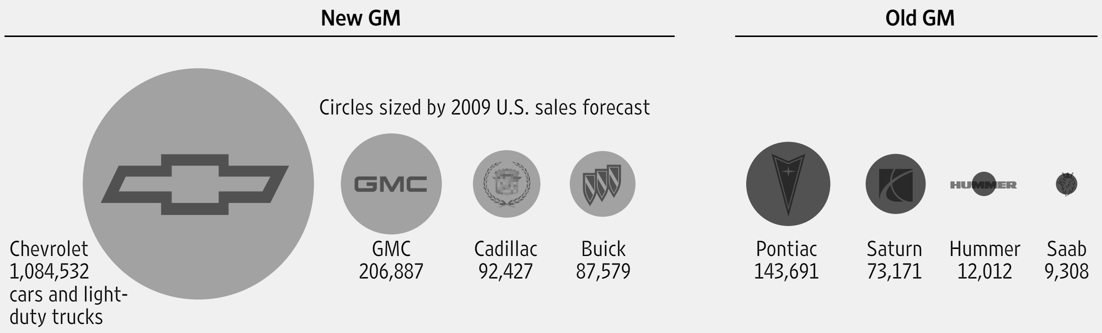
Breaking up GM represents a “very complex and time-consuming series of issues, plant by plant, and jurisdiction by jurisdiction,” said Richard Chesley, a partner in the global bankruptcy and restructuring group at Paul, Hastings, Janofsky & Walker LLP, which isn’t involved with the GM case.

The breakup also could trigger unexpected struggles among New GM, Old GM and creditors, who could fight over the best way to allocate expenses between the two in a way that maximizes creditor recovery.

Old GM—the actual name to be used for the company couldn’t be learned—also would become a parts and service-provider to New GM on an interim basis, which raises the potential for clashes over pricing and contracts, say bankruptcy advisers.

Automotive divorce

The Obama administration hopes to use a quick bankruptcy to separate a ‘New GM’ from an ‘Old GM.’ The latter will consist of Pontiac, Saturn, Saab, Hummer and other assets the company plans to shed under pressure from the administration to cut product lines. New GM is expected to emerge from bankruptcy in as little as three months, while Old GM could languish there for two or more years.



Some potential issues for the two companies:

Environmental liabilities
The New GM will leave many big liabilities to Old GM when it is in Chapter 11. But some environmental liabilities won’t be easy to shed. If a factory faces litigation over pollution, the New GM may remain on the hook.

Employee claims
The two companies will have to decide who pays what percentage of the salaries and benefits for employees who work for both companies.

Shared offices
For offices that do work for both New GM and Old GM, the companies will have to craft delicate ‘transaction service agreements’ to value the work and decide who pays the bills.

Shared plants
Some plants will be taken over by Old GM, but continue to supply parts to New GM on an interim basis. The upshot: That could create pricing and contract disputes.

Source: IHS Global Insight (unit sales)

On Monday, as part of its bankruptcy filing, GM is expected to name turnaround executive Al Koch as its new chief restructuring officer to guide the auto maker’s trip through Chapter 11 and to run Old GM, said people familiar with the matter.

Mr. Koch, who oversaw Kmart’s restructuring, will report to GM Chief Executive Frederick “Fritz” Henderson but also will report directly to the company’s board. Assuming a New GM emerges from Chapter 11, Mr. Koch will then sit atop a new, separate management team winding down Old GM. In this role, he likely will report directly to Old GM’s board, which will be different from the New GM board.

Old GM will be a sizable company itself, controlling 15 to 20 unwanted car plants containing tens of millions of square feet. It will have four vehicle brands that it plans to shed or phase out—Hummer, Saab, Pontiac and Saturn—that last year sold about 500,000 cars and trucks in the U.S.—more than Korea’s Hyundai Motor Co. or Germany’s Volkswagen AG.

The administration plans to spend north of $30 billion to fund GM’s bankruptcy, with the Canadian government lending $9.5 billion, senior administration officials said. Plans call for Old GM to receive hundreds of millions of dollars and a debtor-in-possession loan, said people familiar with the matter, to fund the liquidation and the contractors who will manage it.

While the Obama administration hopes New GM will emerge from bankruptcy in as little as three months, it could take Old GM at least two years—and up to 10 years—to disappear, say people involved in the case. Just closing a factory, for instance, can take up to a year, while moving the massive machinery used to stamp out car-body parts requires special skills.

How quickly GM can strike deals to unload assets could prove critical, given the potential need for ongoing bankruptcy financing. GM has spent months in discussions with suitors for Saturn, Saab and Hummer. It plans to phase out Pontiac, all under a directive from the Obama administration to slash its number of brands. If things don’t go according to plan, Old GM could require more money to operate until its parts are liquidated.

“You would like to have as much of this process in place as you can going in, so you can effectively get these assets marketed as quickly as you can and minimize the cash burn necessary to prop up these noncore businesses,” Mr. Chesley said.

Another critical element of the split will be a “transition services agreement” that manages how much New GM and Old GM will pay for certain employees, services and parts.

Within a few months there will be about eight factories owned by Old GM, some of which will be run by New GM on an interim basis to make parts such as engine components for New GM; later, the plants will be closed or sold. This means Old GM could be subject to all the traditional complications that can come between a supplier and customer.

“There will be complaints quickly from creditors at Old GM that they are paying too much for engineering or accounting from New GM or that New GM is not paying Old GM enough for parts,” said one lawyer involved in the GM matter.

Any conflicts will be a delicate matter for both companies. The creditors’ stake in New GM will technically sit inside the Old GM estate until it finishes reorganizing, said a senior administration official. That gives the Old GM creditors incentive to help New GM succeed.

The New GM would likely leave its more onerous liabilities with the Old GM, including some dealer-franchise disputes, product-liability claims and environmental claims. GM has about $280 million in environmental claims, according to its first-quarter government filing. But the New GM might be forced to keep some environmental liabilities if, say, certain factories have already been subject to government clean-up orders.

Ford sees opening in rivals’ woes

By Matthew Dolan

DETROIT—**Ford Motor** Co. is preparing an effort to gain market share while its two main rivals are bogged down in bankruptcy and restructuring.

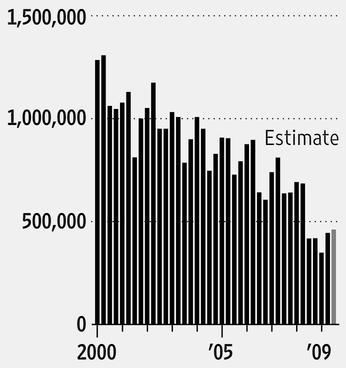
Ford, the only one of Detroit’s Big Three that didn’t need a bailout from the federal government, plans to increase production of cars and trucks in the third quarter by about 10% from the level of a year ago, a company official said. It will be Ford’s first significant production increase in almost two years.

In contrast, **General Motors** Corp., which filed for Chapter 11 protection Monday, and **Chrysler** LLC, which is nearing the end of its bankruptcy reorganization, are planning to shut down their plants for nearly all of the third quarter. The difference in production plans will give Ford a chance to push sales through the prime summer selling months while GM and Chrysler focus on their internal issues.

“This is a once-in-a-lifetime opportunity to separate us from our other domestic competitors,” said a person familiar with the matter at Ford. “No one is going to gift wrap it for us. You have to deliver the product people want to buy. That said, you have to take this historic opportunity to grab market share.”

Ramping up

Ford’s total vehicle production, quarterly data



Source: the company

Ford has seen a gain in retail market share in six of the past seven months and expects to see another boost when May auto sales are reported Tuesday. As of April 30, Ford’s U.S. market share was 13%, according to the company.

In the third quarter, Ford plans to produce 150,000 cars and 310,000 trucks for a total of 460,000 vehicles, according to company officials. A year ago it built 184,000 cars and 234,000 trucks for a total of 418,000. The bulk of the increase stems from high production of the company’s highly profitable F-150 pickup trucks.

The move represents a gamble, however. Gas prices have been creeping higher in recent weeks, topping $3 a gallon in some parts of the country. Further gas-price increases could damp F-150 sales, and a worsening of the overall economy could slow sales of both cars and trucks. If either happens, Ford could end up with elevated inventory levels later in the year.

The truck market “is still going to be a challenge,” said Michael Maroone, president and chief operating officer of **AutoNation** Inc., the largest chain of car dealerships in the U.S. and the largest Ford dealer by volume and locations.

Ford executives played down the notion the company is trying to take advantage of the troubles of GM and Chrysler. “I feel for my competitors. It’s got to be very, very difficult,” Mark Fields, Ford’s president of the Americas, said Sunday. “This is not a case of ‘Gee, let’s stick it to them.’ We have been watching our inventory levels and we’ve seen our market share grow. This is really just us working our plan.”

Getty Images

Ford plans to increase vehicle production in the third quarter by about 10% from a year earlier. Above, CEO Alan Mulally at Ford’s annual meeting last month.

Like most other auto makers, Ford is still losing money—it lost $1.4 billion in the first quarter—but it has been faring better than GM and Chrysler, in part because it borrowed $23.5 billion in 2006, before credit markets started to freeze up, and was quicker to sell some of its fringe brands. As a result, Ford had a larger cash cushion. Recently it also raised $1.6 billion in a common-stock offering.

Ramping up production can be seen as evidence of Ford’s cautious but growing confidence in the state of the U.S. auto market, which saw one of the most severe downturns in its history last year and may now be poised for a rebound.

“We’re starting to see the light nearing at the end of the tunnel,” Mr. Fields said.

THE GM BANKRUPTCY

U.S. government takes conflicting roles

It has to protect its investment in GM and regulate it, too

Even after nine months of extraordinary government intervention, the scope and complexity of the **General Motors** Corp. rescue present a thicket of conflicts unlike any seen before in Washington.

*By **Neil King Jr., Jeffrey McCracken** and **Mike Spector***

The federal government is likely within weeks to emerge as the principal owner of a storied U.S. corporation. It will also serve as the company's regulator, tax collector, customer, pension backstop and lender.

The administration of U.S. President Barack Obama put out a set of overarching principles Sunday meant to guide its interactions with GM and other companies in which the U.S. has an equity stake. After helping a company such as GM restructure, the government would manage its stake "in a hands-off, commercial manner" and not get involved in issuing day-to-day directives to GM, the guidelines said.

Given the size of the $50 billion U.S. investment, it will be hard for President Obama and Congress to say they will remain uninvolved.

"There obviously is a balancing act," White House spokesman Robert Gibbs said Friday. "While not running an auto company on a day-to-day basis, obviously there will be concern about investments by the taxpayer, as there should be."

European Pressphoto Agency

Ed Montgomery, left, White House director of recovery for auto communities, and Duane Zuckschwerdt, a UAW director, at a GM plant. The U.S. has released principles to guide its interactions with the car maker.

Chief among potential conflicts is the environmental arena. GM is one of the world's biggest sellers of full-size trucks and sport-utility vehicles. Yet such products, which include the Chevy Silverado pickup and Cadillac Escalade SUV, have always been among the company's most profitable. Detroit's chief executives recently stood with Mr. Obama on the White House lawn and embraced his aggressive new fuel-economy and emissions targets. GM, **Chrysler** LLC and others have spent millions lobbying against such strict rules for decades.

Sales of small cars with more-efficient engines, for instance, grab only about 17% of the market and remain dwarfed by pickups and SUVs.

"The government has conflicting policy objectives now," says John Casesa, a veteran Wall Street auto analyst who now heads his own advisory firm. Mr. Obama's new regulations will "cost a lot of money" and "create substantial risk to the government earning a good return on its investment," he says.

That could force the government to pump more money into a new GM down the road.

"The government will open its pocketbook again to help these companies rather than back off on its environmental agenda," Mr. Casesa says. "It can't have it both ways."

GM's government ownership also could complicate the company's life overseas, potentially raising trade and other legal disputes. Trade lawyers point out that the U.S. legal system is itself highly wary of foreign state-owned enterprises, whose acquisition efforts in the U.S. often have been rebuffed by federal authorities. GM could face similar roadblocks if it tries to expand abroad.

Congress also is sure to exert its muscle over GM's affairs, as it did in recent weeks. Key lawmakers rebelled in May when word got out that GM, post-bankruptcy, planned to boost its imports of cars made at GM factories in China.

Some experts already are asking what will happen within the Office of Management and Budget when regulations are promoted on fuel-efficiency standards or safety standards, for instance, that will prove costly to GM, and thus also to the federal government.

"Once the federal government is not simply a regulator, but is all of a sudden also on the receiving end of regulations, that fundamentally alters the politics of how the government interacts with the car industry," said John Graham, an auto-safety expert who served as President George W. Bush's regulatory czar within the OMB.

That neutrality issue will be particularly pointed when it comes to **Ford Motor** Co., which alone among the Big Three hasn't received federal assistance. Mr. Graham and others worry that the government could find itself tilting key regulatory or purchasing decisions in favor of GM or Chrysler because of its interest in those companies.

Who will gain and who will lose

General Motors Corp.'s bankruptcy will ripple across business. Here's a look at who gets hit, and how:

*By **Kate Linebaugh, Matthew Dolan, Sharon Terlep** and **Andrew Grossman***

Investors

They will be the biggest losers dollar-wise. Just how badly they fare depends on whether their money is in stocks or bonds.

Bondholders will come out slightly better. Bondholders would get 10% of GM's shares, and warrants allowing them to boost that to more than 20%. For shareholders, the picture is bleaker. Even without a bankruptcy, GM's plan would have left them with just 1% of equity. In bankruptcy, they will be wiped out. GM's stock price, last trading under $1, doesn't have much further to fall. Nine years ago, GM shares were trading at more than $90.

United Auto Workers

The auto workers union faces the bankruptcy with backing from the company and the government.

The union is likely to be treated like a preferred creditor to GM. Unlike some holdout bondholders, the UAW could be painted as a partner in the process to reduce labor costs rather than an obstacle to orderly reorganization. Post-bankruptcy, the UAW, the richest union in the U.S. as measured by assets, will be in solid financial shape. But many workers see future job and benefit cuts as inevitable. As part of the deal, the UAW agreed not to strike until 2015.

Competitors

The bankruptcy of the U.S.'s biggest car maker offers a short-term opportunity for rivals to gain market share, but some analysts say a restructured and recapitalized GM with government backing could have an unfair edge.

Cross-town rival **Ford Motor** Co., for instance, the only domestic auto maker to avert a government bailout, has gained market share this year, as that of GM and Chrysler fell, and is expected to continue to fare well. The biggest issue for Ford "is the debt service," said David Cole, chairman of the Center for Automotive Research in Ann Arbor, Mich.

Meanwhile, GM's chief foreign rival, **Toyota Motor** Corp., is flagging. Toyota reported its first annual loss in 59 years. Toyota has lost out to companies such as **Hyundai Motor** Co. that have seized on the struggles of U.S. auto makers to build brand recognition and grab customers.

Dealers

Car dealers have been slammed by the plunge in sales over the past year. In the past year, more than 1,300 dealers have been forced out of the market. Chrysler and GM cuts have cost an additional 1,900 dealers their franchises. Even survivors have to contend with tough credit markets and rising unemployment. They also must fend off "irrational pricing behavior" caused by dealers who are closing shop and selling their inventory at bargain prices, said Richard Kwas, an analyst at Wachovia Capital Markets.

In the long run, surviving dealers should be able to enjoy higher sales and less competition. The sooner the bankruptcy process proceeds, the sooner consumers may return, say dealers. Many are scouting opportunities to acquire more brands and locations, as weaker dealers throw in the towel.

Suppliers

Parts makers reliant on GM already are struggling with lower volumes, tight credit and rolling production shutdowns that reduce demand for parts. Bankruptcy will only deepen the troubles.

GM likely will ask the court to allow it to keep paying key vendors in order to maintain its supply of parts.

GM last paid its suppliers at the end of May. With production down and a bankruptcy judge in control of the company, it could be a long time until suppliers see their next check. Analysts say those with balance sheets strong enough to stay afloat until production resumes could benefit from a bankruptcy that hastens the demise of rivals.

Companies already short on cash, such as **Lear** Corp. and **American Axle & Manufacturing** Inc., are on shaky ground. GM accounted for 23% of Lear's 2008 sales and 74% of American Axle's. **Metaldyne** Corp. and **Visteon** Corp. already have filed for bankruptcy protection.

Their loss could be a gain for stronger suppliers such as **Magna International** Inc. and **Johnson Controls** Inc.

Stronach likely to use Opel to pursue an old ambition

Canadian auto-parts supplier **Magna International** Inc. was selected by the German government early Saturday as a partner for **General Motors** Corp.'s Adam Opel unit.

*By **Marcus Walker, Andrew Grossman** and **Gregory L. White***

The prospective deal for GM's European operations would mark a major breakthrough for Magna and its founder, Frank Stronach.

Speaking after marathon talks in Berlin that yielded a tentative deal between Magna and GM officials, German Finance Minister Peer Steinbrück said his government agreed to provide about €1.5 billion ($2.1 billion) in interim loans while Magna and GM finalize the contract.

Magna is partnering in the bid with Russian auto maker OAO **GAZ Group** and state-controlled OAO **Sberbank**. The company aims to purchase GM's Opel and British Vauxhall units, as well as Chevrolet's business in Russia.

If the deal is completed, Mr. Stronach would achieve one of his goals—to turn Magna into an auto maker in its own right and not just a producer of parts and an assembler of vehicles for other companies.

Mr. Stronach has "managed to go from a little guy in a garage to being part of an automobile company," said Wayne Lilley, author of "Magna Cum Laude," a Stronach biography. "I think he sees it as a capper on his career."

Mr. Stronach emigrated from Austria to Canada in 1954 and three years later started a tool-and-die company. Through mergers and acquisitions, he built it into one of the world's largest auto-parts suppliers and one of the few that has remained relatively healthy despite the industry's slump. In 2008, Magna reported net income of $71 million on revenue of $23.7 billion.

Magna is already a competitor in the car-assembly business. The Magna Steyr division assembles vehicles for auto makers in Graz, Austria. The vehicles it has made include minivans and Jeeps for Chrysler and the Z4 roadster for BMW.

Taking over Opel could present Magna with many challenges, however. For one, owning a car maker would put the company in competition with many of its customers. Based in Aurora, Ontario, Magna makes seats, electronics, interiors and engine parts, and sells them to auto makers.

Magna faces another challenge: mastering the savvy required to "figure out what the public wants," said Jim Gillette, an auto-supplier analyst at consulting firm CSM Worldwide. "To my knowledge, they really don't have any experience marketing to end consumers."

Magna has for several years focused on Russia as a priority market for expansion and had a close relationship with Oleg Deripaska, the tycoon who controls OAO Gaz. Mr. Deripaska bought a 20% stake in Magna in 2007. But he had to cede it to creditors as the financial crisis squeezed his empire last fall.

CORPORATE NEWS

EU's new tack vs. Microsoft: user chooses

Regulators pursue sanctions that would go beyond fines to address complaints of company bundling browser, Windows

BY CHARLES FORELLE

BRUSSELS—Frustrated with past efforts to change **Microsoft** Corp.'s behavior, European Union regulators are pursuing a new round of sanctions against the software giant that go well beyond fines.

The regulatory push is focused on a long-standing complaint against Microsoft: that it improperly bundles its Web browser with its Windows software. Rather than forcing Microsoft to strip its Internet Explorer from Windows, people close to the case say, the EU is now ready to try the opposite measure: Forcing a bunch of browsers into Windows, thus diluting Microsoft's advantage.

The sanctions would come from an EU investigation that began last year. The potential action would be a sharp parting blow by Europe's competition commissioner, Neelie Kroes. Last month, she hit semiconductor maker **Intel** Corp. with a record antitrust fine of $1.48 billion. The EU hasn't made a final ruling on Microsoft, and likely won't for at least several weeks. An EU spokesman says any sanction against Microsoft "would be based on the fundamental principle of unbiased choice." A spokesman for Microsoft says it is committed to "full compliance" with EU law.

The EU has stacked up more than $2 billion in fines against Microsoft since 2004. The EU's bid in 2004 to separate Microsoft's Media Player multimedia software from Windows is widely viewed as a timid solution that failed. Now, emboldened by a 2007 court ruling that upheld the 2004 case and confirmed the EU's wide discretion, regulators are inclined to go further.

People close to the case say EU regulators are inclined to demand a so-called ballot screen that would present a new computer's user with a choice of browsers to install and the option to designate one of them as a default.

The EU sent preliminary charges to Microsoft in January. In a securities filing that month, the company said the EU might "obligate users to choose a particular browser when setting up a new PC" and require manufacturers to "distribute multiple browsers on new Windows-based PCs." The EU is wrapping up the collection of written submissions from Microsoft, from **Opera Software** ASA, a small Norwegian browser maker whose complaint sparked the case, and from third parties, which were due this week. A ruling could arrive in the coming months and would almost certainly face years of appeals in EU courts.

In its legal filings to the EU, Microsoft questioned whether the EU can legally require it to offer other makers' browsers, people familiar with the matter say. It has also argued that PC users are capable of downloading other browsers like the Mozilla Foundation's Firefox and Google's Chrome, these people say.

European law has long held that a company dominating the market for one product generally can't "tie" another product to its sales. In a key 1991 case, the European Commission—the bloc's executive arm—ruled that Tetra Pak, the dominant maker of machines that package milk into cartons, couldn't force customers to buy their cartons from it alone; a 1987 ruling similarly went against a maker of nail guns and nails. European courts upheld the commission in both cases.

Despite protests by Microsoft that the low cost of downloading lets consumers easily choose another piece of software to watch videos, the commission found in its 2004 ruling that Media Player was illegally tied to Windows. An appellate court agreed and Microsoft later dropped its legal challenge. The EU's remedy was out of the milk-carton playbook: It ordered Microsoft to sell a version of Windows without Media Player. Microsoft did, but at the same price as the full version. It barely registered any sales.

In a sense, the Web-browser ballot screen is the biggest legal leap the EU is taking: A requirement to carry a competitor's product is a step usually taken in cases where the competitor has limited or no access to a distribution network—for instance, operators of electric grids who also sell electricity might be required to let other producers sell power on the grid.

Still, the EU is likely to argue that it has broad powers to fashion an effective remedy. "There's nothing in EU law that requires the remedy to be a mirror image of the infringement," says Thomas Vinje, a lawyer at Clifford Chance LLP who represents Opera Software.

Big penalties

Top antitrust-abuse fines levied by the European Commission, in millions:

2009	Intel U.S.	$1,478
2008	Microsoft U.S.	1,253
2008	Saint-Gobain France	1,249
2004	Microsoft U.S.	693
2007	ThyssenKrupp* Germany	669

*An appeal has been lodged
Source: European Commission

CORPORATE NEWS

Merck, AstraZeneca collaborate on cancer

Companies will test experimental drugs used in combination

By Ron Winslow

ORLANDO, Fla.—**Merck** & Co. and **AstraZeneca** PLC announced Monday an unusual agreement to test a potential new cancer regimen composed of two experimental agents that are still in early human trials and several years away from reaching the market.

The collaboration, sparked by an encounter between scientists from the companies in an airport security line in Dublin, is based on laboratory evidence that the two compounds given in combination could have a much more potent effect against tumors than each may have as separate treatments. Merck and AstraZeneca scientists say the treatment could prove effective against several types of cancer.

The drugs—MK-2206 from Merck and AZD6244 from AstraZeneca—are candidates for the burgeoning arsenal of so-called targeted treatments that is transforming cancer care by disrupting signaling pathways that tumor cells rely on to proliferate and survive. But cancer cells have proven adept at fending off attacks of single-agent medicines, diminishing their effectiveness. That is prompting researchers and pharmaceutical companies to explore ways to combine treatments in hopes of improving chances of curing patients of cancer or keeping their disease in check for prolonged periods.

"The notion that a single agent is going to be dramatically active in a broad population [of cancer patients] is unrealistic," said Alan Barge, vice president and head of oncology at London-based AstraZeneca. Drug cocktails are widely used in cancer treatment, but regimens are typically developed only after the medicines are in late-stage trials or already on the market. For instance, **Bayer** AG and **Onyx Pharmaceuticals** Inc., which co-market the cancer drug Nexavar, and **OSI Pharmaceuticals** Inc. and **Roche Holding** AG, which sell Tarceva, announced Thursday the launch of a trial to see whether combining the drugs will improve survival over Nexavar alone in patients with advanced liver cancer.

Merck, Whitehouse Station, N.J., and AstraZeneca are announcing the collaboration during the annual scientific meeting of the American Society of Clinical Oncology in Orlando. They say they are the first large pharmaceutical companies to join forces to test a combination treatment with compounds so early in development. AZD6244, which blocks a pathway known as MEK, has been tested in early-to-mid-stage trials in patients with skin, colorectal and lung cancers. Merck's drug, which inhibits a pathway called Akt, has been shown to have activity against tumors in a handful of patients in an early-stage test.

MEK and Akt "are two critical pathways in oncogene signaling," said Gary Gilliland, senior vice president and franchise head for oncology at Merck Research Laboratories. "If we shut down one, the other comes up to compensate." The hope is that by hitting both pathways at once, "we will shut down the escape routes."

Pearl S. Huang, a vice president and cancer researcher at Merck, had a similar thought when she heard AstraZeneca scientist Paul Smith give a lecture on the company's MEK inhibitor at a drug-development meeting in Dublin in November 2007. She immediately figured the AstraZeneca drug and the compound her group was developing would make a potentially potent anticancer combination. But when she went looking for the AstraZeneca researcher after giving her own talk, it turned out he had left the meeting.

At the airport, Dr. Huang spotted him near the front of the security line and managed to catch up with him just as he was clearing the checkpoint. "Are you the MEK guy?" she recalls asking him, having forgotten his name.

He looked at her, she says, and replied: "Let me put on my shoes." When she quickly proposed they test their two compounds together, he seemed "bewildered," she recalls. It wasn't public knowledge that Merck was developing an Akt inhibitor. But by the end of the conversation, they both agreed to take the idea to their respective companies. "We immediately clicked," she says. In an email message, Dr. Smith said he recalls thinking that being hailed as "the MEK guy" was an unusual greeting in a public place.

Even though AstraZeneca was working on its own Akt blocker and Merck was developing an MEK inhibitor, the companies say they determined that joining forces would offer a chance to get a treatment to market quicker.

The companies initially crafted an agreement to do lab studies to see if the science supported moving ahead with human tests of the combination. They cleared that hurdle. The new pact calls for the companies to share costs of testing the compounds in an early-stage trial intended to determine if the combination can safely be given to patients.

Enel to shrink debt pile via sale of gas-grid stake

ROME—**Enel** SpA said Friday it agreed to sell a majority stake in its Italian natural-gas-distribution network for €480 million ($669.2 million) to help it tackle its towering debt pile.

A day after releasing the details for an almost €8 billion capital increase, Enel, Europe's most-indebted utility, said its board approved the sale of an 80% stake in its gas grid to funds F2i SGR and Axa Private Equity. The sale will cut its consolidated net debt by over €1.2 billion, Enel said.

In March, Enel announced plans for a capital increase, as well as other multibillion-euro measures, to pay off a large chunk of debt and avert credit-agency downgrades. Among the measures presented at the time was a €10 billion asset-disposal target, which would allow the utility to lower its net debt to €41 billion by the end of 2010. At the end of March, Enel's net debt stood at €50.8 billion.

Late Thursday, Enel said it will sell nearly €3.218 billion new shares for a total of €7.98 billion, or €2.48 a piece. This represents a discount of 44% to Thursday's closing price of €4.43.

CORPORATE NEWS

Ghosn digs for synergies

Renault, Nissan aim for more cost savings to get through 'crisis'

By Steve McGrath

Carlos Ghosn, head of **Renault** SA and **Nissan Motor** Co., on Friday said he wants the car makers' alliance to yield additional savings of €1.5 billion, or roughly $2 billion, to help the companies cope with the auto industry's downturn.

"We have to move faster. Seeking synergies is no longer optional, but mandatory," Mr. Ghosn said. "We have assigned a group of experts to focus on building greater synergies to get us through the crisis and position us competitively for the future."

The alliance between France's Renault and Japan's Nissan, in place since 1999, has resulted in the sharing of platforms and powertrains, cooperation on technology and standardized manufacturing methods.

But the intensified alliance will go further. The companies will look at ways of increasing cooperation in areas including purchasing sourcing, common platforms and parts, powertrains, support functions, logistics,and advanced technologies and zero-emissions operations.

Renault and Nissan said they have identified savings that will contribute €1.5 billion in free cash flow divided between them this year. The car makers, like peers world-wide, have been hit hard by the global slump in auto sales, and Mr. Ghosn had previously said he would look to tighten the alliance.

Carlos Ghosn

Renault is Nissan's biggest shareholder, with a 44.3% interest, while Nissan holds a 15% stake in Renault.

Last month, Nissan booked its first annual net loss since Mr. Ghosn took the helm, The CEO warned that the Japanese car maker would also report a loss for this year, before returning to profitability next year. Renault's latest full-year net profit fell 79%. It said Nissan's loss in the fourth quarter would knock €1.15 billion off its own first-quarter earnings.

The companies said they had identified €363 million of savings in manufacturing and logistics for 2009, €289 million in powertrains, €279 million in vehicle engineering, €157 million in purchasing, €147 million in sales and marketing, €115 million in research and advanced technology, €48 million in information-technology and support systems and €102 million from cooperating on light commercial vehicles.

As part of the measures being implemented, Renault's plant in Brazil is to produce two additional Nissan vehicles this year, while Nissan's plant in South Africa will produce two more Renault vehicles—meaning a total of 11 vehicles will be cross-manufactured by year-end.

The companies will also share more engines and platforms, with a common platform planned for their entry-level project in India.A Nissan spokesman said sharing parts and platforms wouldn't necessarily mean a reduction in the number of models each car maker produces.

—Kazuhiro Shimamura contributed to this article.

Small cars buoy Maruti, Hyundai

By Santanu Choudhury

NEW DELHI—**Maruti Suzuki India** Ltd. and **Hyundai Motor** Co.'s Indian unit reported higher May sales as demand rose for the companies' small cars.

Meanwhile, **Tata Motors** Ltd. and **Mahindra & Mahindra** Ltd. said sales declined.

Sales at Maruti increased for the fifth straight month, gaining 16% from a year earlier to 79,872 vehicles. Local sales rose 10% to 70,785 vehicles, while exports surged 87% to 9,087, according to the Indian unit of **Suzuki Motor** Corp. of Japan.

Maruti, the largest auto maker by sales in India, introduced the Ritz, its seventh small-car model, in May amid intensifying competition from Hyundai of South Korea and **General Motors** Corp. of the U.S.

"We are seeing some initial signs of a revival in the auto industry," said Amit Kasat, analyst at Mumbai-based Anand Rathi Financial Services Ltd.

Hyundai's Indian unit said sales increased 8.4% to 43,628 vehicles. The company's local sales fell 4.1% to 23,503 vehicles, while its exports rose 22% to 20,125.

Arvind Saxena, senior vice president for marketing and sales at Hyundai India, said government incentives to boost automobile sales in Germany, Italy, France and the U.K. had boosted demand in those markets.

Sales at Mahindra fell 18% to 16,866 vehicles. The company said its sales of sport-utility vehicles fell 3.3% to 12,620.

Sales of the Logan sedan, produced by Mahindra in partnership with **Renault** SA of France, fell 72% to 427 vehicles.

Mahindra also said it has canceled a maintenance shutdown scheduled for this week at the company's Nashik plant in western India. The company is attempting to make up for production lost during a two-week labor strike last month.

Tata Motors, India's biggest domestic auto maker by sales, said sales fell 13% to 40,196 vehicles. Local sales of trucks and buses declined 3% to 23,004 vehicles, while local sales of cars and SUVs slid 20% to 15,388. Exports fell 47% to 1,804 vehicles. In the two-wheeler segment, **Hero Honda Motors** Ltd., India's largest motorcycle maker by sales, said May sales rose 23% to 382,678 vehicles.

Hero Honda, the Indian affiliate of **Honda Motor** Co. of Japan, produces motorcycles such as the Karizma and Hunk at three factories in Haryana state.

Real Madrid is set for spending spree

By Jason Sinclair

MADRID—Florentino Perez, the chairman of construction giant **Actividades de Construcción y Servicios** SA, took over the presidency of Real Madrid CF Monday, signaling the start of a spending spree to nab global stars and turn around Spain's emblematic soccer club.

Mr. Perez has said Real Madrid will need to invest as much as €300 million ($424 million) in signings to retake the spot as the world's most successful and lucrative soccer franchise, as consultancy Deloitte called Real Madrid during its golden years earlier this decade.

Mr. Perez led an aggressive expansion at ACS, Spain's largest construction company by market value. He presided over Real Madrid from 2000 to 2006. At the time, Mr. Perez signed some of the world's best-known players, such as David Beckham, Zinedine Zidane and Luis Figo. He also converted the Real Madrid franchise into one of the world's leading teams in terms of revenue.

But after a season of management turmoil and on-the-field defeats, Real Madrid needs a facelift. Former President Ramon Calderon resigned in January amid a vote-rigging scandal. Adding to the team's woes was rival Barcelona CF's victory in the European Champions' League last week.

The Spanish press has cited Portugal's Cristiano Ronaldo, Brazil's Kaká, France's Franck Ribéry and local players Xabi Alonso and David Villa as some of Mr. Perez's top picks. But during a presentation Monday, Mr. Perez didn't confirm any signings and his spokesman declined to comment about coming moves.

Real Madrid elects a management team every four years or when the previous one resigns. The next election was set for June 14, but Mr. Perez won after his candidacy went uncontested.

Mr. Perez has said that his job at Real Madrid won't interfere with his management responsibilities at ACS.

—Carlos Lopez Perea contributed to this article.

Spanish car registrations decline

MADRID—Spanish car registrations in May fell 39% from a year earlier, according to Anfac, the Spanish car manufacturers' association.

Anfac said Monday that 71,161 cars were registered last month, down from 116,112 a year earlier. The decline compared with a 46% drop in April. Car registrations are used as an indicator for car sales in Spain.

Sales to individuals and companies that aren't rental agencies fell 33%, while rental agencies bought 57% fewer cars.

Meanwhile, new-car registrations in Italy fell 8.6% last month from a year earlier to 188,670 units, the Infrastructure Ministry said.

GLOBAL BUSINESS BRIEFS

ITV PLC

U.K. will consider easing rules over advertising rates

British TV network **ITV** PLC came a step closer Friday to getting the government to ease rules on how much it charges advertisers. A potential relaxation in regulation could give ITV some breathing space as it struggles with the larger downturn in advertising. Current rules, known as Contract Rights Renewal or CRR, link the rate ITV can charge for advertising on its flagship ITV1 channel to the number of viewers. As audiences at ITV1 have fallen sharply amid the digital multichannel boom, the company hasn't been allowed to increase its ad rates to make up for the shortfall. John Fingleton, the head U.K. Office of Fair Trading, asked the Competition Commission to consider changes to the rules, with aim of making sure there's "an equal playing field."

AstraZeneca PLC

Dutch health authorities have rejected **AstraZeneca** PLC's application to sell Seroquel XR for major depressive disorder, a ruling that will delay AstraZeneca's attempts to sell the drug throughout Europe for this use. The Netherlands Health Authority decided that the drug's risks were greater than its benefits, an AstraZeneca spokesman said. The health watchdog didn't respond to a request for comment. Had the Netherlands approved the drug, it would have cleared the way for approval in other European Union countries. AstraZeneca said it will now seek approval by submitting its application to the European Medicines Agency, the EU's central medical regulator. Seroquel XR is approved in Europe and the U.S. for the treatment of bipolar disorder and schizophrenia.

Volvo AB

Truck maker **Volvo** AB of Sweden said it will cancel some previously announced layoffs at its Powertrain unit, saving 600 jobs after reaching a deal with a labor union to instead cut salaries and working hours. The division, which makes engines and gearboxes, will save jobs in the Swedish towns of Skovde and Koping by cutting working hours and paychecks by 20% and as much as 8%, respectively. The Goteborg-based company Friday said the agreement is valid from June 1 to March 31 next year. "The agreements on shortening of work hours are extremely important for us since it is then possible to retain expertise in the company despite the highly substantial reduction in demand," said Peter Karlsten, president of Volvo Powertrain.

Deutsche Postbank AG

The chief executive of **Deutsche Postbank** AG, Wolfgang Klein, will step down June 30 because of differences of opinion about the bank's future, Postbank said Friday. A spokesman for the company wouldn't say what issues led to the 45-year-old Mr. Klein's resignation, but said the bank doesn't plan to change its business strategy under his successor, Stefan Jütte, who will begin his new role on July 1. Mr. Jütte, 63 years old, is Postbank's chief risk officer and responsible for its corporate-banking and credit businesses. He previously was CEO of DSL Bank, which was acquired by Postbank in 2000. His contract as CEO runs until the end of June 2012. Mr. Klein, who became CEO in 2007, declined to comment, a spokesman said.

Cie. Financière Richemont SA

Cie. **Financière Richemont** SA said Friday that it created a new senior-management position to revive its fashion and accessories businesses. The luxury-goods company named Martha Wikstrom, 52 years old, as the head of a portfolio comprising most of its less-prominent brands, including Alfred Dunhill and Lancel, which market leather and fashion. Switzerland-based Richemont mainly sells high-end watches and jewelry. The appointment takes some weight off Chief Executive Norbert Platt, who has overall responsibility for the brands, a Richemont spokesman said. Mr. Platt will leave at year end for health reasons.

Vattenfall AB

Volvo Cars said Monday it has set up a joint venture with energy company **Vattenfall** AB of Sweden to develop cars that can be charged directly from a wall socket. Volvo, which owner **Ford Motor** Co. wants to sell shortly, said the cars will be powered by both electricity and diesel. The car's new technology is planned to be introduced to the market in 2012. Volvo said it will make the cars, while Vattenfall will develop the charging systems and supply the cars with electricity. The costs and investments in the project weren't immediately disclosed. The joint venture is the result of a cooperation project between the two companies that started in January 2007. "Through this cooperation we hope to be able to speed up the introduction of electric cars," Vattenfall's president and chief executive, Lars Josefsson, said. Volvo Cars CEO Stephen Odell said the charging time for the car's battery will be five hours, and it will last for about 50 kilometers if driven solely on electric power.

Prime View International Co.

Prime View International Co., a Taiwan company that makes electronic readers, will buy **E Ink** Corp., a U.S.-based producer of digital-ink technology, for about $215 million in cash. The merger, expected to be finalized later this year, could create a stronger competitor in the market for e-readers, such as **Amazon.com** Inc.'s Kindle, which are gaining popularity as tools for viewing books and other publications. The acquisition would give Prime View access to E Ink's key technology and patents and to critical components, the two companies said. Prime View makes the Amazon Kindle as well as **Sony** Corp.'s Sony Reader. It purchased the electronic-paper division of **Philips Electronics** NV several years ago, and has been cooperating with E Ink since then.

—Compiled from staff and wire service reports.

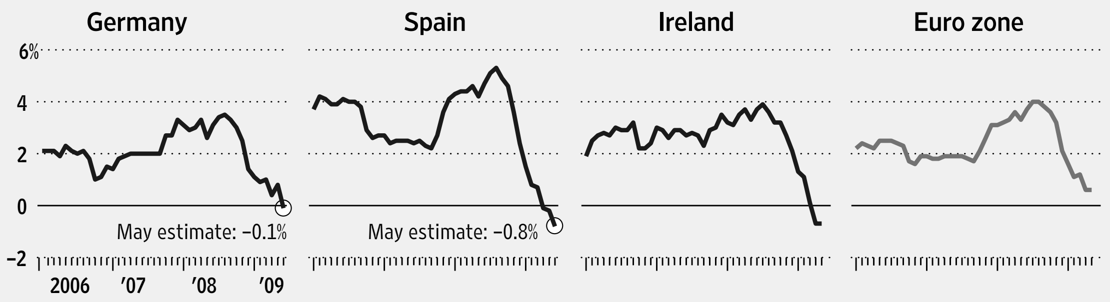
ECONOMY & POLITICS

Euro-zone inflation rate at zero

Fears grow that May decline in wages and prices will hurt recovery; a surprise for economists

By Joellen Perry
And Sebastian Moffett

Negative territory | Consumer-price indexes, change from a year ago



Note: Harmonized consumer-price indexes Sources: Eurostat; German Federal Statistical Office; Spanish National Statistical Institute

The inflation rate across the 16-nation euro zone fell to zero in May, figures showed Friday, its lowest in 13 years of records, underlining the increasing risk of deflation—a damaging decline in wages and prices that could damp recovery prospects world-wide.

Prices are falling in six of the countries that share the euro. Spain logged a third consecutive month of negative inflation in May, with prices down an estimated 0.8% from the year before. German prices slipped 0.1% last month from May 2008.

The euro-zone estimate of 0% annual inflation for May surprised economists, whose consensus was for a 0.2% rise. Even that would have been the euro zone's lowest rate since comparable records began in 1996. Economists at Royal Bank of Scotland estimate inflation hasn't been as low since 1953.

Shallow, short-lived price falls won't wreak economic havoc. But inflation is so low and the recession so deep that risks are rising of a prolonged period of declining prices and wages. Some individual EU countries—particularly Ireland and Spain—are at risk partly because of the nature of the shared euro currency. They can't compensate by allowing national currencies to fall, so wages and prices fall instead.

Deflation can hurt businesses and consumers by reducing incomes while debts remain fixed. Falling prices also can prompt shoppers to defer spending to wait for lower prices, further depressing economic activity.

After daily foot traffic at Dublin's Kingsbury Furniture dropped more than half to about 100 people early this year, the store cut prices 10% across the board. But customers asked for deeper discounts. Kingsbury negotiated lower wholesale prices from suppliers and cut store prices another 10%.

The new cuts have brought visits back up to about 150 a day. "But we don't know how long this will last," says store manager Jim Owens.

Deflation already is stalking Japan, which struggled with it from 1999 to 2005. The central bank recently forecast prices will decline for the next two fiscal years. Consumer prices in the U.S. in April were 0.7% below year-ago levels, the steepest one-year drop since June 1955, though prices excluding food and energy rose.

The U.S. Federal Reserve has fought the deflation threat aggressively, cutting its key rate close to 0% and buying hundreds of billions of dollars of assets to boost economic activity. The European Central Bank, by contrast, maintains the deflation threat is minimal, even though the euro-zone slowdown is likely to be steeper and longer than the U.S.'s. "The likelihood of deflation ... now appears slight," said ECB policy maker Mario Draghi on Friday.

Data out Friday underscored the depth of the economic slowdown. Loans to euro-zone businesses and households increased 2.4% in April from a year earlier, down from 3.2% in March and the slowest pace since comparable records began in 1997, according to the ECB.

Some private-sector economists warn that the ECB's response itself makes deflation more likely in the euro zone than the U.S. Euro-zone "deflation is a risk and the risk is growing," said Julian Callow of Barclays Capital in London.

In April, the International Monetary Fund said the U.S. and the euro zone faced "moderate" deflation risk.

Euro-zone consumers increasingly expect lower prices over the next year. Inflation expectations in May fell to their lowest level since records began in 1990, according to a European Commission survey Thursday. If consumers expect prices to fall, they may hold back on purchases, pushing prices down further.

ECB policy makers believe lower energy prices will push inflation into negative territory this summer, but they see inflation rising later in the year. The ECB's key interest rate is now 1%. The bank waited until May to announce its first modest move to buy €60 billion ($83.65 billion) in low-risk bonds.National falls in prices and wages could be welcome in some respects. Rising prices made Spanish and Irish businesses less competitive in recent years; lower costs could boost exports and draw investment.

Stimulus helps increase income for Americans

By Jeff Bater

WASHINGTON—The income of Americans unexpectedly surged in April, elevated by the economic-stimulus package, while spending declined and the level of savings increased to the highest in 50 years of records.

Personal income rose at a seasonally adjusted rate of 0.5% compared with the month before, the Commerce Department said Monday. Income fell a revised 0.2% in March; originally, income was seen down 0.3%.

Personal consumption in April fell 0.1% compared with the month before. Spending decreased a revised 0.3% in March; originally, spending was seen falling 0.2%.

Economists surveyed by Dow Jones Newswires had forecast a 0.2% decrease in personal income during April and a 0.1% drop in consumer spending. Disposable personal income—income after taxes—jumped 1.1% in April.

The stimulus plan, signed by President Barack Obama in February, provided an extra payment for the unemployed and included tax credits.

Personal saving as a percentage of disposable personal income was 5.7% in April, the Commerce Department said. It was 4.5% in March and 4.1% in February. The 5.7% rate was the highest since 5.9% in February 1995; the personal savings level of $620.2 billion was the largest since records began in January 1959.

About a year ago, the saving rate started running higher, with the economy in recession and layoffs mounting. The Bush administration had passed its own stimulus package, and people put those payments into savings. Since the recession started in December 2007, 5.7 million jobs in the U.S. have vanished, including 539,000 during April.

Separately, U.S. construction spending made an unexpected jump in April, with a rare climb in residential outlays and an increase in commercial construction.

Total spending rose 0.8% to a seasonally adjusted annual rate of $968.67 billion compared with the prior month, the Commerce Department said Monday. Spending increased 0.4% in March; originally, March spending was seen 0.3% higher.

Wall Street had expected April construction spending would sink by 0.9%. Spending was down 10.7% since April 2008.

The U.S. manufacturing sector, meanwhile, contracted at a slower pace in May, helped by growth in new orders, according to data released Monday by the Institute for Supply Management.

The ISM's manufacturing index rose to 42.8 last month from 40.1 in April. May's reading was above the 41.5 reading expected by forecasters surveyed by Dow Jones. Readings under 50 indicate contracting activity.

"While employment and inventories continue to decline at a rapid rate and the sector continued to contract during the month, there are signs of improvement," said Norbert Ore, who directs the survey for the ISM, with May the first month of growth in the new-orders index since November 2007.

The new-orders index increased to 51.1 from 47.2 in April. New orders are considered a leading indicator, and the index has risen rapidly after bottoming at 23.1 in December 2008.

Report proposes BOE oversight of finance

By Adam Bradbery

LONDON—Oversight of the U.K.'s financial stability should be returned to the Bank of England from the Financial Services Authority to help mend a faulty supervisory structure, a U.K. parliamentary committee said.

The government also should consider handing the FSA's day-to-day oversight of banks and other regulated companies to the country's central bank, the House of Lords economic-affairs committee said in a report on banking regulation.

The committee said the division of supervisory responsibilities among the authorities of the central bank, the FSA and the Treasury should be overhauled so it is clearer which entity is in charge during a crisis.

The report comes more than a year after the government proposed overhauls to the tripartite system, beefing up the central bank's financial-oversight role by creating a financial-stability committee within the bank and introducing new procedures for helping failing banks.

The Lords committee, which has been investigating bank regulation since December, said a failure of oversight was at the heart of the financial crisis in the U.K. The turmoil resulted in the collapse of U.K. mortgage lender Northern Rock in 2007 and its subsequent purchase by the government. It also triggered huge losses at many leading U.K. institutions, resulting in the government having to take majority stakes in several of the country's top banks.

The committee said the FSA had been too busy dealing with its consumer-protection role to pick up on the risks to the financial system, which arose from excessive debt levels and banks' involvement in increasingly complex and opaque financial instruments.

As a result, the Bank of England's financial-stability committee should be given responsibility for overseeing the U.K.'s financial stability and the ability to force banks to build reserves during boom periods for use during downturns, the Lords committee said.

The bank's financial-stability committee would be headed by the governor of the central bank but would include senior representatives from the FSA and the Treasury, the Lords committee said.

"This has been the most severe banking crisis since the 1930s," said Iain Vallance, the committee's chairman. "But it is already clear that there is a strong case for reforming many aspects of the supervision and regulation of banking and financial services in the U.K. and internationally."

Not all of the authorities were happy with the government's original tripartite-overhaul proposals, made in January 2008.

The Treasury said it would respond this summer.

The committee also said the government should consider shifting the FSA's microprudential role, which involves making sure companies operate within the rules, to the Bank of England as well. This would create a so-called twin peaks regulatory structure similar to those seen in Australia and the Netherlands.

—Ilona Billington, Natasha Brereton and Laurence Norman contributed to this article.

Manufacturing contracts, but at a slower pace

By Ilona Billington
And Joe Parkinson

LONDON—Euro-zone manufacturing activity in May contracted at the slowest pace since November, providing more evidence that the worst of the European recession could be over.

The purchasing managers index for the euro zone's factory sector rose to 40.7 in May from 36.8 in April, according to Markit Economics. The rise of 3.9 points was the largest since records began in June 1997.

While the data offer some good news for the economy of the 16-country euro zone, the sector remains in a contraction. A reading below 50 indicates that activity is declining.

As the euro remains firm against the dollar, the European Central Bank is widely expected to confirm its plans to buy covered bonds as another step in monetary easing at its monthly meeting Thursday.

"Manufacturers are likely to continue to find life very difficult over the coming months as they are faced by still very weak demand in domestic and export markets, as well as intensified competition," said Howard Archer, chief European and U.K. economist for IHS Global Insight. "There is little doubt that the ECB will press ahead with its plans to buy covered bonds as well as keep its interest rate down at 1% Thursday," Mr. Archer said.

Outside the euro zone, the U.K. manufacturing sector shrank for the 14th consecutive month in May, but the pace of the contraction moderated more than had been expected, in another sign that the worst is over for the sector.

Overhaul by China, U.S. seen as vital to recovery

Geithner says Beijing must help consumers boost their spending

By Andrew Batson
And Maya Jackson Randall

BEIJING—Timothy Geithner, making his first visit to China as U.S. Treasury secretary, said a sustained global recovery depends on the efforts of the U.S. and China to overhaul their economies.

"We understand that we each have a very strong stake in the health and success of each other's economy," Mr. Geithner said Monday in a speech to a small audience of students and faculty at Peking University, where he studied Chinese in the summer of 1981. "How successful we are in Washington and Beijing will be critically important to the economic fortunes of the rest of the world."

Mr. Geithner's focus on the mutual dependence of the two countries reinforces the shift in the U.S.-China relationship since the financial crisis. Under his predecessor, Henry Paulson, U.S. complaints about trade and currency policy dominated the relationship, and Mr. Paulson pushed China to give more access to U.S. financial firms. In recent months, Chinese officials have often criticized U.S. regulatory failings and questioned whether current stimulus policies risk unleashing inflation.

But both governments have been among the most aggressive in rolling out stimulus programs to counter the global slowdown. Mr. Geithner, who is in Beijing for two days of meetings with top Chinese officials, credited current signs of improvement in the global economy to the early measures taken by China and the U.S. What's needed now, he argued, are more fundamental changes to the two economies to ensure a "more balanced and sustainable global recovery."

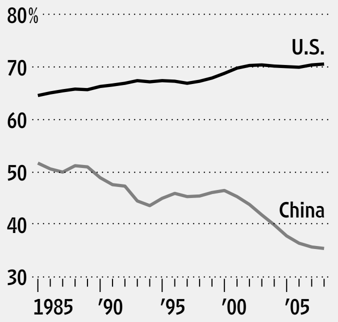
For China, he said, that means recognizing that it can't pull itself out of the slowdown by exporting even more goods to U.S. households, which are digging themselves out of debt. "The purchases of U.S. consumers cannot be as dominant a driver of growth as they have been in the past," he said. By contrast, Mr. Geithner argued, China needs to look for ways to unlock the spending power of its own consumers. "Strengthening domestic demand will strengthen China's ability to weather future fluctuations in global supply and demand," he said.

The U.S., for its part, must control a massive fiscal deficit and unwind market rescue efforts when conditions improve, according to Mr. Geithner, whose trip to Beijing comes amid a rise in long-term interest rates and mounting fears about the U.S.'s ballooning borrowing needs. "In the United States, we are putting in place the foundations for restoring fiscal sustainability," he said.

U.S. pressure on China to boost its own domestic demand—and Washington hopes, buy more U.S. goods—isn't a new policy, but has taken on increased urgency as the damage from the financial crisis has left the world with fewer likely sources of growth. Mr. Geithner urged China's government to improve its health care and social security programs, which could reduce households' need to save so much, and move to more market-based interest rates and prices.

Passing the baton

The U.S. is urging China to do more to boost consumer demand. Household spending as a percentage of GDP:



Sources: U.S. Bureau of Economic Analysis; China's National Bureau of Statistics

Timothy Geithner

Those are areas that China's government has started to address. In January, it promised a $120 billion, three-year effort to give most citizens better access to health care. The government has also raised retirement benefits and welfare payments, and says it is committed to liberalizing energy prices.

But Mr. Geithner also touched on a more contentious subject when he urged China to move toward a "flexible market-determined exchange-rate regime." Economists say that allowing the yuan to rise more would be an important sign that China is serious about boosting domestic demand. A stronger currency could hurt exporters but would also raise China's buying power in international markets, encouraging more imports.

Mr. Geithner had raised hackles in his confirmation hearing when he repeated campaign-trail assertions by President Barack Obama that China "manipulated" its currency. He has since backed away from that language, and the episode doesn't seem to have done him lasting damage in China.

"Actual actions are more important than words, and his actions were correct," said Xiao Lian, a specialist on the U.S. economy at the Institute of World Economics and Politics in Beijing. "He really understands China's situation, because he studied here when he was young," Mr. Xiao said.

Mr. Geithner was repeatedly referred to by his Chinese hosts as "a friend of China." At the end of his visit to Peking University, his former teacher, Fu Min, presented the Treasury secretary with a photo showing him as a student of Mandarin there.

Encouraging more domestic demand in the long term won't solve the woes of China's exporters today, and the government remains protective of their interests. This year, it has kept the yuan basically unchanged against the U.S. dollar. The State Council, China's cabinet, said last week the government would continue to aid exporters with measures such as improved financing and insurance. It also repeated its usual commitment to keeping the exchange rate stable at a "reasonable and balanced level."

Scandal buffets U.K.'s Darling

By Laurence Norman

LONDON—U.K. Treasury chief Alistair Darling scrambled to avoid becoming the most high-profile figure toppled by the scandal over politicians' expenses, apologizing for an "expenses mistake" that has amplified rumblings that he will be replaced by Prime Minister Gordon Brown.

Mr. Darling, one of Mr. Brown's closest allies, has been accused of simultaneously making expense claims on two homes under a program designed to provide living expenses for U.K. politicians. U.K. rules allow members of Parliament to claim expenses necessary to carry out their roles—including the cost of maintaining a second residence for politicians with constituencies outside central London.

Submitting claims for two homes would breach those rules. Mr. Darling's expense claims were among reports published Monday, the latest in a series on politicians' expense claims by London's Daily Telegraph newspaper.

Before the scandal, Mr. Darling faced talk that he might be replaced in a shuffle of Mr. Brown's cabinet. The Treasury chief's reaction to the news shifted during the day. On Monday morning, Mr. Darling called the newspaper's report that he simultaneously claimed for two houses "untrue." Prime Minister Brown said he believed there was nothing substantial in the report.

Mr. Brown later said Mr. Darling had made an "inadvertent" mistake. The prime minister declined to say in an interview with Sky News television whether he would keep Mr. Darling in his post after what are expected to be difficult local and European elections for the governing Labour party on Thursday.

Later in the day, Mr. Darling "unreservedly" apologized in television interviews, offered to repay part of the £1,000 expense claim, and said while he hopes he retains the moral authority to stay in his position, his fate rests in Mr. Brown's hands. Mr. Darling said his mistake shouldn't prompt him to resign.

"I tried to put that right today, and I hope people will accept that, but I understand fully why people are thoroughly...angry about what is going on," Mr. Darling told the British Broadcasting Corporation.

The expenses scandal has led to about a dozen lawmakers being suspended from their Parliamentary parties—but not their seats—or announcing they will step down at the next election. On Monday evening, a spokesman for Mr. Brown said the prime minister retained full confidence in Mr. Darling.

Militants abduct students in Pakistan

By Matthew Rosenberg
And Rehmat Mehsud

ISLAMABAD—Suspected Taliban militants apparently abducted busloads of teenage Pakistani students and staff from a boys' school in a Taliban stronghold near the Afghan border, officials said.

Scant details were available about Monday evening's events in the North Waziristan tribal region, home to some of the most powerful militant warlords in Pakistan. Official said between 25 and 60 people had been taken by the gunmen.

The incident comes amid a jump in attacks on security forces in Pakistan's tribal belt, a strip of mountainous territory where the Taliban holds sway and al Qaeda often operates openly.

Pakistani officials fear the violence is a Taliban attempt to distract the military from the Swat Valley to the north, where the army last month began an offensive after militants there violated a peace deal that had given them control of the area.

With the army now saying it is close to pushing the Taliban from Swat, Pakistani officials have begun strongly suggesting their next target will be one or both of the twin regions of North and South Waziristan, arguably the Taliban's most important strongholds in Pakistan.

The abduction occurred when the students and staff of Cadet College Razmak in North Waziristan piled into buses to leave the area after local officials decided to close the school two weeks before its scheduled summer holiday because of the deteriorating security situation, said a security official in Bannu, a town near the tribal region where the convoy was headed.

But the convoy of 20 to 30 buses managed to get only about 30 kilometers from the school before it was hijacked by men armed with assault rifles, grenades and rockets, the official said.

Authorities were working to determine exactly how many people were missing. The Bannu security official said four buses carrying 50 to 55 students and four teachers had been taken by the gunmen. But Javed Alam, the vice principal of the school, said only two buses were missing, and surmised there could be "around 25 to 35" people missing.

Pakistan's Cadet Colleges are boarding schools for teenage boys that are often run by retired military officers, although they have no direct link to the military and don't funnel their students to the armed forces. There was no immediate claim of responsibility.

ECONOMY & POLITICS

CAPITAL JOURNAL ▪ GERALD F. SEIB

In his bid to ease Muslim relations, what exactly should Obama say?

WHEN U.S. President Barack Obama walks to a lectern at Cairo University on Thursday, he'll be talking to an auditorium full of Egyptians—and to more than a billion people beyond.

Quite explicitly, Mr. Obama will be directing a speech to the world's Muslims, a fifth of the globe's population. Regardless of how much attention he gets at home, it will be one of the most carefully observed performances around the globe by a president in recent history.

Yet it's hard to know what to say. Especially since the Sept. 11, 2001, attacks, Americans associate Islam with terror and danger—and Muslims know that full well.


Barack Obama

Americans also tend to think of the Islamic world as synonymous with the Arab world, or at least the Middle East. Reality is far more complicated. The four nations with the largest Muslim populations actually lie outside the Middle East. The U.S. has good relations with some Islamic nations and terrible relations with others, but confronts extremism in many and mutual suspicion in most.

That's what Mr. Obama is trying to change. White House officials say he will tell Muslims that there isn't an inherent conflict between the modern world and the Islamic world, contrary to what Islamic radicals claim. Muslim societies have produced great advances in science and culture; those who say modernity and Islam are in conflict are willfully ignoring reality and history.

But what else? In a search for answers, the Capital Journal column asked some wise foreign-policy thinkers to summarize what *they* would say. Here are excerpts from their replies; to see their full responses, go to the Capital Journal blog at Wsj.com/capitaljournal.

Richard Haass, president of the Council on Foreign Relations and author of "War of Necessity, War of Choice: A Memoir of Two Iraq Wars": Any speech needs to address the Israeli-Palestinian issue, which will be uppermost on the minds of many in Egypt and beyond....President Obama must also challenge Arab and Muslim societies and leaders. It is correct to point out that the overwhelming number of Arabs and Muslims everywhere reject terrorism—but it is no less true that a high percentage of today's terrorists are Arab and Muslim. Something is deeply wrong. Educational reform is a must. Literacy is necessary but not sufficient.

There are also several things the president should not do. He should not present a detailed blueprint for Israeli-Palestinian peace. It would be inappropriate to do so in an Arab capital....Second, he should not hype elections; electocracy is not democracy. What is needed is more civil society, independent institutions, and checks and balances. And third, he should not apologize....Many Americans have risked or lost their lives defending Arabs and Muslims in Kuwait, Bosnia, Afghanistan and Iraq.

Lee Hamilton, president of the Woodrow Wilson International Center and former chairman of the House International Relations Committee: I think he has to show respect for the Islamic world. He has to welcome a new chapter in our relationships with that world....He should indicate his broad policy goals. We don't seek any territory; we don't seek to capture any resources. That may sound kind of irrelevant to an American audience, but it is not to that audience.

I think he should indicate a willingness to help them with their problems but make it clear that only they can solve their problems....In the words of an old politician, there's a simple rule in American politics when you appear before an audience, and that is you want to let them know you're on their side. In a sense I think that is what Obama's mission is.

Elliott Abrams, Middle East adviser to President George W. Bush: The speech should be about freedom and the future: about the need for Muslim societies to open up so that every citizen can contribute his and especially her talents. Political, social and gender limitations are preventing these societies and the people in them from realizing their God-given abilities. He should declare our complete belief in political freedom, democracy and the equality of all citizens and of men and women....

And he should not adopt the view that the world's troubles and those of Islamic countries are bound up in the Israeli-Palestinian conflict. Probably the single worst thing he could do is buy into that false line of reasoning. He should not pander. He should not apologize for our country.

Aaron Miller, adviser to six secretaries of state on Arab-Israeli negotiations: We don't need another "Why America loves and respects the Muslim world" speech. I would argue that what he needs to do is address an issue which resonates with the Arab and Muslim world. I would argue that issue is the Palestinian issue. He doesn't have to lay down a peace plan, but he has to be the breaker of icons.

Nabil S. Mikhail, Egyptian native and adjunct professor at George Washington University and the University of Maryland: For a couple of days, President Obama will be the honorary chairman of the The Islamic World Inc., addressing the Arab and Islamic masses—the shareholders of that huge conglomerate....He will tell them, "Here are our interests, and these are your interests. Can we meet, or even correlate somehow, somewhere?"