Leading the News: Lloyds must fill in for Blank as chairman plans departure

THE WALL STREET JOURNAL.

VOL. XXVII NO. 73 | EUROPE | MONDAY, MAY 18, 2009

DOWJONES A News Corporation Company

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Reuters

Congress party supporters in the northern Indian city of Allahabad celebrate the general-election victory. Party officials said they expect to propose a new coalition government to India's president by midweek.

India victors plan overhaul

By Peter Wonacott

NEW DELHI—India's Congress party, fresh from winning the world's largest democratic vote, is preparing to inject new blood into India's government as it attempts to revive the country's economy and scrub the sullied image of Indian politicians.

On Sunday, a day after securing the largest number of seats in Parliament of any single party, the Indian National Congress began work to form the next government. A meeting of senior Congress party officials endorsed their prime ministerial pick, Manmohan Singh, who has occupied the post for the past five years.

Party officials said they expect to propose the new coalition government to India's president by midweek, and ministerial slots will begin to fill soon after that. The deadline for the new government to be in place is June 2.

A decisive victory has made the task of reaching a parliamentary majority of 272 seats easier. By the latest tally, the Congress-ruled United Progressive Alliance had won about 260 seats, compared with about 160 seats for its rival, the National Democratic Alliance, which is led by the Bharatiya Janata Party. On its own, the Congress party won about 205 seats of the 543 elected seats in the lower

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U.S. investors get impatient for a recovery

By E.S. Browning

Investors have been easy to please in the past two months. The global economy started getting worse at a slower pace and the financial system avoided a meltdown, so they pushed up stocks more than 30%.

Now, investors are starting to ask for something more. They want signs that actual economic improvement is coming. They didn't get anything like that last week, and they began selling stocks again.

"All we have now is 'less-worse' economic data, and that is a big step, but what we would like to see is growth," said Marc Stern, chief investment officer at Bessemer Trust, which manages about $50 billion in New York. "For this rally to sustain itself, it can't simply be a matter of 'less-worse' forever."

The data last week were downright disappointing—the opposite of what people had hoped to see. The government reported that U.S. retail sales fell more than expected in April. Chinese industrial production rose less than expected in April. Weekly U.S. jobless claims abruptly turned higher.

With stocks getting close to their highs for the year, investors cashed in some of their recent profits. The Dow Jones Industrial Average fell 3.6% last week and the broad Standard & Poor's 500-stock index 5%. Those were the sharpest declines since the week ended March 6, the week before the recent rally began.

On May 8, the S&P finished at 929.23, almost back to its 2009 high of 934.70, reached on Jan. 6. Since then it has headed south.

The Dow remains down 42% from its 2007 record close and the S&P down 44%.

Credit Suisse warned clients to brace for a further pullback after the big gains. Its global equity strategist, Andrew Garthwaite, published a report saying any stock recovery was more likely to look like a W than a V. He urged clients to cut back on holdings of stocks tied to things like consumer spending, such as retailers, and buy stocks of companies that are likely to have steadier sales, such as food producers.

New York research firm Strategas Research Partners was even more pessimistic. It warned clients that economic performance could look more like a square-root sign: down, up and then sideways.

Much of the recent optimism was based on data suggesting that the pace of the economy's slide was slowing, which was seen as a prelude

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U.K. speaker faces pressure to resign

By Alistair MacDonald And Aaron O. Patrick

LONDON—The U.K.'s ruling Labour Party suspended a second member of Parliament over expense claims, as pressure increased from politicians for the speaker of the Commons, the lower House of Parliament, to step down.

Several MPs have said Speaker Michael Martin may face a no-confidence vote from members. Over the weekend, Nick Clegg, the head of the opposition Liberal Democratic Party, became the most senior politician to call for Mr. Martin's resignation. Members of Mr. Martin's Labour Party have also called for his resignation.

Mr. Martin will make a statement to Parliament on Monday about "resolving the problem of allowances as swiftly as possible," a spokeswoman said.

Over the past two weeks, the London-based Daily Telegraph newspaper has run a series of stories claiming dozens of members of Parliament have been reimbursed for expenses ranging from the petty to the extravagant, provoking widespread anger across the U.K.

Recent opinion polls show British voters turning away from the two biggest parties, Labour and the Conservatives. Both parties have been hurt by the news of the expense claims and by revelations that some MPs are earning extra money

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GM's dropping of dealerships points toward imminent filing
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Markets

	CLOSE	PCT CHG
DJIA	8268.64	-0.75
Nasdaq	1680.14	-0.54
DJ Stoxx 600	202.92	+0.60
FTSE 100	4348.11	-0.33
DAX	4737.50	-0.02
CAC 40	3169.05	+0.40
Euro	$1.3592	+0.01
Nymex crude	$56.34	-3.89

LEADING THE NEWS

Euro-zone GDP drops

Germany records first fall since 1970; seeds of recovery seen

By Marcus Walker

BERLIN—The euro-zone economy suffered its sharpest slump on record in the first quarter of 2009, underlining the severity of Europe's recession.

Gross domestic product in the 16-nation euro currency area fell by 2.5% in the period from January to March, compared with the fourth quarter of 2008. That means Europe's economic heartland was contracting at an annualized rate of nearly 10% in the first quarter. Germany, Europe's biggest economy, had an even bigger quarterly fall, its worst since 1970—contracting by 3.8%, or an annualized minus 14.4%.

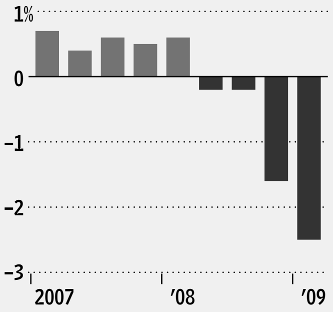
However, the latest monthly indicators for business activity suggest the pace of Europe's recession has slowed sharply. "This kind of pace of contraction will probably not be repeated," said Greg Fuzesi, economist at J.P. Morgan in London: "You're not going to get minus 10% again."

A growing number of analysts believe the euro-zone economy could stabilize by this fall and return to growth around the end of the year, although unemployment is expected to continue rising until well into 2010. Business surveys have shown new orders stabilizing, while big drops in inventories in the past two quarters are expected to lead to higher production by firms in coming months.

Few business people in Europe are that confident yet, but some see signs that a trough is near. At German engineering company **Trumpf Group**, which makes machine tools, orders in the first quarter fell by more than 20% from a year earlier. But in April, orders stopped falling for the first time since the financial crisis escalated in September.

Falling further

Gross domestic product of the 16 countries that share the euro, change from the previous quarter



Note: Seasonally adjusted Source: Eurostat

In some markets, including China and parts of Europe, demand even started to grow slightly again last month, says spokesman Ingo Schnaitmann. "Whether it is sustained or a flash in the pan remains to be seen," Mr. Schnaitmann said.

What's certain is that the euro zone took an unprecedented beating in the first quarter, with the biggest contractions coming in countries that rely on exporting manufactured goods.

European labor unions are stepping up demonstrations against rising job cuts. Around 40,000 people marched in Brussels on Friday, calling on governments to strengthen worker protections. A march in Madrid on Thursday that drew 20,000 people. French farmers also blockaded several dairy companies across Thursday and Friday to protest against wholesale buyers slashing milk prices amid a slump in global demand.

In Germany, sharply falling exports and business investment were behind the slump, the government said, while consumer spending grew slightly thanks mainly to Germany's cash-for-clunkers incentives that lifted new-car sales. In March, German exports and industrial orders started to recover. Retail sales, though, have continued to weaken.

Retail conglomerate **Arcandor** AG on Friday became the first retailer to say it will apply for credit guarantees from the German government's bailout fund for companies hit by the financial crisis. Arcandor is asking for €650 million ($877 million); Chief Executive Karl-Gerhard Eick blamed banks rather than weak sales.

"Not only for us, but many other companies, it's barely possible in these times to get new loans or to extend existing ones," he said.

Italian GDP fell 2.4% in the first quarter, or by 9.4% at an annualized rate. One bright spot for Italian industry is car maker **Fiat**, whose new-car registrations in Europe rose 4.7% in April from a year earlier. Overall, European new-car registrations fell by 12% year-to-year in April.

France's economy, which depends less on exports, shrank by 1.2% in the first quarter. The French government also revised down GDP for the third quarter of last year to minus 0.2% from plus 0.1%, meaning that French GDP has contracted in the past four quarters, like the euro-zone.

Spain published figures on Thursday showing that its economy shrank by 1.8% last quarter, or by 7% at an annualized rate.

Many economists believe the euro-zone economy, and Germany, will contract much more slowly in the second and third quarters. The terrible first quarter means euro-zone GDP is on course to contract more than 4% this year, even if it stabilizes in the months ahead.

Countries in Eastern Europe are hurting even more than their Western neighbors. In both Slovakia and Latvia, GDP dropped 11.2% in the first quarter. Hungary's economy contracted by 2.3%, its fourth straight decline.

—David Gauthier-Villars and Paul Hannon contributed to this article.

Lloyds Chairman Blank will retire within a year

By Sara Schaefer Muñoz

Associated Press

Victor Blank will step down from Lloyds Banking Group by June 2010.

Lloyds Banking Group PLC's Chairman Victor Blank will step down in the next year, reflecting fallout from the bank's disastrous decision to acquire lender HBOS PLC in September.

Mr. Blank, 66 years old, will leave at some point before the bank's 2010 annual general meeting, the bank said Sunday. Lloyds named director Alexander Leitch to the new role of deputy chairman until a successor for Mr. Blank can be found. A spokesman for Lloyds couldn't say how long it will be before the bank names a successor.

Mr. Blank and Chief Executive Eric Daniels have faced heavy criticism from shareholders since Lloyds, the U.K.'s fifth-largest lender, agreed to take over HBOS last fall in what amounted to a government-sanctioned bailout. The combined group has since been forced to take billions of pounds in government capital and participate in a U.K. asset-insurance plan in which the bank agreed to surrender a majority stake to the government.

"I believe it is the right time for the group to appoint a new chairman," Mr. Blank said in a statement released by the bank. "I will continue working until my successor is appointed to ensure the successful integration of the two banks."

Mr. Blank, the former CEO of U.K. investment bank Charterhouse, has been chairman of Lloyds for three years. He was widely seen as key in facilitating the HBOS merger, encouraging the government of Prime Minister Gordon Brown to waive competition concerns.

The U.K. Shareholders Association, a group that represents individual investors, sent a letter to Lloyds shareholders on Saturday urging them to vote against Mr. Blank's re-election at the bank's annual meeting June 5.

The HBOS merger "has turned out to be a mistake," Roger Lawson, the group's spokesman, said in an interview on Sunday. "He should accept the responsibility for it, and resign and go quickly."

U.K. Financial Investments, which manages the government's 43% stake in Lloyds, said it "looks forward to working closely, alongside other shareholders, with the Lloyds board as they identify his successor."

Lloyds insured £250 billion ($379 billion) of bad assets under the U.K. asset-insurance plan, the majority of which were risky, legacy loans belonging to HBOS. As part of the price for the insurance, it agreed to let the government's stake in the bank rise above 50%.

In a trading update this month, Lloyds said it expects impairment charges on souring corporate loans to rise more than 50% in 2009, from about £9 billion in 2008, as the U.K. economy worsens, leading to a loss for the year.

The bank "will be able to comfortably manage through the expected near-term economic downturn," Mr. Daniels said when giving the trading update.

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

Editeur responsable: Daniel Hertzberg M-17936-2003

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

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

LEADING THE NEWS

VW, Porsche take break

German auto makers disagree on how long talks will be halted

A WSJ News Roundup

Volkswagen AG said Sunday it was indefinitely postponing talks over a planned integration with **Porsche Automobil Holding** SE, but the sports-car maker insisted that only the next round had been canceled.

As the power struggle between two of Germany's leading auto companies appeared to increase, Volkswagen spokesman Peik von Bestenbostel told the Associated Press that the talks had been put on hold for an undetermined period of time, and urged a more direct engagement from Porsche.

"Before we can take up talks again, it is necessary that Porsche adopts a clearly constructive attitude toward them," Mr. von Bestenbostel said.

But Porsche insisted in a statement Sunday that while a working-group meeting Monday on the fusion of the two car makers had been canceled, "The negotiations that were begun last week will continue as planned."

The wrangling occurred ahead of a Monday meeting by Porsche's supervisory board, which is to bring together Volkswagen Chairman Ferdinand Piech and members of the Porsche family. The Porsche and Piech families control 100% of the voting stock at Porsche.

On May 6, Porsche's owner families decided to enter talks with the Wolfsburg, Germany, auto company over forging an integrated company with 10 independent brands, including Porsche's sports-car operations.

But Mr. Piech, a grandson of Ferdinand Porsche, who founded the company that bears his name, questioned the plan Tuesday by saying that Porsche must reduce its debt before an integration could be possible. Porsche took on €9 billion ($12 billion) in net debt as it increased its stake in Volkswagen to 51% last year.

How best to handle that debt is expected to be the focus of Monday's board meeting. Porsche's supervisory-board chairman, Wolfgang Porsche, who opposes a sale of Porsche's sports-car operations, so far hasn't publicly commented on the remarks by his cousin, Mr. Piech.

Gunnar Kilian, spokesman for the head of Volkswagen's works council, Bernd Osterloh, told the AP that constructive talks aren't possible in the "current environment," and he urged Porsche to clarify exactly how it envisions the integration process moving forward.

Porsche spokesman Albrecht Bamler said the company can finance its credit payments.

Reuters

Volkswagen employees assemble a VW Passat in Emden, Germany, last month. VW is urging Porsche to take a 'constructive' attitude toward integration talks.

Japan opposition chooses veteran as party leader

By Yuka Hayashi

TOKYO—Yukio Hatoyama, a veteran lawmaker from a well-known political family, won an election Saturday to lead Japan's main opposition party, making him a likely candidate to seek to become the nation's next prime minister.

The Democratic Party of Japan selected Mr. Hatoyama, 62 years old, as its leader at a time when the party has a strong chance of unseating Prime Minister Taro Aso's Liberal Democratic Party in national elections later this year.

Since the departure of popular Prime Minister Junichiro Koizumi in 2006, the LDP, a conservative party that has ruled Japan nearly continuously for more than half a century, has grown unpopular and weak, hurt by policy mishaps, gaffes and an empowered opposition in parliament.

Mr. Hatoyama replaces Ichiro Ozawa, who was forced to step down as leader of the upstart, 11-year-old DPJ on Monday after a campaign-finance scandal eroded his popularity. In an internal vote of the party's members of parliament, Mr. Hatoyama easily beat Katsuya Okada, a 55-year-old former trade ministry bureaucrat popular among voters for his clean and serious image.

A grandson of a prime minister and son of a foreign minister, Mr. Hatoyama is known for his pedigree and considerable personal wealth—a combination that has also propelled Mr. Aso, his LDP counterpart, to the top of his party. In contrast to Mr. Okada, who has publicly discussed the need for tax increases to achieve fiscal discipline, Mr. Hatoyama isn't known for any particular economic policy stance, although his party is expected to continue with its populist policies.

"I pledge to lead in our effort to realize a change in power," Mr. Hatoyama told DPJ members as he accepted his appointment. "Let's make the DPJ the driving force in a wholesale cleanup of Japan."

The appointment ends a brief period of uncertainty at the DPJ. The arrest in March of Mr. Ozawa's top aide, for charges of knowingly accepting illegal political donations, has eroded voter support for the DPJ, while enabling Mr. Aso to rebound from his rock-bottom popular ratings.

CORPORATE NEWS

GM to close 1,100 dealerships in U.S.

Move indicates auto maker is heading toward bankruptcy filing, as court would be able to break franchise pacts

By Sharon Terlep

General Motors Corp.'s announcement Friday to owners of 1,100 U.S. dealerships that it intends to drop them from its retail network is a new indication that the auto maker appears headed for a bankruptcy filing as soon as June 1.

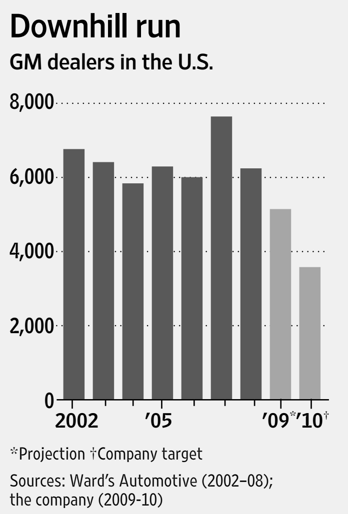
Letters to the affected dealers said the company doesn't expect to continue doing business with them beyond October 2010. In a conference call with reporters, General Motors sales chief Mark LaNeve acknowledged that carrying out the plan would be difficult outside of bankruptcy-court protection.

State franchise laws make it onerous and expensive for manufacturers to force dealers out of business, but franchise contracts can be nullified in bankruptcy court. **Chrysler** LLC is taking advantage of bankruptcy court to close 789 of its 3,200 dealerships by voiding their contracts, the company said Thursday.

"Without a legal [bankruptcy] filling, these [dealer cuts] would be hard to enforce," Mr. LaNeve said. Dealers "may want to take legal action. We're not looking to get into a legal battle."

He added that "the legal parameters around what you can do and can't do would change" in bankruptcy.

MOVING OFF THE LOT: A closed dealership in New York's Long Island, above, will have more company.



GM has said it hopes to avoid a Chapter 11 bankruptcy-protection filing. But earlier last week, Chief Executive Frederick "Fritz" Henderson said a bankruptcy filing by the auto maker is "probable."

The 1,100 GM dealerships to be cut represent the first wave of a wider downsizing of the company's network. In total, the company plans to eliminate about 2,400 of its 5,969 stores. Among them are 470 dealerships that sell Saturns, Saabs and Hummers. GM plans to sell or shut down those brands.

Mr. LaNeve said dealers whose brands are being eliminated in many cases will have a chance to sell GM lines that survive.

GM reported losses of nearly $90 billion in the past four years and has required $15.4 billion in government loans to keep operating. The White House's auto task force has given the company until June 1 to reach cost-cutting agreements with workers and bondholders and begin trimming dealers or face a bankruptcy filing.

GM is close to a deal with the United Auto Workers union, but bondholders have resisted its offer to swap $27 billion in debt for a 10% stake in the reorganized company.

The letters that went to the 1,100 GM dealerships don't mention the possibility of a bankruptcy filing. They simply state that GM doesn't believe it can have "a productive relationship" with the selected dealers and doesn't expect their "contractual relationship to continue past October, 2010," according to a termination letter reviewed by Dow Jones Newswires.

GM declined to disclose which dealers were sent the letters.

Years of declining sales have left both GM and Chrysler with many more dealerships than they need. As a result, their dealers often compete with each other for customers, hurting their profits.

Most of the GM dealers selected are "hurting, losing money and in danger of going out of business anyway," Mr. LaNeve told reporters. "It's a move that people could argue should have been taken years ago."

GM said the 1,100 dealerships to be cut represent 18% of its network but produced just 7% of its sales last year. Nearly 500 of them sell fewer than 35 new GM vehicles a year, Mr. LaNeve said.

The National Automobile Dealers Association said the affected dealerships employ about 63,000 salespeople, mechanics and other personnel.

"We view GM's action with a profound sense of sadness and disappointment," the trade group said, adding that, "NADA fully expects GM to honor all its obligations to the affected dealers, whether or not they decide to wind down their operations."

AutoNation Inc., a large dealership chain, was informed that contracts for six of its 41 GM stores won't be renewed. The company's chief executive, Michael J. Jackson, said the six outposts weren't generating any operating profit.

Overall, the GM stores to be closed have a combined inventory of 65,000 cars and trucks. GM plans to buy back some of the dealers' remaining inventory, parts and equipment. In addition the auto maker plans to shut down production for much of the summer to trim its backlog of unsold vehicles.

GM expects additional dealership reductions will come as dealers, struggling with the worst sales environment in decades, go out of business on their own.

The company believes that having fewer, healthier dealers will help it better compete with foreign-based rivals such as **Toyota Motor** Corp. and **Honda Motor** Co., which tend to have newer, better-financed stores in more attractive locations.

Deal would slice GM's labor and health costs

By John D. Stoll

General Motors Corp., under the direction of the U.S. Treasury, is near a deal that would cut its hourly labor costs by more than $1 billion a year and reduce its $20 billion pledge to the United Auto Workers to cover health-care obligations, said people familiar with the matter.

The plan is still in flux, but GM and the union could finalize terms as early as this week.

The Detroit auto maker expects to halve its remaining cash outlays for retiree health costs to about $10 billion, and supplement that contribution with a 39% equity stake in the reorganized GM, the people familiar with the matter said.

Cutting GM's health-care costs is an essential part of the "controlled bankruptcy" plan the Treasury Department is formulating for GM.

GM declined to comment on the matter. A UAW spokesman couldn't be reached.

The proposed deal, which could still fall apart, would have to be approved by the UAW's 60,000 members at GM, who are expected to face steep cuts in pay and benefits, as well as 20,000 additional layoffs.

By at least tentatively agreeing to the latest concession, the union—which once prided itself on offering members gold-plated benefits, job security and pay increases—is taking another big hit in hopes of saving the auto maker, which employed nearly 200,000 UAW workers just a decade ago.

In 2007, the UAW moved to protect one of its key benefits: health care for retirees. It did so by agreeing to fund a new $35 billion health plan—known as a Voluntary Employees' Beneficiary Association—that would assume responsibility for retiree health-care costs starting in 2010.

The trust ended GM's exposure to health-care inflation by capping what it would pay in long-term health-care costs. The cap meant the UAW would eventually need to cut coverage for hundreds of thousands of retirees and their family members.

GM has already provided about $15 billion to the VEBA, but still owes $20 billion under an agreement that would have let it fund the trust over time.

The original plan was viewed as the largest UAW concession in history. The idea was to help clear long-term obligations off GM's balance sheet, and eliminate billions of dollars a year in cash outlays.

But the collapse of the U.S. auto market in 2008, and continued erosion of GM's market share, upended the company's financial assumptions, and forced the parties back to the bargaining table. People involved in the negotiations say the two sides have been able to approach an accord this time without the lengthy battles that hampered previous negotiations.

Many worries remain for union officials, say people involved in the discussions. They say that the stock GM proposes to contribute to the VEBA is illiquid and hard to value, posing a big risk for UAW members. The union had initially asked for more from Treasury officials in the negotiations, but was rebuffed.

With UAW backing in sight, people inside the Treasury are increasingly confident they can push through a massive reorganization of the auto maker, overriding protests from its bondholders and dealers. Some GM bondholders are expected to argue in court that their interests are being trampled on, with their claims taking a back seat to those of employees.

A key element in the plan is the ability to execute what the Obama administration has dubbed a "quick rinse," which would place GM under bankruptcy protection and then remove its most valuable assets from court oversight.

Treasury hopes to short-circuit protests from creditors by lining up deals before GM enters bankruptcy proceedings. In coming days GM is expected to approach secured lenders, including major banks, to renegotiate about $6 billion in debts, according to people familiar with the matter.

GM plans to ask its lenders for more time to pay its debt. It doesn't plan to ask for a significant reduction in the amount of debt it owes, said people close to the discussions.

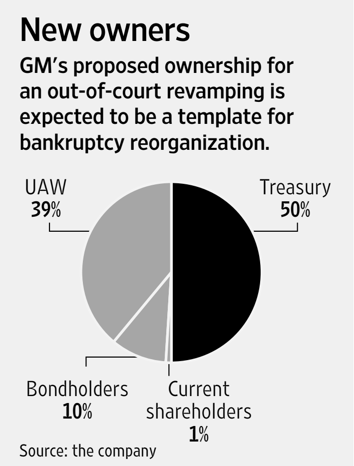
Another critical task for the auto maker will be to persuade a bankruptcy judge that unsecured bondholders—owed at least $27 billion—are being treated fairly in a reorganization. GM has offered them 10% of the company's equity.

The bondholders, who say the offer is equivalent to four cents on the dollar, have fired back with a counterproposal asking for 58% of the new GM's equity, and a bigger slice than the UAW's. But administration officials, emboldened by concessions wrested from **Chrysler** LLC's lenders, are taking a hard line, according to people close to the Treasury.

These people say the Obama administration wants a GM bankruptcy "to be as clean as possible," but isn't "going to pay ransom to bondholders."

A steering committee representing the bondholders has had trouble persuading the administration's automotive task force to sweeten terms of a debt-for-equity swap, people attending the meetings said.

The steering committee and other bondholders expect to raise legal objections to GM's bankruptcy plan if it doesn't change the current offer, said Eric Siegert, managing director at Houlihan Lokey, which represents the steering committee.



Germany considers giving aid to Opel

By Andrea Thomas

BERLIN—Adam Opel AG could be taken into a government-supported trusteeship to keep the German car maker operating if its parent, **General Motors** Corp., enters bankruptcy before Opel can be sold.

German Economics Minister Karl-Theodor zu Guttenberg said Thursday the government would consider the step, which could include interim financing, only if the two remaining bidders for Opel submit bids in more detail by Wednesday.

Should the U.S. government and GM fail to be responsive to the proposal, "we have to continue to consider an orderly insolvency," Mr. zu Guttenberg said in an interview with German weekly Welt am Sonntag published Sunday. "For me such a non-state led trusteeship model is the maximum conceivable offer that can be made."

Italian auto maker **Fiat** SpA and a consortium that involves Canadian auto-parts maker **Magna International** Inc. are the two bidders.

GM must institute a variety of cost reductions, including culling its dealers and cutting debt, by a June 1 U.S. government deadline or face a bankruptcy-court filing.

A trusteeship and bridge, or interim, financing from banks would keep Opel operating so takeover negotiations could continue without tapping taxpayer money, Mr. Guttenberg said.

Carl-Peter Forster, head of GM's European operations, told the Frankfurter Allgemeine Zeitung newspaper that Opel would need credit in excess of €1 billion ($1.36 billion).

Fiat Chief Executive Sergio Marchionne has told German officials that his plans to create a company by merging Fiat's auto unit with Opel will require as much as €7 billion in financing backed by state guarantees.

—Stacy Meichtry contributed to this article.

Fiat to meet with unions

Talks, also planned with government, aim to ease Opel deal

By Stacy Meichtry

Bloomberg News

Fiat CEO Sergio Marchionne, seen at a book presentation Friday in Italy, is under pressure to preserve jobs as the auto maker attempts to merge with Opel.

Fiat SpA Chief Executive Sergio Marchionne has agreed to hold talks with Italian government officials and unions in an effort to avoid labor opposition that could derail his plans to make Fiat one of the world's largest car makers.

Italian Industry Minister Claudio Scajola on Friday released excerpts of a letter Mr. Marchionne recently sent the minister, pledging to meet with the Italian government and unions as soon as Fiat knows the outcome of its proposed merger with Opel, the German unit of **General Motors** Corp. Fiat, of Turin, Italy, already has signed a deal to buy 20% of **Chrysler** LLC.

A Fiat spokesman confirmed the contents of the letter.

Mr. Marchionne is coming under pressure from the governments of Italy and Germany over potential plant closures and job losses that could result from his plan. Mr. Marchionne told reporters Friday that he hadn't set a date to meet Mr. Scajola. The executive also confirmed his plan to submit an offer for Opel by the German government's May 20 deadline.

Any government opposition could hurt Mr. Marchionne's plans because Fiat is counting on the Italian and German governments to guarantee financing of as much as €7 billion, or around $9.4 billion, for the new company.

German union leaders who sit on Opel's board are adamantly opposed to the deal, saying the merger could eliminate 18,000 jobs across Europe. Pressure is mounting in Italy, as well. A week ago, Mr. Scajola sent an open letter to Mr. Marchionne requesting a meeting with the executive and highlighting the "centrality" of Fiat's Italian plants to Italy's economy.

"I agree to the opportunity of a meeting," Mr. Marchionne responded in writing, according to the industry ministry statement. Mr. Marchionne wrote that his plans to create a new company, which would include Fiat's 20% stake in Chrysler, aimed to "secure an industrial future for the Italian automotive system, despite the grave crisis that has hit the automotive sector worldwide," the statement said.

Separately, Chrysler began notifying the initial 1,200 parts makers it plans to keep after the company merges with Fiat.

Chrysler Chief Executive Officer Bob Nardelli told the suppliers in a letter Friday how they could switch their contracts to the new company. Mr. Nardelli also told them they will be paid some of the money Chrysler owed them before the auto maker filed for bankruptcy protection April 30.

—Jennifer Clark and Jeff Bennett contributed to this article.

GMAC rebrands itself Ally Bank

By Aparajita Saha-Bubna

GMAC LLC, starting Friday, renamed its bank Ally Bank.

GMAC's conversion to a bank holding company in December formed the central plank of its survival plan, as prohibitive borrowing costs fueled by the funding freeze in credit markets and losses piling up at its auto-finance and mortgage units forced the lender to drastically shrink its lending operations in 2008.

The company's executives hope that the rebranding of GMAC Bank will spur retail deposit growth, a key funding source for GMAC amid the continuing credit squeeze. Aside from federal help, GMAC LLC, the lender affiliated with **General Motors** Corp., has few avenues to raise capital.

The name change marks a shift away from the GMAC brand that underscored the lender's association with the auto maker. GMAC, set up in 1919 to provide financing to buyers of GM vehicles, initially was an acronym for General Motors Acceptance Corp. Its name, at the time, underscored its complete and undivided ownership by and loyalty to the auto maker.

"We certainly value our relationship with GM and GM continues to be an important customer," said Sanjay Gupta, GMAC's chief marketing officer. "In addition to that, GMAC wants to grow as a bank holding company. The launch of Ally Bank provides a new platform to increase deposits."

The new name was culled from a shortlist of about a dozen names. "Ally conveys the sense of a trusted partner, the attributes we are trying to convey" Mr. Gupta said.

GMAC is jointly owned by GM and an investor group led by private-equity firm **Cerberus Capital Management LP.** The auto maker and the investor group will significantly scale back their ownership in GMAC by the end of this month as a condition of the lender becoming a bank holding company.

GMAC is awaiting federal funds after the company assumed the mantle of lender for **Chrysler** LLC vehicles.

Steelmaker Severstal swings to loss

By Andrew Langley

MOSCOW—Russia's largest steelmaker, OAO **Severstal**, on Friday swung to a first-quarter net loss, said it is unlikely to pay dividends this year and declined to give a forecast, saying the future of the market remains too uncertain.

"The restocking and increased government investment in infrastructure seen in the first quarter is likely to continue to support steel demand this year," Severstal said. "But, since the market visibility remains limited, we will not be providing earnings guidance," it added.

London-listed Severstal said its board hasn't recommended a first-quarter dividend and is unlikely to do so for the year as a whole, unless conditions improve.

"Although we have seen an increase in consumption from restocking in the first quarter, weak economic conditions continue to affect demand for our products," Alexei Mordashov, Severstal's chief executive, said in a statement.

Alexei Mordashov

Severstal posted a net loss of $644 million for the three months ended March 31, compared with a year-earlier net profit of $470 million.

Revenue slumped 36% to $2.8 billion from $4.36 billion as global steel demand ebbed amid tough economic conditions, pushing sales volumes and average prices for the metal lower.

Severstal, which is controlled by Mr. Mordashov, also recorded a $381 million pretax foreign-exchange loss as the central bank steered the Russian currency lower to offset capital flight and falling oil prices.

But in a climate of rising corporate defaults, Severstal said it has sufficient cash and committed facilities in place to meet this year's debt payments.

Russia is in the midst of its first recession in a decade.

For Chrysler, digital tools stretch scant ad dollars

By Emily Steel

ADVERTISING

With a meager advertising budget and a desperate need to increase sales, **Chrysler** is relying more heavily on new technologies to predict how ad purchases will translate into sales.

A team of statisticians, economists, software engineers and media planners at Chrysler's digital marketing agency, Organic, has designed a "media modeling" system that helps the company calculate the best ways to allocate its marketing dollars. The system calculates how much ad spending is needed to meet certain sales targets and then analyzes how both online and offline ads affect Web activity and, ultimately, sales.

Car makers and other companies have used forecasting tools for years, but digital ads have ramped up the systems' sophistication and accelerated reaction time to the information gathered.

"As a marketer, it helps me be smarter about the dollars I need to reach the sales goals we are responsible for," says Susan Thomson, Chrysler's director of media and events. "It gives you some science."

Chrysler, operating under bankruptcy amid a government bailout, proposed spending $134 million in advertising during the nine weeks it expected to be in bankruptcy court, but the U.S. Treasury's auto-industry task force said Chrysler can spend only half that amount. As it was, its total U.S. ad spending had fallen to $801.3 million in 2008, down 34% from $1.2 billion in 2007, according to WPP's ad tracking firm TNS Media Intelligence.

So Chrysler is deploying the new technology to calculate its ad budgets and tweak its marketing campaigns. A campaign to promote the recent launch of the new Dodge Ram truck illustrates how it works.

Nearly six months before the launch, a team at Organic started calculating how much Chrysler would need to spend on marketing to sell its target number of vehicles by figuring out how much Web traffic the company needed to generate. When the ad campaign went live, the system started calculating whether the commercials were generating enough Web visits. Certain Web activities have become a good barometer for car sales, says Jason Harper, group director of analytics at Organic. The agency estimates that about 70% to 80% of consumers research vehicle purchases on the Web, providing an indicator of whether visits translate to sales.

The TV spots, appearing during NFL football games and on the show "Sarah Connor Chronicles," among other places, didn't result in enough traffic to its Web site, so Chrysler made a couple of changes. One included tripling the amount of time that the URL appeared during the TV spot from two to six seconds. Chrysler also tweaked the homepage of its Ram Challenge Web site.

The agency says it noticed an uptick in traffic to the site.

When it started building the technology nearly five years ago, Organic, an **Omnicom** unit, was trying to figure out the impact of the auto maker's online ad dollars. As the model evolved, Organic started including broader sets of data, ranging from sales data related to advertising in traditional media like print and TV to economic factors that affect car sales, such as housing starts, fuel prices and unemployment rates.

Ad agencies long have used complex models to calculate the best ad spending mix, but the rise of digital media has revolutionized these systems. Instead of waiting weeks or months for data, marketers now can get them in real time, allowing them to adjust their ad spending or the creative elements of their campaigns on the fly.

"Instead of looking in the rear-view mirror, you have a heads-up display," says Greg Green, managing director at VivaKi, **Publicis Groupe**'s digital marketing unit.

In refining its model, Organic learned how certain ads, ranging from TV and print to radio and online, spur people to visit the Web. It then figured out which Web activities translate into actual auto sales. Some actions, such as scheduling a test drive online or entering a ZIP code to locate a dealer, are a good predictor of sales. Other actions, such as pricing a vehicle or playing with the colorizing features on the site, occur earlier in the buying process and aren't a direct indicator that consumers are interested in buying a vehicle.

The result was a system that predicted 2008 sales within one percentage point of actual sales figures for its Jeep brands, Chrysler says. Still, most of the focus is on planning ad dollars for specific marketing campaigns rather than on setting rigid guidelines for long-term spending, as in the coming upfront negotiations with TV networks.

Chrysler

Chrysler has been trying to use ad dollars to drive more traffic to its Web site. Above, a scene from one of the many videos on its Dodge Ram site.

CORPORATE NEWS

BofA urged to revamp its board

Government owns no stake but exerts unusual influence

BY DAN FITZPATRICK
AND DAMIAN PALETTA

U.S. officials have pressured **Bank of America** Corp. to revamp its board by bringing in directors with more banking experience, as regulators place the bank under increasingly heavy government scrutiny.

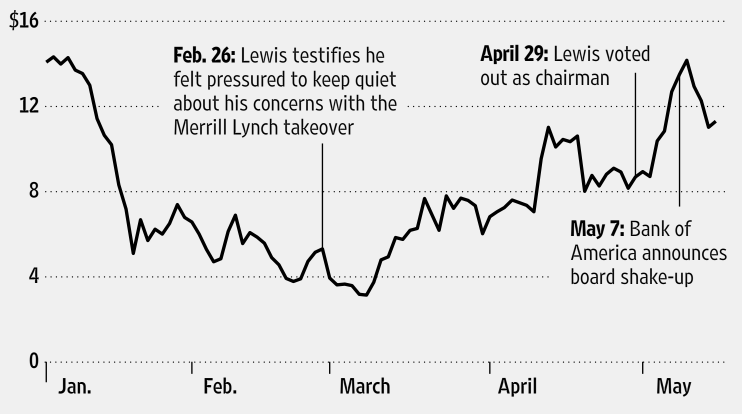
The move represents unusual influence by the federal government over the workings of a financial institution in which it doesn't own a stake. It's particularly significant because many of the bank's woes stem from its purchase of Merrill Lynch & Co.—an acquisition that was completed after heavy prodding by federal regulators. The Merrill deliberations were the beginning of regulators' deepening involvement in the Charlotte, N.C., lender's day-to-day operations.

The moves underscore the balancing act faced by the federal government as it tries to steer the banking sector through its crisis while also involved in a broader pattern of engagement in the operations of individual U.S. banks.

On May 7, a week after the Bank of America board named Walter Massey to replace Chief Executive Kenneth Lewis as chairman, Mr. Massey unveiled a committee to recommend changes to the board's structure and size. The committee would also oversee the bank's response to a federal "stress test" that showed the need for $33.9 billion in additional equity.

Prior to those moves, federal banking regulators—the Federal Reserve and the Office of the Comptroller of the Currency—had signaled to the bank's leadership that such steps would be well received by the government. Government officials also suggested that the task of reshuffling the board be led by independent directors, and that the board needed more members with banking experience.

Under pressure | Bank of America's daily share price



Source: WSJ Market Data Group (share price)

In another case, **Citigroup** Inc. recently named four financial experts to its board as part of a U.S.-directed overhaul of its directors. The changes followed months of pressure on new chairman Richard Parsons and an agreement that the U.S. would expand its stake in Citigroup to as much as 36%. Bank of America says it won't need to accept additional government investment as it adds to its capital buffer.

The Obama administration hasn't been shy about recommending leadership changes at several big bailout recipients. The government, in fact, is now playing a key role in a board shake-up at **General Motors** Corp.—another company the U.S. has aided but doesn't own a stake in—and at insurer **American International Group** Inc.

The U.S. has provided GM and AIG with a combined $188.7 billion in aid. It has provided $45 billion to Bank of America, taking preferred shares in return.

The changes to Bank of America's 18-member board and the expanded influence of its independent directors could also alter the calculus surrounding Mr. Lewis's tenure.

The CEO, who recently turned 62 years old, has told directors he would remain in the position at least until the crisis is over.

During a call with analysts, Mr. Lewis said the decision on how long he stays wasn't his. "I would like to see us at least start to be able to pay back the government money, if not do it all, and then regroup and decide how much energy I have left and how well prepared are we to make the transition."

The committee led by Mr. Massey, who is a retired president of Morehouse College, also includes former MBNA Corp. Executive Vice Chairman Frank Bramble; NSTAR CEO Thomas May; former Internal Revenue Service Commissioner Charles Rossotti; and former FleetBoston Financial Group CEO Charles Gifford, who served as chairman for several months in 2004 following Bank of America's acquisition of FleetBoston.

This group is expected to examine the strength of the team and the issue of CEO succession, said a person familiar with the situation. Bank of America executives Brian Moynihan, Barbara Desoer and Joe Price have all been cited internally as candidates. There are "several people inside the company that I think would be very good successors, all of whom will go unnamed," Mr. Lewis said during the analyst call. He said the list "could change" and other names "could pop up." Mr. Massey couldn't be reached for comment.

Within the bank, some see the request by federal regulators concerning the bank's board as part of the normal give-and-take between banks and regulators. Others view it as governmental interference in the board.

Bank of America spokesman Robert Stickler declined to comment on regulators' requests. But he said "every bank" that participated in the recent U.S. stress tests "was directed to review [its] board and management."Mr. Stickler also said that Mr. Lewis "got the shareholder message" and has acknowledged that the April 29 annual meeting, where shareholders stripped him of his chairmanship, was "humbling."

Separately, **Temasek Holdings** Ltd. sold its entire 3.8% stake in Bank of America as of March 31, according to a quarterly report filed with the U.S. Securities and Exchange Commission. A Temasek spokeswoman confirmed the Bank of America divestment, but didn't elaborate. The Singapore state investment company reported holding about 219.7 million Merrill Lynch shares in December. Those shares were later converted into Bank of America shares.

Panasonic sees more red ink in year ahead

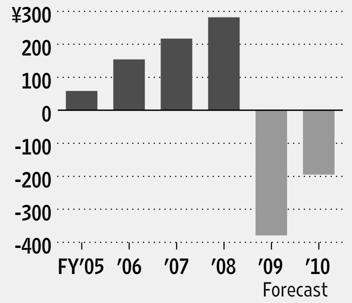
BY DAISUKE WAKABAYASHI

TOKYO—**Panasonic** Corp. reported a deep annual loss and warned it will spend the current year in the red as well, making it the latest Japanese electronics company to acknowledge there will be no quick recovery for an industry weighed down by relentless price cuts on televisions and other gadgets.

Panasonic's results came one day after rival **Sony** Corp. offered a bleak outlook of its own by forecasting a second straight year of losses and announcing further measures to cut costs and close plants. Other major Japanese conglomerates, including **Toshiba** Corp., have also signaled there are tough times ahead.

Panasonic couldn't escape the slowdown in spending on televisions and home appliances. The company was forced to drastically cut prices along with the rest of its peers when demand started to dry up in late 2008, leading to the worst quarter in Panasonic's history. In the three months ended March 31, Panasonic posted a net loss of 444.3 billion yen ($4.6 billion), as sales fell 30% from a year earlier to 1.54 trillion yen.

Panasonic
Net profit/loss, in billions of yen



Note: Fiscal years end March 31 of year shown
Source: the company

That left the company with a loss for the full year of 379 billion yen. Panasonic expects a net loss of 195 billion yen in the current year, with sales off 10%.

"We'd heard a lot about the possibility of bright spots here and there once we enter this new fiscal year, but now that we are running the business, I can say that a strong recovery is just not possible," Panasonic President Fumio Ohtsubo said at a news conference.

Panasonic is trying to replicate a turnaround it pulled off earlier this decade when it revived flagging earnings by reducing its work force, slashing inventory and closing factories.

The company has a goal of reducing its 230 global manufacturing sites by 20% by the end of March. About half of those closures will come in Japan, Panasonic said. All told, Panasonic expects to cut annual costs by 135 billion yen this year.

Panasonic aims to boost sales of flat-panel televisions by 54% this year to 15.5 million units. That's in contrast to Sony, which said last week it expects shipments of its liquid-crystal display TVs to remain mostly flat this fiscal year around 15 million units.

Panasonic agreed in December to buy **Sanyo Electric** Co., a leading maker of rechargeable batteries and solar panels, in a deal that values Sanyo at about $9 billion. Panasonic said it is waiting on regulatory clearance before launching a tender offer for Sanyo's shares.

H-P tries reviving PC sales with touch screens

BY JUSTIN SCHECK

Hewlett-Packard Co., seeking to revive the sagging desktop-computer business, has tried to woo consumers with sleek personal computers with glossy, touch-sensitive screens.

But the touch-screen PCs, which can cost twice as much as typical machines, have been slow to catch on. H-P sold only about 400,000 of its TouchSmart desktops last year, compared with 54 million traditional desktops and laptops, estimates research firm IDC.

So H-P is embarking on a new strategy to find commercial uses for the technology. Last month, H-P installed 50 touch-screen PCs in Chicago's O'Hare International Airport for travelers to access online maps and restaurant listings.

In Michigan, H-P's touch screens are being put into luxury boxes in the Detroit Pistons' arena, where basketball fans can use them to access player statistics and see instant replays.

The commercial touch-screen effort is key to generating growth, since companies will "buy 10 TouchSmarts at a time" and not just one like an individual would, said Phil McKinney, an H-P chief technology officer overseeing the touch-screen project.

H-P's PC business will be closely watched when the Palo Alto, Calif., giant reports quarterly earnings on Tuesday. Desktop sales, which accounted for 38% of the $8.8 billion in revenue for H-P's PC division in the quarter ended Jan. 31, have been hit hard by the recession and a consumer shift toward laptops.

Desktop prices have also been falling. While it has fared better than rivals, H-P sold 15% fewer desktops last quarter than the same period a year earlier, and desktop revenue was down 25%.

The deteriorating desktop PC market is a problem for H-P Chief Executive Mark Hurd, who revived the company's once money-losing PC division and helped H-P solidify its spot as the world's largest PC maker in terms of shipments.

Still, H-P's PC division saw its operating margin, a measure of profitability, shrink to 5% in the January-ended quarter, down from 5.8% a year earlier.

Touch screens can help H-P combat that profit decline, analysts say. The average consumer desktop, excluding machines from **Apple** Inc., sold for $531 in March, down 6.7% from a year earlier, according to NPD Group, which tracks retail sales. In contrast, H-P's cheapest TouchSmart model has a list price of $1,200.

Uniguest Inc., a Nashville-based company that provides PCs with Internet access to hotels, began in January installing TouchSmart PCs in about two-dozen hotels like the Nashville Airport Marriott.

"We're really pushing the new touch-screen technology," said Shawn Thomas, Uniguest's CEO. He said his company is paying between $1,200 and $1,600 per TouchSmart, but is in talks with H-P to place a large order and hopes to get a discount.

H-P isn't the only PC maker trying to boost falling desktop sales. **Dell** Inc. has introduced desktops in compact cases made of materials like bamboo and clear plastic, and earlier this year it also released a touch-screen desktop. Taiwan's **Asustek Computer** Inc. also entered the touch-screen market last year.

H-P is offering the assistance of hardware and software consultants from its services division to help customers come up with new uses for touch technology.

The strategy pits H-P against rivals like **International Business Machines** Corp., which has long sold touch-screen computers to do things like print out airline boarding passes. IBM is also putting public computer kiosks into restaurants and retail stores.

Norma Wolcott, vice president of IBM's kiosk business, said IBM has tailored its touch screens, software and services for business use, arguing H-P's TouchSmart is more suited to consumers.

"It's what you want in your kitchen" and not in a high-traffic place like an airport, she said of the TouchSmart.

Bob Ducey, an H-P executive who is leading the TouchSmart's commercial marketing, said competitors like IBM are selling computers that do a single task—such as printing out movie tickets—rather than access a range of information over the Web. In contrast, Mr. Ducey said, the TouchSmart can be used to access information much like a home PC.

At the Palace in Auburn Hills arena near Detroit, a small company called Konsyerzh LLC plans to install 35 new TouchSmart machines by June.

Gregory Nasto, the company's CEO, said Konsyerzh has developed programs that let fans access instant replays and order food and merchandise.

Mr. Nasto said he could end up spending up to $1,200 per machine but he's trying to negotiate additional discounts. He expects touch-screen PC prices to drop further in the next year as more competitors enter the field.

Recently, he said, Dell salespeople made a pitch for him to buy a competing touch-screen PC.

CORPORATE NEWS

Reuters

The French government said Luc Vigneron will succeed current Thales Chairman and CEO Denis Ranque, shown above at a Paris news conference in January.

Vigneron clinches move to head France's Thales

By Geraldine Amiel

PARIS—Luc Vigneron will be the new chairman and chief executive of French defense electronics group **Thales** SA, after the government Friday made official its support for Mr. Vigneron, though the official appointment may have to wait until the company's annual meeting.

The French prime minister's office said that the government's support for Mr. Vigneron to succeed current Thales Chairman and CEO Denis Ranque has been agreed with Thales' other main shareholders, **Alcatel-Lucent** SA and **Dassault Aviation** SA.

Mr. Vigneron's candidacy will be submitted to the company after its annual meeting Tuesday, the prime minister's office said. Mr. Vigneron is currently CEO of French state-controlled tank builder Nexter.

The French state, which directly and indirectly owns 27% of Thales but around 38% of the voting rights "is confident in Mr. Vigneron's ability...to pursue the Thales group's development with a new governance," the office added.

The move comes after months of uncertainty regarding the Thales helm and as the government has publicly embarked upon reforming France's defense industry. No one at Thales was immediately available for comment.

The annual shareholder meeting "will be quite interesting in that respect, as it is not obvious the succession can take place before this date," Cheuvreux analyst Antoine Boivin-Champeaux said.

For months, Dassault Aviation has been publicly supporting former Thales executive, Francois Quentin, who had been ousted from his position by Mr. Ranque.

In December, Dassault Aviation signed an agreement with Alcatel-Lucent to buy out the telecom equipment company's roughly 20% stake in Thales. The French state and Alcatel-Lucent are bound by a shareholder's pact. Dassault Aviation currently owns about 5% of Thales through its parent holding Groupe Industriel Marcel Dassault.

After the transaction, the public sector and Dassault Aviation are to hold a joint 53% capital stake and 61% of the voting rights in Thales. But the deal hasn't been finalized yet.

Railroad aims to be ready

Union Pacific keeps some furloughed staff at hand for rebound

By Alex Roth

The rail-shipping business is off by double-digit percentages, but railroad giant **Union Pacific** Corp. doesn't want to worry about meeting demand if and when it rebounds.

For that reason, almost a third of Union Pacific's 5,000 furloughed workers are operating on a retainer, with full benefits and partial wages, even though it is costing the company $50 million a year.

James R. Young, Union Pacific's chief executive, said the company is determined to avoid a repeat of a 2004 fiasco, when it was caught unprepared for a sharp upturn in business. The U.S. had gradually emerged from the recession that followed the dot-com bust and the 2001 terror attacks. Then suddenly in 2004, the company's shipping volumes jumped roughly 10% to 12% in a six-month period. Union Pacific wasn't ready and the result was a network meltdown, with rolling bottlenecks and delays with disastrous repercussions for its thousands of customers.

"We just flat-out cut too far" in the years preceding the 2003 and 2004 recovery, said Mr. Young, who was named CEO of the Omaha, Neb., company in 2005.

To make sure it has adequate staffing should the economy recover quickly this time around, Union Pacific is paying full health benefits for 1,600 of its roughly 5,000 furloughed employees. These 1,600 employees, many of them train conductors, also work eight days a month so they can remain current on their training and qualifications. Mr. Young estimates that calling one of these employees back to work will take fewer than 30 days, compared with 60 to 90 days for other furloughed workers.

"This thing could snap back pretty quickly, and in our business we don't have the luxury of telling a customer 'No,' " Mr. Young said.

All big U.S. railroads face a complicated calculus now: how to cut expenses as freight volumes fall without leaving themselves unable to respond quickly as the economy rebounds. Union Pacific's approach represents a compromise of sorts. While it is furloughing a larger percentage of workers than its largest competitor, **Burlington Northern** Corp., it is also investing millions to make sure these sidelined employees can return to work as quickly as possible.

Railroads are expected to experience a jump in volumes several months before a broader economic recovery. Getting caught unprepared could cost them business and could hamper a larger economic rebound by snarling the movement of the goods that railroads transport. More than 40% of freight in the U.S. moves by rail.

Until December, rival Burlington Northern had a similar furlough policy to Union Pacific's. A certain percentage of furloughed workers kept their benefits and were paid a "modest monthly income," spokesman Patrick Hiatte said. But the Fort Worth, Texas, company discontinued the practice "when it became clear to us that the recession was getting worse" and that costs needed to be cut, Mr. Hiatte said.

Now, furloughed workers at Burlington Northern, like the other big railroads, **CSX** Corp. and **Norfolk Southern** Corp. , lose their benefits after several months.

Burlington, which has a current work force of 38,000, has furloughed roughly 7.8% of its employees, compared with more than 10% for Union Pacific, which employs 45,000.

James Stem, national legislative director for the United Transportation Union, which represents 55,000 conductors working on the North American railroads, praised Union Pacific's approach and predicted the other railroads would spend more money in the long run on hiring and retraining.

Norfolk Southern, the nation's fourth-largest railroad by revenue, says that rather than mimic Union Pacific's furlough policy, it has chosen to minimize the number of furloughs. The company has furloughed only 1,200 from its 30,000 work force, compared with 2,300 for CSX, the nation's third-largest railroad and Norfolk Southern's main competitor in the eastern half of the U.S.

Union Pacific's furlough program comes at a time when the railroad has been making what some customers and analysts say are noticeable gains in its performance in recent years.

The company's reputation was in need of burnishing. Aside from the problems of 2004, many customers still remember 1997 and 1998, when Union Pacific's merger with Southern Pacific Rail Corp. caused widespread service problems and paralyzed ports on the West Coast.

Rick Paterson, a UBS analyst, said Union Pacific's average train speed, considered a good measure of performance, has increased 22% during the past year. Only some of this improvement is a function of lower volumes, which result in less-congested tracks, Mr. Paterson said.

By comparison, Burlington Northern's average train speed has improved only 11% in the past year, Mr. Paterson said.

The true measure of the company's progress, Mr. Young says, will come when the economy improves, adding that Union Pacific simply can't afford another poor performance. "Customers have a long memory," he said.

Chinalco and Rio Tinto gain U.S. clearance for deal

By Robert Guy Matthews And Dana Cimilluca

Rio Tinto and **Aluminum Corp. of China** obtained clearance from the Committee on Foreign Investment in the U.S. to link up in a deal that would give the Chinese company an 18% stake in the miner. But the transaction still faces some opposition.

Rio Tinto shares rose Friday as the miner reaffirmed its commitment to the alliance with the Chinese company, also known as Chinalco, and played down the possibility of a rights issue to raise capital.

Earlier this year, the Anglo-Australian miner was backed into a corner by heavy debt, frozen credit markets and tumbling commodity prices. The proposed sale to state-owned Chinalco of assets and bonds that convert into stock offered management a way out.

Three months later, Rio remains under pressure, and the deal has raised concerns among some investors and politicians. Some analysts say they are sensing less enthusiasm for the deal from Rio.

Rio says it remains fully committed. New Chairman Jan du Plessis has been talking to analysts and investors in the U.K. in an attempt to shore up support for the $19.5 billion Chinalco deal.

Mr. du Plessis has said he won't present a deal that shareholders aren't likely to bless, which may lead to revisions, including possibly opening up the convertible-bond portion to other investors or scrapping it.

Some Rio investors in the U.K. have criticized the Chinalco deal, arguing that it violates their right to participate in any share sales. The appreciation of Rio shares has also made the convertible-bond portion of the deal appear increasingly sweet for the Chinese.

But given the 35% rally in Rio shares since the Chinalco deal was announced in early February, investors could lose out if the company were to launch a rights issue, which would likely be priced at a deep discount to the current price.

—Jeffrey Sparshott contributed to this article.

CORPORATE NEWS

Abercrombie rethinks prices

Charging a premium backfires as retailer loses sales, posts loss

By Nicholas Casey

Teen retailer **Abercrombie & Fitch** Co. reported a larger than expected fiscal-first-quarter loss Friday and said it would lower prices to boost sales, an about-face from its previous strategy of keeping prices high through the recession.

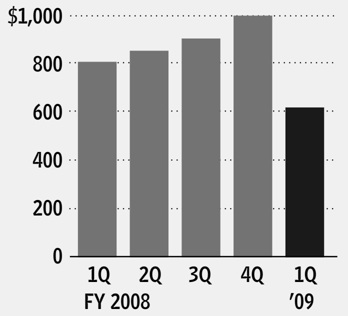
The New Albany, Ohio, retailer reported a 24% decline in revenue for the quarter ended May 2, while sales at stores open for more than a year, a key measure of retail health, fell a sharper 30%.

It also disclosed a "strategic review" of Ruehl No. 925, a chain of 29 stores that Abercrombie introduced in 2004 to capture more of the adult market. While it didn't say how long it would take to do the review, the company said it could result in a charge of about $55 million.

As late as last year, Chief Executive Mike Jeffries vowed he wouldn't lower prices, despite sharp declines in consumer spending and moves by competitors including **American Eagle Outfitters** Inc. and **Aeropostale** Inc. to slash their price tags.

Sales slump

Abercrombie & Fitch's delayed discounts hit sales, in millions



Note: Fiscal year ended Jan. 31
Source: the company

On Friday, Mr. Jeffries said "meaningful reductions" in price were now required in light of "a headwind where the consumer is reluctant to spend on premium brands." He declined to specify the size of planned price cuts but said they would be concentrated on its Southern California-themed Hollister brand and children's store Abercrombie Kids.

For the first quarter, Abercrombie reported a loss of $26.8 million, or 31 cents a share. Sales fell 24% to $612.1 million. In the year-earlier quarter, it posted a profit of $62.1 million on sales of $800.2 million.

It is unclear whether the new pricing will be aggressive enough to win back customers, said Amy Noblin, a retail analyst at brokerage Pali Capital. Shoppers have deserted the chain for other teen retailers that have slashed prices more deeply. Abercrombie had argued that while significant price cutting would boost sales it would destroy its high-end image and the company's pricing power.

But as inventories piled up, it began drawing customer's attention to deals in mid-March with signs toward the middle and front of many stores. "They've taken more second and third markdowns, and it's clearly reflective of the environment," said Ms. Noblin.

The move, along with Easter demand, helped revenue during April, when Abercrombie's sales at stores open at least a year fell 22%, less than the March decline. The downside: Abercrombie's gross margin, a measure of profitability, narrowed by 3.5 percentage points to 63.3% during the first quarter.

Though selling basic clothes like khakis and button-down shirts, the company has long commanded some of the industry's highest markups through branding initiatives and racy advertising, and its margins had remained well above 60%.

Microsoft to add sites in China

By Aaron Back

BEIJING—In a new tack against piracy, **Microsoft** Corp. will make a series of investments in the Chinese city of Hangzhou, which has promised to clamp down on illegitimate software.

Microsoft will build two new technology centers and make other investments in the wealthy city on China's east coast, with the aim to establish a model city where intellectual-property rights have greater protections than elsewhere in China.

"We wanted to find a showcase," said Simon Leung, Microsoft's chief executive for Greater China. "The city had to be committed to doing the right thing."

Technology companies around the world have tried various measures to stop the drain on their revenue that piracy represents. The move marks a new approach for Microsoft, which in the past has mainly prodded the central government to step up enforcement actions.

In October, Microsoft started sending out software updates that turned users' computer wallpapers black if they had a pirated Windows operating system, a move that sparked anger among some Chinese users.

In January, a Chinese court convicted 11 people of manufacturing and distributing counterfeit Microsoft software, in a case hailed by the company as a milestone.

With several Chinese cities competing to become high-tech hubs, Microsoft is hoping that more can be prompted to follow Hangzhou's lead. Last month, the western city of Chongqing also declared it will "robustly protect international [intellectual-property rights] throughout China for those companies which decide to locate in the city."

Mr. Leung declined to say how much Microsoft's total investment in Hangzhou will be under the agreement but said that the program is above and beyond the $1 billion over three years that Microsoft said last November that it plans to spend on research and development in China.

In Hangzhou, Microsoft will establish a center aimed at developing new applications and business models for "cloud computing," a term that refers to the growing trend of storing and accessing data and applications on remote servers.

It will also launch a second technology center in the city that will work with local companies to put their systems on Microsoft platforms, and it will expand an existing technology center operated in conjunction with the Hangzhou government.

As part of the program, Microsoft plans to offer heavily discounted software to start-up companies in Hangzhou and provide technology and training to a local university.

In return, Hangzhou has set targets for enforcement of intellectual-property rights, including ridding shops of pirated software and encouraging local enterprises to use legitimate programs.

Alec Cooper, general manager of Microsoft's "Genuine Software Initiative" in Greater China, said that piracy fears are among the top concerns for technology companies when they consider investments in China, so it is in Hangzhou's interests to stand out as a strong enforcer.

Hangzhou is attempting to position itself as a hub for high-tech industries such as software outsourcing. It is the headquarters to **Alibaba Group**, one of China's largest Internet companies, with operations in search, online retailing and the business-to-business transaction platform Alibaba.com Ltd.

"Hangzhou can't change the piracy rate for China, but what they can do is differentiate Hangzhou from the rest of China in a very profound way," Mr. Cooper said.

A recent study by research firm IDC estimates that 80% of software installations in China last year were done without proper authorization, down from 90% in 2004, thanks to measures such as a requirement that computer makers sell PCs with legitimate software pre-installed.

"I'm encouraged by the trend, but by working with local governments and the central government, we can do better," said Mr. Leung.

China has increasingly signaled an intention to get serious on enforcement of intellectual-property rights, but antipiracy measures handed down from Beijing often take time to be enforced at the local level.

"What we can do is work aggressively with different cities to accelerate the adoption of those things," said Mr. Cooper.

Hangzhou is the capital of eastern Zhejiang province, home to many small, export-oriented companies.

GLOBAL BUSINESS BRIEFS

Hennes & Mauritz AB

Same-store sales increase for first time since July

Fashion retailer **Hennes & Mauritz** AB said Friday that sales in stores open at least a year rose last month for the first time since July. Same-store sales were up 8% in April, said H&M—the world's third-largest fashion chain by revenue behind U.S.-based **Gap** Inc. and Spain's **Inditex** SA, which vie for the No. 1 spot. The increase may be a sign the low-cost retailer is recovering from the global trend of consumers reining in spending. H&M's total sales rose 19%. Analysts expected sales to be strong, mainly because the weather was nicer this April than a year earlier, encouraging customers to buy spring clothes. Also, in Germany apparel sales rose 13% last month, according to industry journal Textilwirtschaft.

Belgacom SA

Belgacom SA's first-quarter net profit fell 10% on higher costs from two acquisitions. However, the Belgian telecom company stuck to its forecast for 2009, saying sales to residential customers were holding up well amid the economic downturn, even though sales to business customers have suffered. Net profit fell to €212 million ($289.1 million) in the three months ended March 31 from €236 million a year earlier. Sales rose 1.4% to €1.49 billion. Operating expenses rose 5.1% to €1 billion, mainly because of costs related to telecommunications companies Scarlet and Tango, which Belgacom bought last year. Cuts in mobile termination rates, or fees charged when transferring calls from one telecommunications operator to another, also weighed on the results.

AngloGold Ashanti Ltd.

AngloGold Ashanti Ltd., one of the world's biggest gold producers, Friday said it swung to its first profit in seven quarters as it cut its exposure to forward sales contracts to benefit from a buoyant bullion price. AngloGold posted a net profit of one million rand ($120,300) for the three months ended March 31, compared with a year-earlier net loss of 3.81 billion rand. Revenue was virtually unchanged at 6.82 billion rand. "This was a milestone quarter in terms of earnings leverage to the gold price," said Chief Executive Mark Cutifani, adding that the Johannesburg-based company will continue to cut its hedge-book exposure and is targeting exploration to boost reserves. Mr. Cutifani has focused on ridding the company of commitments to sell at fixed prices well below recent average spot prices.

Bharti Airtel Ltd.

Bharti Airtel Ltd. said it hopes to double its number of customers to 200 million within three years, adding that any acquisition would help it reach the target even faster. Bharti, India's largest mobile-phone operator by subscribers, said Friday its total subscriber base had crossed 100 million, doubling since October 2007. The company is adding close to three million mobile customers a month. India has more than 10 players offering mobile-phone services and several more are waiting to start operations. Analysts say there is space for only about five operators in India—the world's fastest growing mobile-phone market, adding more than 10 million users a month. "There will be consolidation in India," Chairman Sunil

Arcandor AG

Squeezed by tight lending conditions, German retail and travel company **Arcandor** AG said Friday it aims to apply for state-backed guarantees by the end of this week to meet its immediate refinancing needs. Arcandor said it will submit an application for state-backed financial guarantees of €650 million ($886 million). Furthermore, Arcandor said it will apply for a loan from the government-owned KfW bank. The company has to refinance €650 million by June, while a further €300 million in loans will come due in September. Arcandor posted a loss of €745.7 million for fiscal 2008. For now, it is pinning its hopes on the German government's special fund containing €115 billion to provide guarantees and direct loans to companies struggling with choked credit conditions. "We don't want any gifts, nor do we want the state to become a shareholder of Arcandor or to receive any special financial injections," said Chief Executive Karl-Gerhard Eick. The company only wants state assistance to temporarily compensate for dysfunctional financial markets, he said.

Toshiba Corp.

Toshiba Corp. said it was taking legal action against **Imation** Corp. and several recordable DVD manufacturers and distributors, claiming they are infringing on its patents. In a lawsuit filed in the U.S. Friday, Toshiba named eight firms in the U.S., India and Taiwan for allegedly infringing its DVD patents. The Japanese firm is seeking monetary damages and an injunction to prohibit production, sale and import of recordable DVD media by those companies in the U.S. Imation said it hadn't been notified of the lawsuit.

Sony Corp.

Sony Corp. hired an executive from **International Business Machines** Corp. to lead the Japanese electronics maker's shift to create new networked gadgets that link to Web services and content. George Bailey will take the new position of chief transformation officer on June 1. Mr. Bailey will lead the recently formed transformation management office to support Sony's consumer-products and -devices group.

Temasek Holdings Ptd.

Temasek Holdings Pte. Ltd. sold its 3.8% stake in Bank of America Corp. in the first quarter, swelling the Singapore company's losses from soured investments by about $4.6 billion. Temasek, a state-owned investment company, disclosed the sale in a quarterly report with the U.S. Securities and Exchange Commission. Temasek sold the Bank of America shares for an average price of $7 a share, taking in $1.3 billion, people familiar with the situation said. A Temasek spokeswoman confirmed the sale but didn't provide other details. Temasek has made high-profile investments in the past two years, including in Merrill Lynch and in Barclays PLC, in which it increased its stake last June to a little over 2%, paying about $399 million. When Bank of America acquired Merrill in January, the stake was converted into 189 million Bank of America shares.

—Compiled from staff and wire service reports.

ECONOMY & POLITICS

Iraqis pursue corruption in government

After flurry of arrests, combative trade minister appears for televised testimony; 'a duty to listen to the people'

By Gina Chon

BAGHDAD—Iraqi lawmakers are seeking the removal of a government minister after he was publicly grilled over allegations of malfeasance on his watch, in the latest pre-election effort to fight corruption.

Trade Minister Abdul Falah al-Sudani was defiant and at times insulted lawmakers during the questioning on Saturday and Sunday, some of which was shown in a delayed broadcast on Iraqi television. It was a rare chance to see a top official on the hot seat in what is seen by some Iraqis as an effort by some leaders to gain public support ahead of national elections, scheduled for the end of this year.

The allegations against Mr. Sudani, who denied the charges against him, are mainly related to the food rations program run by the Trade Ministry. He has accused a former general inspector at the ministry of being corrupt. Mr. Sudani's appearance in parliament comes after the May 7 arrest of one of his brothers, who is an aide to the minister, a week after a gunfight broke out at the ministry when authorities arrived at the building to arrest nine officials on corruption charges.

The trade minister's brother, Sabah Mohammed al-Sudani, has been charged with embezzlement in relation to food imports for the food rations program. He is still in custody and couldn't be reached to comment. A relative said he denies the charges, and the family is putting together a team of lawyers.

Associated Press

Prime Minister Nouri al-Maliki, at center in a ceremony Friday for a new bridge east of Karbala, has renewed a campaign against government corruption in Iraq, a country Transparency International listed last year as the world's third-most corrupt.

This is the first time serious actions have been taken against top officials at the Trade Ministry, despite a history of allegations of corruption . Prime Minister Nouri al-Maliki stated in 2008 that that fighting corruption would be a priority, but extortion, bribes and nepotism, among other concerns, have continued largely uninhibited. Corruption watchdog Transparency International listed Iraq as the world's third-most corrupt country in 2008.

Still, after many incumbents were voted out of office in provincial elections held in January, politicians are taking new steps to prepare for national elections set to take place at the end of December. Public outrage against corruption has been growing, making battling malfeasance a key election issue.

Many Iraqis said they doubted the government would make progress fighting corruption. "Many corrupt officials are connected to the big ruling parties, which have common interests with Maliki and the parliament," said Asa'ad Mahmood, a 35-year-old Baghdad shop owner.

In a recent speech, Mr. Maliki said Iraq needed to fight corruption with the same intensity that it battled insurgents and militias. His push includes the removal of obstacles to prosecuting corruption cases, such as a regulation that requires a minister's approval before a case involving his ministry can be referred to the courts.

A spokesman for Mr. Maliki said politics weren't the motivation for the stepped-up corruption fight. Instead, the spokesman said, the improving security situation was allowing the government to tackle other challenges.

In the near future, parliament's Integrity Committee, which has summoned Mr. Sudani, also plans to call top officials from the Electricity Ministry, the Oil Ministry and the national elections commission.

Sheikh Sabah al-Saedi, chairman of the Integrity Committee and one of the body's most vocal anticorruption voices, denied politics are playing a role in the timing of the parliament's actions.

He said the newly elected head of the parliament, Ayad al-Sammaraie, has encouraged lawmakers to feel free to tackle corruption and other challenges facing the government, without having to obtain permission from political bloc leaders.

"People have realized what a big problem corruption is and how it drains government resources," Mr. Saedi said. "So we have a duty to listen to the people."

—Munaf Mustafa contributed to this article.

Iraq deal furthers plan for natural-gas pipeline to Europe

By Guy Chazan

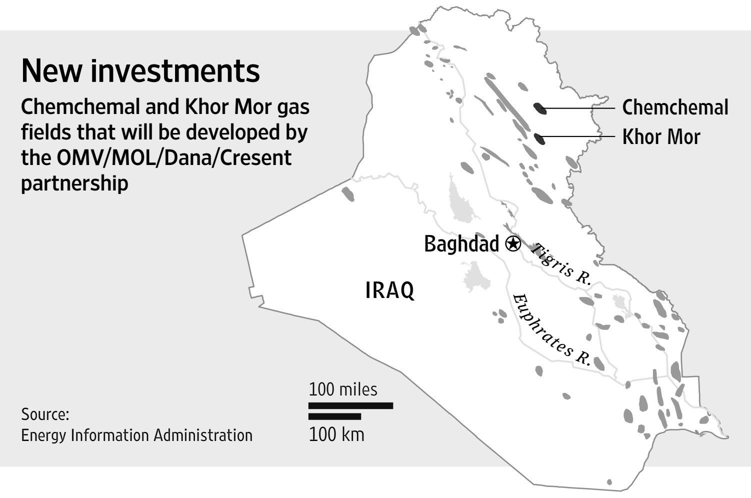
Two big European oil and gas firms said they would invest up to $8 billion in an energy project in the northern Iraqi region of Kurdistan, in a push to make the country a major exporter of natural gas to Europe.

The announcement by **OMV** AG of Austria and Hungary's **MOL** Nyrt. could give a big boost to the troubled Nabucco pipeline project to bring natural gas from Central Asia and the Middle East to Europe, and lessen the continent's reliance on gas imports from Russia.

"This could really kickstart Nabucco," said Badr Jafar, executive director of **Crescent Petroleum**, one of OMV and MOL's two partners in the Kurdistan gas project. "The main problem was finding a secure, viable, long-term gas supply for the pipeline. That was the rationale for this partnership."

On Friday, Russian and Italian energy companies agreed to double the capacity of a new gas pipeline from Russia into the heart of Europe that will bypass Ukraine—a project widely seen as a rival to Nabucco.

The Kurdistan deal reflects the desire of energy companies large and small to gain access to Iraq's untapped reserves of low-cost oil and gas. **Royal Dutch Shell** PLC and **Exxon Mobil** Corp. are among a clutch of oil majors expected to bid for oil service contracts in Iraq next month—the first such licensing round since the end of the U.S.-led war that began in 2003. With Iraq facing a big budget deficit and oil prices that have slumped since hitting highs of $145 a barrel last summer, Iraq is eager to bring in foreign oil companies to boost production.



While oil is the biggest draw—Iraq sits on the world's third-largest crude reserves after Saudi Arabia and Iran—the country's gas resources have also aroused interest. In September, Shell announced a multibillion-dollar joint venture with the Iraqi government to gather, process and market natural gas in the oil-rich southern province of Basra. The fuel is currently being flared because of a lack of adequate infrastructure.

OMV and MOL already have a presence in Kurdistan, where they are among a number of smaller oil companies that have signed production-sharing agreements with the Kurdistan Regional Government. Those companies got a boost earlier this month when the KRG gave them the go-ahead to export the oil they produce in the region by pipeline to Turkey. Larger companies such as **BP** PLC and Shell have avoided investing in Kurdistan, for fear of antagonizing the central government in Baghdad, which has denounced the Kurdistan Regional Government's deals as illegal.

Mr. Jafar said the partners didn't envisage any problems with Baghdad, saying they were "absolutely convinced of the legal, moral and technical correctness of our investments in northern Iraq."

Under the deal signed Sunday, OMV and MOL will form a partnership with **Dana Gas** PJSC and Crescent Petroleum, both of which are based in the United Arab Emirates. They will each acquire a 10% stake in Pearl Petroleum, a holding company for Dana and Crescent's assets in Kurdistan. OMV will pay $350 million for its stake, and Crescent and Dana Gas will each take a 3% stake in MOL.

Dana and Crescent have already invested more than $600 million over the last two years in developing the Khor Mor gas field in Kurdistan and building pipelines to carry gas to nearby power plants. According to the agreement, the partners would invest up to $8 billion over the next seven years to develop the Kurdistan assets and build an export pipeline. Gas not consumed domestically would be exported to neighbors, including Turkey, and beyond into Europe.

Mr. Jafar said Khor Mor currently produces about 90 million cubic feet a day, but it and the partnership's other field, Chemchemal, could ultimately produce 3 billion cubic feet of gas a day by 2014. He said the partners anticipated local, Iraqi demand not exceeding 500 million cubic feet a day, and demand from Turkey of about 1 billion cubic feet a day. "That means 1.5 billion cubic feet a day for Nabucco," he said.

Japan, China and Hong Kong confirm new flu cases

Associated Press

TOKYO—Japanese health officials in waves of announcements Sunday confirmed dozens of new cases of swine flu as the government shut down schools and canceled community activities in affected cities.

The country now has at least 78 confirmed cases, most of them teenagers. China and Hong Kong confirmed new cases as well.

In Japan, health officials confirmed about 70 domestic swine-flu patients over the weekend, most of them high-school students in the western prefectures of Osaka and Hyogo. All tested positive for the H1N1 virus and were recovering in local hospitals or their homes, officials said.

Japan's first cases were believed to have been contracted outside the country. The students didn't travel overseas recently but tested positive for the same strain that has killed more than 70 people world-wide.

Hong Kong on Sunday confirmed its third case of swine flu, in a 23-year-old mainland Chinese student who flew to Hong Kong from New York.

In China, the Health Ministry said an 18-year-old student in Beijing who recently returned from a U.S. university has swine flu, the mainland's third confirmed case.

Women gain in Kuwait vote

Four females to join parliament in a first; Islamists lose ground

By Maria Abi-Habib

KUWAIT CITY—Kuwait elected a more progressive parliament Sunday, including its first female lawmakers, while Islamists lost ground.

Analysts said the nation's rulers must now match the vote with a cabinet focused on change in order to help revive the economy of the Persian Gulf state, which is home to the world's fifth-largest oil reserves.

"We need a clear position and road map," Kamel Harami, an independent oil analyst and former executive at Kuwait Petroleum Corp., told Zawya Dow Jones. "Parliament will support a five-year program as long as there's a vision."

Associated Press

Dr. Asil Al Awadi, among the first group of women elected to Kuwaiti parliament, celebrates her victory at her campaign headquarters in Kuwait City on Sunday.

The vote delivered four new female members to parliament. Preliminary results Sunday showed university instructor Aseel al-Awadhi and economist Rola Dashti were among the four women to win seats. Kuwaiti women were given the right to run for office and vote in 2005.

Attention will now turn to the shape of the new government and the appointment by the emir, Sheikh Sabah al-Ahmad Al-Sabah, of government ministers, who will put forth an economic plan to turn around the nation's flagging economy. Merrill Lynch expects Kuwait's gross domestic product to contract by 1.8% this year.

A five-year economic-overhaul program is expected to be presented to the new parliament when it opens in weeks. The plan must diversify the country away from oil, while at the same time provide money to boost the industry and lure foreign companies to help increase output, Mr. Harami said.

The government also must inject funds into badly needed infrastructure improvements to help stimulate Kuwait's economy and allow it to catch up with its more diversified neighbors in the Gulf, such as the United Arab Emirates and Qatar.

Legislation to create a stock market regulator is also needed, economists say. Kuwait's bourse, once the envy of many Gulf countries, has seen heavy losses this year. A new foreign investment law is being called for to help the country compete better in the region. Foreign companies in Kuwait face a 15% tax, which makes the state less competitive, economist argue.

The new parliament will be the second this year. The emir dissolved the 50-member National Assembly in March, complaining that lawmakers, especially Islamists, were holding back Kuwait's economic progress by clashing with the cabinet.

Islamist lawmakers resisted Project Kuwait, an ambitious plan to invite foreign companies to helpdevelop Kuwait's northern oil fields. They also opposed a vital economic rescue package to kickstart lending in Kuwait's frozen credit markets.

Liberal politicians warned that if the government doesn't have a progressive plan to move the country forward, there could be another standoff.

"We need to elect a parliament that wants to move forward to send a message to the emir to request a good, capable government so we can work together to move forward," said Ms. Dashti ahead of the vote. The emir chooses the prime minister, who then nominates the cabinet.

Pakistan district scarred by battle

By Zahid Hussain

BUNER DISTRICT, Pakistan—The Pakistani army says it is making progress against the Taliban in this district 110 kilometers from Islamabad, but the fighting has left devastation in its wake.

Burned vehicles, spent artillery shells and broken electric poles lay strewn along the dusty main road in Ambela, the small mountain town that became the main battleground when Pakistani troops moved in to Buner to oust the Taliban.

Troops have succeeded in pushing the militants from the town after fierce fighting that began after the Taliban occupied the district in what the government said was a violation of a peace agreement in neighboring Swat Valley.

Associated Press

Pakistanis displaced from the Swat Valley line up for food at a refugee camp Sunday. The continuation of fighting gave refugees little hope of going home soon.

A few young men chatted inside an Ambela tea shop, which was opened briefly on Sunday during a day-long break in the army-imposed curfew, near houses riddled with bullets and artillery shells.

Arsalan Khan, who fled the fighting along with thousands of other villagers some three weeks ago, has settled with his family in a refugee camp in Mardan, a provincial town. He returned to Ambela Sunday to see if his house was still standing: It was damaged, and the factory where he worked has closed. He said there was nothing in the village to bring his family back to. "I don't have any work and can't move because of the curfew," he said.

Most of Ambela's entire population of 10,000 fled. A few families returned after the security forces relaxed curfew restrictions to allow farmers to harvest their wheat crop. But most didn't return, leaving most of the crop to go to waste.

They have joined another one million refugees fleeing from Swat and other battle zones in northern Pakistan, triggering one of the worst humanitarian crises in the country's 62 years history.

Pakistan rushed some 5,000 army and paramilitary troops to Buner after the Taliban advanced from neighboring Swat. Pakistani military officials said scores of militants have been killed in the combat. But hundreds of militants were still entrenched in the Sultanwas and Pir Baba areas, just several kilometers from Daggar, Buner's main town and administrative headquarters.

Yahaya Akhunzada, Buner's top civil administrator, said the situation was still too tense for people to return to their homes. "We can only ask the people to return when the entire area is cleared," he said.

U.S. contractors fired at civilian car in Kabul

By August Cole

Four U.S. contractors affiliated with the company formerly known as Blackwater Worldwide fired on an approaching civilian vehicle in Kabul this month, wounding at least two Afghan civilians, according to the company and the U.S. military.

The off-duty contractors were involved in a car accident around 9 p.m. on May 5 and then fired on the vehicle, which they believed to be a threat, according to the U.S. military. At least some of the men, who were former military personnel, had been allegedly drinking alcohol that evening, according to a person familiar with the incident. Off-duty contractors aren't supposed to carry weapons or drink alcohol.

The incident occurred at a delicate time for the U.S., which faces rising outrage from Afghan leaders over civilian casualties from U.S. airstrikes. For **Xe**, which is the name Blackwater chose this year to distance itself from its controversial security work in Iraq, the shooting comes as the Obama administration and Defense Secretary Robert Gates reconsider the role of military contractors, a practice that boomed during the Bush years.

The contractors were trainers hired by Paravant LLC, a subsidiary of Xe. Paravant has terminated contracts with the four men "for failure to comply with the terms of their contract," according to Xe spokeswoman Anne Tyrrell. "Contractual and or legal violations will not be tolerated," she said.

The contractors were ordered not to leave Afghanistan without permission of the Defense Department, she said, and the company said it is cooperating with authorities.

The U.S. military is investigating the incident, according to a May 7 news release that didn't name the company involved. The statement also said two Afghans received hospital treatment for their wounds.

Afghanistan's ambassador to the U.S., Said Jawad, said he is still waiting to learn the details from his Interior Ministry. "Blackwater has reached out to us and offered compensation to the families of the victims," he said.

Paravant was set up to subcontract to **Raytheon** Co. on a large U.S. Army training contract, according to a person familiar with the situation. Raytheon referred questions to U.S. Central Command, which runs the military effort in Afghanistan.

Large defense contractors typically rely heavily on specialized subcontractors when operating in hot spots such as Afghanistan and Iraq. Raytheon's use of Paravant is for a program called Warfighter Focus, a U.S. Army training effort valued at more than $11 billion over a 10-year period.

The incident comes at a transition point after Blackwater changed its name in February and Blackwater founder Erik Prince announced in March he was stepping back from day-to-day operations after bringing in new senior executives. The company, which has had problems with weapons-export paperwork, also moved to shore up its operations after a meteoric expansion from a small training outfit founded in 1997 to the biggest U.S. private security company.

"While this kind of change does not happen overnight, we are confident that we have the right team in place to provide the best possible services to our customers," said Ms. Tyrrell.

Xe is now winding down its guard work in Iraq as the government there is effectively forcing them out after a 2007 shooting incident involving one of its State Department security teams left 17 Iraqis dead. The company is counting on offsetting that loss of business, for hundreds of millions of dollars a year, with contracts in Afghanistan.

—Yochi J. Dreazen and Siobhan Gorman contributed to this article.

Sri Lankan president claims win in long war with rebels

By Peter Wonacott

NEW DELHI—Sri Lanka's president said Asia's longest-running insurgency had been vanquished, after government troops trapped the remnants of the Tamil Tigers in a nine-hectare area and a senior rebel leader issued a statement of surrender.

A Sri Lankan military spokesman, Brigadier V.U.B. Nanayakkara, said troops were conducting "mopping up operations" within a tiny wedge of territory along the country's northeast coast.

Brig. Nanayakkara said troops continued to draw fire from the rebels and were fending off suicide bombers but he predicted fighting would be over in days.

There's no trace of the Tamil Tiger chief, Velupillai Prabhakaran, according to the military spokesman, though the government has recently captured other top rebels trying to escape the country by boat.

The accounts of continuing battlefield clashes were at odds with a statement Sunday from a senior Tamil Tiger leader surrendering to avoid more bloodshed.

"To save the lives of our people is the need of the hour," said the rebel leader S. Pathmanathan in a statement carried on the pro-Tiger Web site TamilNet. "Mindful of this, we have already announced to the world our position to silence our guns." He added: "This battle has reached its bitter end."

The 26-year civil war has come with a huge human cost, especially as fighting has intensified in recent months. Hundreds of thousands of ethnic Tamils have been forced to flee the country's north while thousands are estimated to have been killed in crossfire and artillery barrages. The government and Tamil Tigers have blamed each other for the civilian deaths, and aid groups have faulted both.

In acknowledging defeat, the Tamil Tiger leader, Mr. Pathmanathan, said 3,000 civilians lay dead on the streets. The deaths were caused by "shells, illness and hunger," he said, according to the statement.

In a speech Saturday in Jordan, President Mahinda Rajapaksa said the elimination of an insurgency "paves the way for democracy to root itself and development to march ahead after decades of conflict."