Weekend Journal: Studios bet on prequels to reboot the summer blockbuster season

THE WALL STREET JOURNAL.

VOL. XXVII NO. 67 | EUROPE | FRIDAY - SUNDAY, MAY 8 - 10, 2009

DOWJONES A NEWS CORPORATION COMPANY

europe.WSJ.com

9 772191 986955 19

THE WALL STREET JOURNAL.

What's News

GM's loss widened to $5.98 billion as bankruptcy jitters and a sales slump created a "revenue implosion." The auto maker and Fiat are weighing a deal to let the Italian firm take control of GM's European and Latin American operations without putting cash on the table. Page 3

■ **Barclays posted** a first-quarter profit, driven by a surge in sales and trading income at its investment bank. Page 17

■ **Société Générale reported** a quarterly loss as it wrote down bad loans. Page 17

■ **U.S. stocks declined,** helped by weakness in technology shares following Cisco's earnings report. European stocks fell. Page 18

■ **Shell dropped** plans to explore for oil in Alaska's Beaufort Sea amid environmental-group challenges. Page 3

■ **The EU offered** $798 million in incentives to six ex-Soviet nations to strengthen ties and encourage democratic reforms. Page 2

■ **Hedge-fund** investors appear ready to put some money back to work as sentiment thaws after months of withdrawals. Page 17

■ **A receiver alleged** financier Danny Pang misused investor funds for personal use and improperly transferred millions of dollars. Page 23

■ **The trustee** of Bernard Madoff's defunct investment firm sued J. Ezra Merkin to return $558 million. Page 23

■ **A report said** the U.K. needs more-effective financial regulation to stay globally competitive. Page 19

■ **Unilever posted** drops in sales volume and profit for the quarter, a sign its new CEO's strategies could take a while to pay off. Page 4

■ **AB InBev's profit jumped** 92% but the company warned rising costs would make that hard to repeat for the rest of 2009. Page 4

■ **Pope Benedict XVI begins** his three-stop Middle East visit Friday, on hopes that he will avoid the missteps of his previous tours. Page 11

■ **Afghan police fired** Thursday on rock-throwing protesters enraged by the deaths of dozens of civilians they blame on American bombing.

EDITORIAL&OPINION

Legal nihilism
The rule of law means little in Putin's Russia. Review & Outlook. Page 12

Breaking news at europe.WSJ.com

Rate cuts across Europe

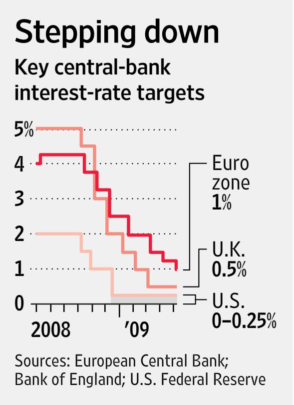
'Severe downturn' prompts banks to act; ECB, BOE plan to buy securities

By Joellen Perry

FRANKFURT — European central banks ramped up efforts to combat the recession Thursday, cutting key interest rates and pledging to purchase billions of dollars of securities.

The moves indicate that policy makers remain acutely concerned about the slowdown, despite tentative signs of stabilization in some sectors of the economy.

The European Central Bank, which sets interest rates for the 16-nation euro zone, cut its key rate to a new record low of 1% and launched a slate of programs aimed at goosing growth across the bloc, including a plan to buy about €60 billion ($79.82 billion) of low-risk corporate bonds.



Sources: European Central Bank; Bank of England; U.S. Federal Reserve

The Bank of England kept its key rate at 0.5% but boosted by £50 billion ($75.30 billion) a program to buy corporate and government bonds that is aimed at bolstering U.K. bank lending. Central banks in the Czech Republic, Iceland and Denmark also cut their key rates.

Slowing growth across Europe prodded policy makers into action. ECB President Jean-Claude Trichet said in a news conference after the central bank's decision that new staff forecasts, due next month, are likely to mirror bleak predictions from organizations including the International Monetary Fund. Last month, the IMF said it expects the bloc's $12.2 trillion economy to contract by 4.2% this year—worse than both the U.S. and the U.K.

Still, Mr. Trichet emphasized that "the latest economic data and survey information suggest tentative signs of a stabilization at very low levels." Some euro-zone confidence indicators have been inching up and official data Thursday showed German manufacturing orders jumped unexpectedly by 3.3% in March—their first monthly rise since August 2008—amid a surge in foreign demand.

Mr. Trichet left the door open for future rate cuts, though he suggested policy makers are likely to hold steady at 1% at their next rate-setting meeting in June. In a bid to keep euro-zone banks—

Please turn to page 27


Agence-France Presse

ECB President Trichet said 'the latest economic data and survey information suggest tentative signs of a stabilization at very low levels.'

EBRD to invest in eastern UniCredit units

By Paul Hannon

LONDON—The European Bank for Reconstruction and Development said it will invest €432.4 million ($575.3 million) in subsidiaries of Italy's UniCredit SpA in Eastern Europe, marking the development bank's largest capital injection of the economic crisis.

In a separate statement, the EBRD slashed its growth forecasts for Eastern Europe and the former Soviet Union, and said a sustainable recovery will only begin in late 2010.

The bank said it now expects the gross domestic product of the 30 countries in which it invests to shrink 5.2% this year, compared with an earlier forecast that it would increase 0.1%.

With its Unicredit investment, the EBRD said its goal is to ease the impact of the global financial crisis on Eastern Europe by providing medium-term and long-term loans as well as equity investments. It said it would make similar investments in other banking groups, though it didn't provide details.

Western European banks own large parts of the financial system in a number of Eastern European economies, mainly as a result of privatizations in the late 1990s and the first half of this decade.

UniCredit is the largest banking group in Central and Eastern Europe, with more than 4,000 branches in 19 countries.

The EBRD investment will go to UniCredit subsidiaries in eight eastern European countries.

UniCredit's Ukrainian subsidiaries will be the largest recipients of EBRD investment.

Separately, the EBRD's forecasts for 2009 were the most downbeat yet for the region. It expects the largest economy in which it invests—Russia—to contract 7.5% this year, having previously forecast it would grow 1.0%. By contrast, the International Monetary Fund last month said it expects Russia's GDP to decline 5.1% this year.

However, the EBRD does expect the economies in which it invests to grow in 2010 by a combined 1.4%. It hadn't previously published a forecast for next year.

"Growth is generally expected to be flat or very weak in the first half of next year, as credit growth remains cur-

Please turn to page 2

Obama reveals details of budget

By Jonathan Weisman

WASHINGTON—U.S. President Barack Obama delivered Congress the details of his $3.6 trillion budget Thursday, eliminating or cutting back 121 programs but swamping the $17 billion in savings with new efforts, from a college-completion fund to a new affordable-housing trust fund to 50,000 more cops on the beat.

At a time when state and local governments are slashing services, the Obama budget for 2010 shows little real sign of belt-tightening. It would mark a dramatic reversal for a government that had pulled back on many social programs in the eight years of the Bush administration or shaped them to reflect conservative priorities. President George W. Bush's program to promote abstinence to teens, for instance, would be replaced with a teen-pregnancy-prevention program that includes abstinence and contraception.

The president's budget overview in February laid out the top-line spending in each federal department, with almost all of them slated for an increase. The detailed plan reflects those increases program by program.

"We must build a government of the 21st century—a government that is more efficient and more effective," Mr.

Please turn to page 27

Inside

Brand Obama

A former Mardi Gras queen sells the White House
WSJ. Magazine

Markets

3 p.m. ET

	CLOSE	PCT CHG
DJIA	8400.77	-1.31
Nasdaq	1711.51	-2.71
DJ Stoxx 600	206.29	-0.83
FTSE 100	4398.68	+0.05
DAX	4804.10	-1.57
CAC 40	3251.52	-0.97
Euro	$1.3408	+0.80
Nymex crude	$56.71	+0.66

LEADING THE NEWS

EU offers aid, loans to six Eastern nations

Package will promote democratic reforms as Russia looms large

By Adam Cohen

PRAGUE—The European Union on Thursday offered six former Soviet states €600 million ($798 million) in incentives to promote stronger energy and economic ties and democratic reforms.

The plan, called the Eastern Partnership, has inflamed tensions between the EU and Russia, as Moscow worries that the bloc is encroaching on its traditional turf. The EU, for its part, remains wary following Russia's war in Georgia last year and a weekslong January cutoff of gas supplies to the EU during a dispute between Moscow and Ukraine.

"The EU knows, not just because of the Georgia crisis and the gas crisis at the beginning of this year, that safety and prosperity in Europe also depend on the stability of the Eastern partner countries," German Chancellor Angela Merkel said at a summit here of the six countries and the EU.

In addition to the money, international institutions, including the European Bank for Reconstruction and Development and the European Investment Bank, have been asked to increase their lending in the six—Armenia, Azerbaijan, Belarus, Georgia, Moldova and Ukraine—some of which have been hit hard by the downturn.

But the EU may be losing the competition for influence with a more-determined Russia. Only €350 million of the money is new, suggesting limited commitment. Moscow sees the Eastern Partnership, which it has described as EU "meddling," as an attempt by the West to carry on with a failed attempt to expand NATO into the region, says Alexander Rahr, director of the Russia program at the German Council on Foreign Relations.

In a sign of EU divisions over the Eastern Partnership plan, Ms. Merkel was the only leader of a big EU nation to attend the summit. Leaders of the six Eastern Partnership countries also gave the offer a mixed reception. Alexander Lukashenko, president of Belarus, and Moldovan President Vladimir Voronin, who have close ties to Moscow, didn't attend.

The EU didn't specify how quickly the €600 million will be distributed, or how reforms in the six countries will be measured. Belarus is a dictatorship; some of the countries have significant human-rights problems. Among them, the six countries have four open territorial conflicts.

At a separate EU meeting Thursday in Prague, at which policy makers sat down with labor leaders and employers to discuss jobs, EU leaders agreed to coordinate measures to cut growth in unemployment.

—Andrea Thomas contributed to this article.

Bank bailout

The EBRD is making investments in UniCredit subsidiaries across eight eastern European countries, to help them finance small and medium-size businesses and energy-efficiency projects.

Bank	Country	Investment, in millions
UniCredit (UC) Bank	Hungary	€50
Unicredit Bulbank	Bulgaria	50
Zagrebacka Banka	Croatia	50
UC Bank	Serbia	30
UC Bank	Bosnia	30
UC Leasing	Serbia	15
UC Leasing	Bosnia	15
UC Leasing	Ukraine	18.8*
ATF Bank	Kazakhstan	75.2*
Ukrsotsbank	Ukraine	75.2*
ATF Bank	Kyrgyzstan	15*

*Converted from U.S. dollars at current rate
Source: EBRD, Unicredit

EBRD to invest in UniCredit units

Continued from first page
tailed by high nonperforming loans and bank deleveraging, and external demand remains weak," the EBRD said. "A sustainable, gradual recovery is assumed to set in only in the second half of 2010, in line with slowly improving external conditions."

Meanwhile, currencies in the region rose markedly, led by the Hungarian forint, which rose 2.24% Thursday, to 277.70 to the euro.

The forint caught up with a rally by other Eastern European currencies, which have climbed in recent weeks as risk aversion has faded. The Czech koruna rose 0.3%, although the Polish zloty fell 0.1% against the euro.

India nears end of national elections

By Niraj Sheth

NEW DELHI—Many voters in troubled Kashmir defied a call for a boycott and headed to the polls Thursday amid tight security, as India neared the end of its month-long national elections.

A heavy security force kept violence to a minimum in Srinigar, the capital and largest city of Jammu and Kashmir state, and voters turned out despite the separatist group Hurriyat Conference's calling for a boycott of the elections. The locked-down city reported a turnout of 24%, slightly more than the 21% that voted in the last national elections in 2004.

"The poll process was absolutely peaceful," said a spokesman for India's election commission.

Violence was reported further afield—in West Bengal and Rajasthan states, which also voted Thursday. Skirmishes between rival party workers at one polling booth left one dead in West Bengal, while another was killed when police opened fire on a mob outside a ballot booth in Rajasthan, according to media reports.

While the turnout in Srinigar was notably less than the 57% reported elsewhere Thursday, voting there is typically lower due to the region's history of violence and separatist militants. In recent months, Kashmir has been hit by a string of demonstrations and a growing threat from Islamist terrorists crossing the border from Pakistan.

With only one phase of polling left until the May 16 vote count, Indian parties jostled Thursday for 85 of the national Parliament's 545 seats. For the incumbent Indian National Congress and opposition Bharatiya Janata Party, the largest prize of the day is in the northwestern state of Rajasthan. Rajasthan is one of the few states where none of India's myriad regional parties have a strong presence, leaving the battle for its 25 seats essentially a fight between the two national parties. In 2004, the BJP won 21 of Rajasthan's seats, while Congress brought in only four.

But the BJP has since run into trouble. In state elections last year, a wave of anti-incumbency sentiment swept the right-wing party out of power, bringing Congress to the helm of the Rajasthan government. This year, in national elections, Congress could repeat the performance and steal more seats from the BJP's sizable share.

The elections are shaping up to be a very tight race, and no single party is expected to score a majority of seats. The difference between Congress and the BJP, which is expected to garner more seats than any other party, could come down to fewer than a couple dozen seats. A substantial loss in Rajasthan could sound the death knell for the BJP's hopes of coming to power, analysts say.

"Wherever it goes head to head with Congress, it matters even more for the BJP than for Congress," says Seema Desai, a London-based analyst for the Eurasia Group. "It could lose out on its vote count from last time and that would be bad news."

CORRECTIONS & AMPLIFICATIONS

Munich Re AG declined to forecast its 2009 results. A Money & Investing article Thursday incorrectly said the company declined to forecast 2008 results.

Mike Patterson bought a repossessed Harley-Davidson Electra Glide Classic that originally came with saddlebags and a windshield at a sale in Indianapolis last week. A Marketplace article Wednesday incorrectly called it an Ultraglide Classic and said those features were added.

The production of flu vaccine involves injecting a virus into embryonated chicken eggs, which are then incubated for days. Two articles, published on April 30, 2009, and Nov. 5, 2004, incorrectly said that the virus is injected into the embryos of chicken eggs, and that the eggs are incubated for months.

INDEX TO BUSINESSES

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

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

Editeur responsable: Daniel Hertzberg M-17936-2003

INDEX TO PEOPLE

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

LEADING THE NEWS

GM's loss widens to $5.98 billion

Bankruptcy jitters, sales slump cause 'revenue implosion'

By Sharon Terlep

Associated Press

GM reported a first-quarter loss of $5.98 billion. Above, CEO Fritz Henderson talks to reporters in Washington this week.

General Motors Corp. said bankruptcy jitters and a global sales slump created a "revenue implosion" that led to nearly a $6 billion loss in the first quarter.

The auto maker burned through $10.2 billion as revenue plunged 47%, the latest sign GM is running out of options as it races to meet a June 1 restructuring deadline set by the White House. The company is surviving on $15.4 billion in federal loans and has said it needs another $11.6 billion to stay afloat.

"The concern about bankruptcy is having an impact on our sales," Chief Financial Officer Ray Young told reporters. He noted that a U.S. government guarantee of GM and **Chrysler** LLC warranties wasn't announced by the Obama administration until March 30. As a result, consumers for most of the quarter were unsure about warranty protection. Chrysler last week filed for protection from creditors under the bankruptcy code.

"We're spending our time to avoid bankruptcy court," Mr. Young said.

GM on Thursday reported a loss of $5.98 billion, or $9.78 a share, compared with a loss of $3.28 billion, or $5.80 a share, a year earlier.

Revenue dropped to $22.43 billion from $42.38 billion because of declining sales world-wide, but principally in North America and Europe.

"Our first-quarter results underscore the importance of executing GM's revised viability plan, which goes further and faster to lower our break-even point," Chief Executive Fritz Henderson said in a prepared statement.

As weak as the results look, analysts were expecting worse. Excluding items, GM's loss was $9.66 a share. Analysts had predicted a loss of $11.05 a share on that basis and revenue of $20.2 billion, according to Thomson Reuters.

GM's shares were down six cents at $1.60 in afternoon trading Thursday on the New York Stock Exchange.

Although the company cut structural costs by $3 billion, Mr. Young said that wasn't sufficient. "We cannot cut costs fast enough to offset that revenue loss," he said.

The losses aren't expected to let up soon. GM will idle most of its assembly plants this summer, further slashing revenue.

GM has less than four weeks to squeeze painful concessions from its union and bondholders, victories critical to convincing the Obama administration it can survive outside bankruptcy court.

The company reported an operating loss of $3.2 billion from its North American operations and an operating loss of $2 billion in Europe. Only GM's Latin America, Africa and Middle East region made money, $16 million.

GM ended the quarter with $11.6 billion in liquidity, down from $14.2 billion the previous quarter. The decline was largely offset by federal loans GM received in the quarter.

Mr. Young said quarterly production dropped 40% to 900,000 vehicles from a year earlier. GM temporarily closed factories to stop its inventory from bloating.

"That's why we saw the revenue implosion, a combination of weakness and global volumes," he said.

Mr. Henderson, the CEO, has said that while he hopes to avoid a bankruptcy filing, the scenario is increasingly likely. The company needs 90% of bondholders to sign off on a deal to exchange $27 billion in debt for 10% of the company's stock. The company also needs the United Auto Workers union to agree to accept equity in exchange for at least half of the $20 billion GM owes a retiree health-care trust.

If GM succeeds, it would ask the U.S. Treasury to approve a plan in which the government would swap much of the auto maker's debt in exchange for taking a 50% stake in the company.

Mr. Young said GM hasn't engaged with an ad hoc committee representing some of the company's institutional bondholders. The group proposed a counteroffer to GM's debt swap that would give bondholders, rather than the government, a majority stake in the auto maker. Mr. Young said any changes to GM's offer would have to happen in the near term for the swap to be complete by June 1. He declined to comment on the likelihood of any changes.

GM and Fiat are weighing cash-free deal

By Stacy Meichtry And Dana Cimilluca

After months of negotiations, **Fiat** SpA and **General Motors** Corp. are weighing a deal that would allow Fiat to take control of GM's European, Latin American and South African operations without paying the Detroit auto maker any cash, people familiar with the matter said.

GM, which is running on loans from the U.S. government, burned through $10.2 billion in the first quarter and has undertaken an extensive restructuring.

Instead of paying cash, Fiat Chief Executive Sergio Marchionne is offering GM a stake in a new, publicly traded company that Fiat would create by splitting its auto unit from the rest of its businesses, which range from farm equipment to Ferraris, the people said.

Fiat aims to merge the car unit—which eventually would hold a stake Fiat is taking in **Chrysler** LLC—with GM's Latin American and European operations, including GM's German unit Opel and the British Vauxhall brand.

The merger is part of Mr. Marchionne's plan to create an automotive behemoth with annual revenue of about €80 billion, or roughly $100 billion, that could reshape the global auto industry.

But he is trying to pull off the three-way alliance with scarce financial resources. Fiat, which is saddled with €6.6 billion in net debt, refused to inject any cash into its alliance with Chrysler.

Many hurdles remain to reaching a deal between GM and Fiat, the people familiar with the matter said. The size of GM's potential stake hasn't been settled as the companies negotiate over the value of GM's European and Latin American operations.

Fiat is counting on the support of European governments to help finance the new company's operations.

Mr. Marchionne on Monday met with senior German officials and presented his plan to restructure GM's European and Latin American operations.

If a deal is reached, it would mark yet another turning point in Fiat's on-again-off-again history with GM. In 2000, the auto makers forged an alliance with GM taking a 20% stake in the Italian car maker.

The companies touted the potential synergies between GM's Opel unit in Germany and Fiat, which dominates the Italian market.

But the relationship frayed as the companies' engineering teams struggled to work together, and Fiat's finances fell into disarray. After Mr. Marchionne's appointment as CEO of Fiat in 2004, the Italian auto maker succeeded in getting GM to pay $2 billion to end the alliance.

Asian officials try to coordinate response to flu

A WSJ News Roundup

Health officials from across Asia met in Bangkok to discuss ways to coordinate their defense against the A/H1N1 flu virus, including the possibility of establishing some kind of joint mechanism for the development and production of vaccines.

Meanwhile, South Korea reported its third positive test for the flu in a human.

Health ministers in Southeast Asia are also considering steps to boost their stockpiles of Tamiflu and other drugs to fight the virus, officials meeting in Bangkok said.

"In a more globalized and interconnected world, an outbreak of an emerging infectious disease is immensely swift. To deal with it requires strong cooperative efforts," said Thailand's health secretary, Prat Boonyawongvirot. Delegates in Bangkok are expected to meet again Friday to draft more details on their plans for regional cooperation.

Chinese authorities Thursday started lifting a seven-day quarantine on passengers from the Mexico City-Shanghai flight, where a Mexican man was confirmed to be infected with the flu on May 1.

Shell scales back plans for drilling in Beaufort Sea

By Guy Chazan

Royal Dutch Shell PLC dropped a three-year plan to explore for oil in Alaska's Beaufort Sea following challenges by environmental groups, highlighting the obstacles facing Western oil majors venturing into the frontier territories of the Arctic.

Shell is one of several oil companies that have flocked to the icy waters off Alaska, seen as one of the world's last great unexplored petroleum provinces. But they've faced strong resistance from conservationists worried about the impact of drilling on what is widely seen as a pristine wilderness. Many claim the oil industry hasn't yet figured out how to clear up oil spills in the Arctic's iceberg-strewn waters, home to wildlife such as polar bears that are already under pressure from global warming.

Shell said it informed the U.S. Minerals Management Service, the MMS, that it had withdrawn its original 2007-2009 exploration plan for the Beaufort and would file a stripped-down, one-year drilling program for 2010 that "addresses concerns of North Slope stakeholders related to the pace of Arctic drilling."

In a statement, the company said that, thanks to newly acquired seismic data, its plans for the Beaufort had become "more focused" over the past three years and the original program "no longer represents Shell's current drilling objectives."

The U.S. Geological Survey estimates the area above the Arctic Circle contains just over a fifth of the world's undiscovered, recoverable oil and natural-gas resources, and with climate change shrinking the ice cap the region is becoming more accessible than ever before.

Shut out of other great oil-producing areas like the Middle East, Western majors have spent millions of dollars on licenses to explore, develop and produce oil in the Arctic. Last year, rights to drill in the Chukchi Sea off northwest Alaska attracted record bids of $2.66 billion. Shell paid the most—some $2.1 billion—to acquire 275 blocks there.

The Beaufort Sea has also generated huge interest. Some think its petroleum reserves might be comparable to those of Alaska's nearby North Slope, site of Prudhoe Bay, one of the world's largest oil fields. Shell spent $84 million on leases in one prospect, Sivulliq, but was forced to abandon exploration drilling there after a legal challenge by Alaska native groups and environmentalists.

Last November, the U.S. Court of Appeals for the Ninth Circuit ruled that the MMS didn't properly consider the risk of oil spills, disturbances to migrating whales and disruptions to the traditional hunting lifestyle of local Eskimos that related to Shell's plan to drill at Sivulliq.

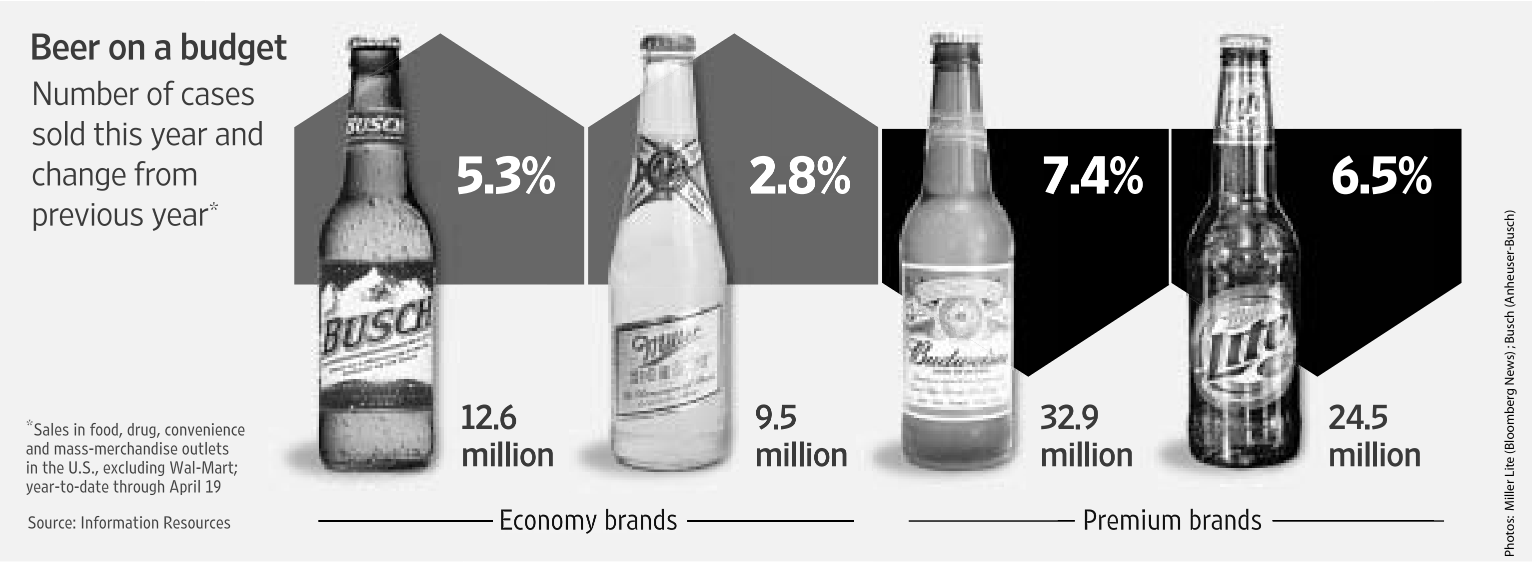
Oil companies working in Alaska's waters suffered a setback last month when a federal appeals court ruled the MMS's five-year plan to award leases in the Beaufort, Bering and Chukchi seas was illegal.

CORPORATE NEWS

Economy beers give brewers a boost

Sales of 'subpremium' brands help Pabst, Anheuser-Busch and Miller offset slower growth during slump

By David Kesmodel



Mark Lehr's favorite beer is Heineken, but one recent afternoon, the Chicagoan emerged from a 7-Eleven with a 12-pack of Busch that cost him $8—about $7 less than a dozen Heinekens.

"My funds are limited right now," said the 39-year-old house painter, noting that he has had far fewer customers during the recession.

Sales of so-called economy brews, including Busch, Miller High Life and **Pabst Brewing** Co.'s Pabst Blue Ribbon, are rising faster than the U.S.'s beer sales overall, and are helping industry giants **Anheuser-Busch InBev** NV and **MillerCoors** LLC weather the economic downturn.

Though less profitable, low-priced brews such as Natural Light and Busch Light are helping Anheuser offset slower sales growth for its larger brands. "We feel we have brands that can meet any consumer need," said Dave Peacock, president of the company's U.S. unit.

This year through April 19, U.S. retailers' sales of domestic "subpremium" brands were up 2.6% by volume and 8% by value from a year earlier, according to market-research firm Information Resources Inc. The data exclude sales at bars, restaurants and **Wal-Mart Stores** Inc. outlets.

By contrast, the U.S. beer industry's total volume rose just 0.5%. Sales of "premium" beers, such as Bud Light and Miller Lite, which account for about half the industry's total sales, fell 1.4%.

For shoppers, the math is simple. While prices vary, Busch Light or MillerCoors's Keystone Light generally cost around $14 a case, about $5 less than a case of Bud Light or Coors Light.

Not long ago, drinkers were "trading up," favoring imports, small-batch "craft" beers and premium lights. Now, Heineken and other import brands are struggling, and the growth of craft beers has slowed.

MillerCoors President Tom Long said in an interview that some drinkers are embracing a wider cultural shift toward thrift.

MillerCoors, a joint venture of **SABMiller** PLC and **Molson Coors Brewing** Co., has seen sales growth for its Miller High Life brand accelerate recently, thanks partly to TV ads that deride expensive purchases like $11.50 hamburgers, Mr. Long said.

Anheuser's Mr. Peacock said beer is better-positioned amid the recession than other consumer-goods sectors because private-label brands aren't much of a factor. Many established, low-priced brands are available, he said. Also, consumers tend to care more about image with a social product like beer than they do with goods like milk or cereal, which enjoy sizable private-label sales.

Gillian Singletary, 24, of Los Angeles, has been buying more Pabst Blue Ribbon and Miller High Life and less Stella Artois and Pete's Wicked Ale. She said Blue Ribbon is seen as hip—in a retro way—at some L.A. bars.

Pabst declined to comment for this article.

The economy brews are flourishing despite relatively little advertising. Natural Light, Busch Light and Busch are the nation's fifth-, seventh- and eighth-largest beer brands by volume, but Anheuser spent less than $4 million, combined, promoting them last year, according to research firm TNS Media Intelligence. That compares with more than $270 million for Bud and Bud Light.

Several convenience-store chains—the largest single channel for U.S. beer sales by volume—began seeing a big rise in spending on low-priced beers at the start of the year. At 7-Eleven Inc., with 6,000 U.S. stores, sales of such beers are up 9% in dollar terms this year, said Alan Beach, vice president of merchandising.

The chain noted that after cigarette makers raised prices this spring ahead of a federal tax increase, a significant number of shoppers who buy both cigarettes and beer began buying cheaper beer.

Some retailers have begun to promote cheaper brews harder than ever. Bob Gulley, senior category manager for alcohol sales at the ampm convenience-store chain, told its stores this year to begin offering 30-can packages of Busch Light, Keystone Light and other low-priced brands so he could better compete with supermarkets.

Anheuser buoys AB InBev profit

By Matthew Dalton

BRUSSELS—Brewing giant **Anheuser-Busch InBev** SA said Thursday its first-quarter net profit rose 92%, but warned that rising costs and stronger results last year would make it difficult to repeat that performance through the rest of 2009.

The newly merged company posted a net profit of $716 million for the three months ended March 31, up from $373 million a year earlier. The company noted that the year-earlier results don't include U.S.-based Anheuser-Busch Cos., which InBev purchased in November. It didn't report pro forma figures for the 2008 quarter combining results from InBev and Anheuser-Busch.

Sales totaled $8.2 billion, down 7.4%. The year-earlier sales figure includes results from Anheuser-Busch.

The sales decline was mainly due to a drop in the value of the Brazilian real against the dollar, along with other currency fluctuations, which hit sales by about $1 billion. Excluding these effects, sales would have risen 4.7%, the company said.

AB InBev, the brewer of Budweiser, Stella Artois and dozens of other brands, also confirmed it would sell Oriental Brewery, its South Korean beer unit, to U.S. private-equity firm **Kohlberg Kravis Roberts** & Co. for $1.8 billion to help pay down the debt it took on to buy Anheuser-Busch.

It has features that are likely to be repeated in other leveraged-buy-

AB InBev brews Budweiser, Stella Artois and dozens of other brands.

out deals as long as difficult credit conditions persist. KKR will fund more than 40% of the purchase price, for example, and AB InBev will initially provide $300 million of financing. That helped AB InBev secure a healthy multiple of more than 10 times cash flow for the business.

The deal gives AB InBev the right to buy back Oriental Brewery within five years at "predetermined financial terms," which weren't disclosed. AB InBev will book a capital gain of $500 million from the sale, which will close in the third quarter, it said.

In the first quarter, AB InBev continued to feel the impact of last year's soaring commodity prices, with costs per unit of beer sold rising 2.5%. However, the company said its plans to capture savings from the Anheuser deal were helping to keep costs down.

AB InBev has promised to cut annual costs by $2.25 billion as a result of its purchase of Anheuser, with $1 billion of those cuts coming this year. The brewer achieved $295 million of cost cuts in the first quarter, putting it on track to meet its targets.

The company's first-quarter earnings before interest, tax, depreciation and amortization—adjusted for one-time items—totaled $2.79 billion, up from $2.53 billion a year earlier on stronger results in North America, particularly in the U.S. Last year's quarterly core earnings result is the company's estimate of what the earnings would have been if they had included the results of Anheuser-Busch.

"Overall, beer is confirming to be a very resilient business, even in a downturn," AB InBev Chief Financial Officer Felipe Dutra told reporters.

But investors shouldn't expect similar Ebitda growth during the rest of the year, the company said. The brewer estimates a percentage increase in costs per unit of beer sold in the "low single digits" for the rest of the year.

Goldman Sachs Group Inc. advised KKR on the Oriental Brewery deal, and J.P.Morgan Chase & Co., Deutsche Bank AG and Lazard Ltd. advised AB InBev.

—Dana Cimilluca contributed to this article.

Unilever sales, earnings fall amid halt to price increases

By Aaron O. Patrick

LONDON—Consumer-goods giant **Unilever** reported drops in first-quarter profit and sales volume, in a sign that the new chief executive's moves to boost sales by keeping prices in check could take a while to pay off.

The Anglo-Dutch company reported Thursday that sales volume fell 1.8%. That exceeded the 1.6% recorded for the previous quarter, even as Unilever halted price increases around the world in an effort to stimulate buying—part of CEO Paul Polman's strategy to win market share from rivals such as **Procter & Gamble** Co. and **Nestlé** SA.

Net profit at Unilever—the world's second-largest consumer goods company by revenue, after P&G—fell to €731 million ($974.5 million). That was down 45% from the year-earlier period, which was boosted by a large gain from the sale of businesses.

Revenue fell 1% to €9.5 billion.

In one bright spot, sales by value rose 4.8%, excluding the effects of acquisitions, disposals and currency movements. The increase was greater than what analysts had expected and alleviated investors' concerns that the company may have been suffering particularly badly from the economic downturn.

The results were "not a disaster, as some had feared," Sanford Bernstein analyst Andrew Wood wrote in a note. Unilever shares jumped 9% to €16.91 in early trading on the Amsterdam Stock Exchange. They are down about 7% this year.

Mr. Polman joined Unilever, which owns such brands as Ben & Jerry's ice cream, Dove soap and Lynx deodorant, at the start of the year after stints at P&G and Nestlé. One of his first decisions was to place more emphasis on volume and less on price increases, a strategy that requires a tricky balancing act as Mr. Polman aims to maintain profit margins and spend money on developing new products.

In a media briefing Thursday in London, Mr. Polman attributed the company's mixed performance to tough economic conditions in some countries, particularly Germany and Russia. "I think we are in for a period of slow growth over a long time and we are planning accordingly," he said. "The economic situation continues to be tough for the foreseeable future."

Unilever held prices steady in the first quarter. In 2008 Unilever increased prices 7.2% despite the economic crisis and falling commodity prices. The higher prices triggered a fall in sales volume as some consumers switched to less-expensive rivals.

In February, Mr. Polman scrapped the company's sales and profit targets, citing the uncertain economy. He didn't provide an outlook Thursday.

— Michael Carolan contributed to this article.

CORPORATE NEWS

Telecoms' results sag

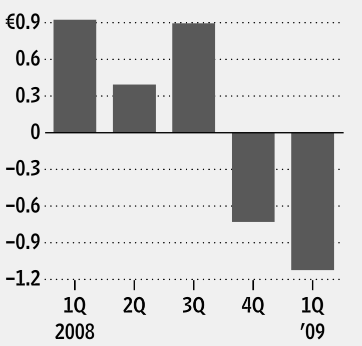
European carriers suffering amid global downturn

BY ARCHIBALD PREUSCHAT AND GIADA ZAMPANO

Customers shop at a Deutsche Telekom T-shop in Bonn, Germany

Weak signal

Deutsche Telekom's net profit/loss, in billions



Sources: the company; Bloomberg News (Photo)

Two European telecommunications heavyweights, **Deutsche Telekom** AG and **Telecom Italia** SpA, Thursday reported first-quarter results that were weighed down by the economic downturn, but sought to reassure investors on their full-year forecasts.

Deutsche Telekom posted a net loss of €1.12 billion ($1.49 billion) for the quarter ended March 31, compared with a year-earlier net profit of €924 million. The company's bottom line was hurt by a €1.8 billion write-down related to its T-Mobile operations in Britain, for which it said it is reviewing all options.

Despite the hefty write-down, the German company still expects to post a net profit for the full year, said Chief Financial Officer Timotheus Höttges, in a conference call.

Deutsche Telekom last month issued a surprise profit warning, saying that its 2009 operating profit would fall short of expectations because of weak mobile operations in the U.S., Britain and Poland, in particular. The company on Thursday further amended its full-year outlook to account for the consolidation of Hellenic Telecommunications Organization SA.

The company said it now expects 2009 earnings before interest, tax, depreciation and amortization, adjusted for exceptional items, to come in 2% to 4% lower than 2008's €19.5 billion. The acquisition of Greece's OTE will contribute an additional €2 billion to 2009 adjusted Ebitda, the company said. Telecom Italia said its first-quarter net profit fell 4.5% becaue of a weak performance in Brazil and slowing mobile revenue at home due to the tough economic climate, but the company confirmed its targets for 2009.

Italy's largest telecom operator, which is focusing on reducing debt and slashing costs, posted a net profit of €463 million, down from €485 million a year earlier. Revenue fell 6.7% to €6.79 billion from €7.28 billion a year earlier, as a slowdown in mobile spending and a sales-network restructuring were only partially offset by domestic broadband growth.

Chief Executive Franco Bernabe said the first-quarter results were "satisfying," in light of the tough macroeconomic environment, and confirmed the company's commitment to profitability and revenue generation.

Nintendo expects flat net as Wii, DS demand cool

BY DAISUKE WAKABAYASHI AND KENNETH MAXWELL

TOKYO—**Nintendo** Co., after several years of sharp earnings growth, says it expects sales and profit to level off this fiscal year as consumer demand for its Wii game machine and DS handheld starts to plateau.

Nintendo first showed some signs of a slowdown last year in Japan, considered an early indicator for global consumer trends. The Japanese casual gamers who fueled the Wii's growth aren't stocking up on extra games, at least not at the rate of more devoted videogame players. In the fiscal year that ended March 31, Wii hardware sales fell 47% in Japan, and total Nintendo sales there fell 30%.

So far, the problem has remained contained to its home market. For the year, Nintendo reported profit rose 8.5% to 279.2 billion yen ($2.84 billion); sales rose 9.9% to 1.84 trillion yen.

In the U.S. and Europe, Nintendo has bucked the spending slump that has saddled other Japanese exporters with heavy losses. Nintendo's sales to North and South America rose 20% in the past fiscal year, and European sales increased 17%.

Over a three-year period, Nintendo's profits have nearly tripled, and the Wii has sold 50 million units since its 2006 release. The Wii has nearly outsold **Microsoft** Corp.'s Xbox 360 and **Sony** Corp.'s PlayStation 3 combined, with causal videogame players flocking to play simple games like bowling and tennis with the Wii's motion-sensing controllers.

Nintendo sold 25.95 million Wii machines in the past fiscal year, short of the 26.5 million it forecast in January. (Back in October, it had projected sales of 27.5 million machines.) For the current fiscal year, Nintendo expects sales to remain flat at 26 million units.

Hiroshi Kamide, an analyst at KBC Securities, says he doesn't see any Wii price cut built into Nintendo's projections for the current year. The company has so far resisted cutting the Wii's $249 price, while Microsoft trimmed prices last September and Sony is expected to do so in the near future.

For the current fiscal year, Nintendo sees revenue declining 2.1% to 1.80 trillion yen. The Kyoto-based company forecasts profit to rise 7.5% to 300 billion yen in the current fiscal year from the previous year.

The company targets an 8% rise in Wii software sales to 220 million units for this fiscal year. For the DS handheld, Nintendo expects a 4% dip to 30 million units.

UAL chief pans limits on alliances

BY DANIEL MICHAELS

BRUSSELS—The U.S. will face increased pressure to relax restrictions on foreign ownership of its airlines after a recently signed aviation treaty between Canada and the European Union, a top U.S. airline executive said Thursday.

In a speech here, Glenn Tilton, the chairman and chief executive of United Airlines parent **UAL** Corp. urged U.S. lawmakers to reject proposed legislation currently before Congress that could limit cooperation between U.S. and foreign carriers.

Canada and the EU Wednesday signed an "open skies" agreement under which airlines from either side can fly to any point on the other, and will eventually be allowed to buy large stakes in each other. The Canadian pact goes further than a similar deal between the U.S. and EU signed in 2007 because the new treaty gives Canadians and Europeans much greater access to each other's markets.

"This is hardly the time for further protectionism," Mr. Tilton said. He was referring to legislation—proposed by House Transportation and Infrastructure Committee Chairman James Oberstar of Minnesota—that would place greater limits on foreign investors in U.S. carriers and restrict commercial links between U.S. airlines and foreign partners. The proposed bill could even force carriers to unwind alliances that they have struck over the past 16 years.

The U.S. currently limits foreign ownership of its carriers to 25%, and Mr. Oberstar's proposal would also limit foreign investors influence on management of an airline, in areas such as marketing. The EU limits foreign ownership to 49%, but is willing to lift that limit if other countries do likewise, as Canada is doing. European officials are pressing the U.S. strike a bilateral deal like the one with Canada.

Reacting to Mr. Tilton's description of Mr. Oberstar's proposal as protectionism, a spokesman for Mr. Oberstar, Jim Berard, said: "It's up to airlines that want to change the existing law [restricting ownership] to state their case to Congress. So far they haven't."

Mr. Oberstar has questioned the benefit to consumers of allowing U.S. carriers to ally closely—such as selling tickets on each other flights and uniting frequent-flier programs—with foreign airlines or investors. Several labor unions linked to the U.S. aviation industry and some consumer groups support Mr. Oberstar's efforts.

Airlines say their alliances—Star, oneworld and SkyTeam—not only provide financial benefits, but also give fliers advantages. Airlines are generally forbidden from merging across borders, and alliances give them some of the efficiencies that might otherwise come from international acquisitions.

The Canada-EU treaty comes as **ACE Aviation Holdings** Inc.'s Air Canada is struggling financially. The airline plunged to a net loss of 1.03 billion Canadian dollars (US$883 million) last year and is facing a severe liquidity crisis that some analysts believe could push it back into bankruptcy-court proceedings for the second time since 2003.

—Susan Carey in Chicago contributed to this article.

Outlook remains bleak for Japanese electronics

BY YUZO YAMAGUCHI AND HIROYUKI KACHI

TOKYO—**Hitachi** Ltd. and **NEC Electronics** Corp. both warned that their fiscal-year net losses would be wider than previously forecast, suggesting the outlook for Japanese electronics manufacturers remains bleak despite signs of economic recovery in other parts of the world.

Hitachi, which had forecast a record net loss for a Japanese manufacturer, now estimates a net loss of 788 billion yen ($8.02 billion) for the fiscal year ended March 31, compared to an earlier forecast for a loss of of 700 billion yen.

The company said the economic downturn had led it to write down deferred tax assets, resulting in a higher-than-expected income tax bill. Deferred tax assets are credits against future taxable income.

"We remain in very severe conditions for the first and second quarters" of the fiscal year that started April 1, company Executive Vice President Takashi Miyoshi said. He wouldn't predict whether the company would be able to return to profitability during the fiscal year.

The maker of electrical products ranging from trains to television sets, however, more than tripled its operating profit estimate to 127 billion yen from 40 billion yen, as businesses such as a power generation and industrial systems improved on higher sales and deeper cost cuts.

Investors reacted favorably to the operating profit estimate revision. Hitachi shares rose 7.3% to 370 yen Thursday in Tokyo for their third straight session of gains. The benchmark Nikkei 225 Stock Average rose 4.6%.

Hitachi, which spent 150 billion yen on restructuring during the last fiscal year, plans to spend a "large amount" of money for this fiscal year to continue the restructuring, according to Mr. Miyoshi. He said the company has no plans to raise capital from the Japanese government.

Growing losses also have forced NEC Electronics into fundamental change, with the company last week announcing it was discussing a merger with **Renesas Technology** Corp. to become the world's third-largest semiconductor maker.

NEC said it now expects a net loss of 83 billion yen for the just-ended fiscal year, bigger than the 65 billion yen loss it forecast in late January and considerably worse than the 16 billion yen loss it reported a year earlier.

Hitachi and NEC will release fiscal-year financial results next week.

The company blamed the poor performance on a slide in demand for chips used in consumer electronics, automobiles and industrial equipment.

NEC lowered its fiscal-year revenue outlook to 546 billion yen from 555 billion yen. It also expects a deeper operating loss of 68.5 billion yen, compared with a previously forecast loss of 55 billion yen.

NEC Electronics shares fell 0.8% to 1,066 yen.

Hitachi, NEC plan to release financial results next week. Both companies' earnings are based on U.S. accounting standards.

Airlines cheer EU's waiver of slot rule

BY KAVERI NITHTHYANANTHAN

The Association of European Airlines welcomed the European Union's decision to waive the "use it or lose it" flight-slot rule for the summer season.

A slot is a period of time allocated to, or reserved by, an airline for taking off or landing. The current rule states if an airline doesn't use its allocated slot at least 80% of the time, then it will lose it.

Members of the European Parliament met and overwhelmingly supported relaxing the rules. Airlines will now gain further flexibility and will be able to retain slots for the following year, even if they use them less than 80% of the time. A total of 508 votes were cast in favor of relaxing the rules, while 20 voted against and seven abstained.

The AEA, which represents 34 major airlines, said the economic downturn has created a temporary excess in capacity compared with demand. "Having to permanently give up a slot is an extreme option which the airlines will avoid if they can, but flying nearly empty to protect slots is neither economically nor environmentally responsible," said AEA Secretary General Ulrich Schulte-Strathaus.

More than 80% of European airports have seen traffic fall since the beginning of the year, and the summer season is expected to continue this trend, the European Parliament said.

The EU took similar action in the aftermath of the Sept. 11, 2001, attacks and in 2003 after the breakout of severe acute respiratory syndrome, or SARS.

Retailers report April sales jump

Wal-Mart's gain propels U.S. stores to monthly increase

By Kerry E. Grace

Wal-Mart Stores Inc. smashed analysts' expectations with a 5% jump in April same-store sales and the rest of the industry followed the trend, posting results higher than analysts' views.

Retailers overall posted a 1.2% rise in same-store-sales for April, beating expectations for a small decline. The gains in many cases, however, remain incremental and analysts say a full recovery is still a ways off.

The April sales figures "are encouraging, but I wouldn't call them a victory," said Chris Donnelly, a partner in the retail practice of consulting firm Accenture Ltd.

Brian Sozzi, an analyst with Wall Street Strategies Inc., said he wasn't surprised by the industry's monthly and quarterly results. "Retailers aggressively managed down inventories coming out of the dismal holiday quarter and are finally benefiting from serious store-closing campaigns orchestrated in 2008," he noted.

March sales were hurt by Easter moving back to April this year, and April sales likely benefited from the shift. Most analysts say they prefer to look at the two months together for this year and 2008 to get a better idea of Easter-season shopping trends.

All news wasn't positive from Wal-Mart, as it expects sales of about $93 billion for the fiscal first quarter ended April 30, below analysts' estimates of $96.82 billion, according to Thomson Reuters. Still, in afternoon trading, shares were up 1.4% at $50.22 on the New York Stock Exchange.

Wal-Mart, the world's largest retailer, posted a 5% increase in U.S. same-store sales last month, excluding gasoline sales, with the namesake chain posting a 5.9% jump and warehouse chain Sam's Club rising 0.3%. Analysts expected a 2.9% increase overall. April's results were driven by the grocery, health and wellness, entertainment and home segments, and seasonal merchandise.

Vice Chairman Eduardo Castro-Wright said the company gained new customers, boosted its market share and found that when customers had more money to spend, "they spent it more often at Wal-Mart."

Rival discounter **Costco Wholesale** Corp. didn't fare as well, posting flat same-store-sales excluding gasoline and currency fluctuations. But **BJ's Wholesale Club** Inc. said same-store sales rose 5.5%, excluding gas, widely beating analysts' estimates.

Other companies that beat views included department-store **Stage Stores** Inc. and retailers **Gap** Inc. and **Ross Stores** Inc. **TJX** Cos. also beat expectations, posting a 3% increase when analysts were looking for same-store sales to fall.

Department-store operator **Macy's** Inc. and **Saks** Inc. missed analysts' estimates with drops of 9.1% and 32%, respectively, in sales at stores open at least a year.

—Karen Talley contributed to this article.

Heartburn concerns

The four proton-pump inhibitor drugs affected by Wednesday's recommendation:

- **Prescription**
  - Nexium (AstraZeneca)
  - Prevacid (Takeda)
  - Protonix (Wyeth)
- **Over the counter**
  - Prilosec OTC (Procter & Gamble)

Heartburn pills used with Plavix found to pose risk

By Alicia Mundy And Jared A. Favole

A cardiologist group warned doctors to limit the use of popular heartburn pills in certain patients, citing a new study that says these pills raise the risk of heart attacks by interfering with the anticlotting medicine Plavix.

The warning affects a multibillion-dollar-a-year class of heartburn drugs known as proton-pump inhibitors, which include the widely advertised "purple pill," Nexium.

The study by pharmacy-benefits company Medco Health Solutions Inc. and the Indiana University School of Medicine showed the four most commonly used proton-pump inhibitors boosted the risk of heart attacks and strokes by 50% among cardiac patients taking Plavix. The other main proton-pump inhibitors are **Takeda Pharmaeceutical** Co.'s Prevacid; **Wyeth**'s Protonix; and Prilosec OTC, an over-the-counter pill sold by **Procter & Gamble** Co. Plavix is co-marketed in the U.S. by **Bristol-Myers Squibb** Co. and **Sanofi-Aventis** SA.

The warning by the Society for Cardiovascular Angiography and Interventions in Washington targets only patients simultaneously taking one of the heartburn drugs and Plavix, not those taking a heartburn drug alone. Plavix is commonly prescribed for patients receiving a heart stent, which props open arteries, or for those who have had a heart attack or stroke. Stomach bleeding and acid reflux are frequent side effects of Plavix. Doctors say about half the patients on Plavix take a proton-pump inhibitor to address those side effects.

The new study is the latest to raise concern among cardiologists and patients that the combination could be undermining Plavix's effectiveness.

AstraZeneca PLC, the maker of Nexium, said it is too soon to rule out use of Nexium in people taking Plavix. "There is a lot of conflicting data on this," said spokesman Blair Hains. He suggested people wait until the U.S. Food and Drug Administration issues more information. Mr. Hains said the Medco study, presented Wednesday at a meeting of the cardiovascular society, had limitations.

The makers of the other proton-pump-inhibitor drugs didn't respond to requests for comment.

Paul Gurbel, a cardiologist at Sinai Hospital in Baltimore, said it may be the severe heartburn itself—not the drugs taken to treat it—that causes the additional risk. "Until we have a prospective study set up to answer this, we'll never have a definitive answer," said Dr. Gurbel.

The medical society said it recommends alternative medications like antacids as well as Zantac and Tagamet. The Medco study could help a potential Plavix competitor called prasugrel, from **Eli Lilly** & Co. and **Daiichi Sankyo** Co. That drug, which is awaiting FDA approval, doesn't appear to be affected by proton-pump inhibitors.

CORPORATE NEWS

Hermès sales benefit amid system of exclusivity

Long 'waiting lists' help hedge against consumer downturns

By Max Colchester

PARIS—Kasia Al Thani owns 18 versions of the $7,000 Birkin handbag made by French luxury-goods company Hermès and is on waiting lists for two more bags, including one in white crocodile skin.

"When I see other women carrying a Birkin in a color that I want, I get bag envy," says the 32-year-old chief executive of luxury retail Web site savoir-faire.com. "The more you can't have something, the more you want it."

For years, **Hermès International** SA has kept an elite band of high-spending clients coming back for more by making them wait for what they crave most. Waiting lists, which can stretch for years for certain handbags, are part of the company's broader approach of keeping demand and prices high. Hermès also keeps tight control over its retail outlets and rewards loyal clients with private parties, tickets to horse races and yoga sessions.

Getty Images

Victoria Beckham in Milan in January with an Hermès Birkin bag.

Today, the strategy is helping Hermès prove resilient as the luxury-goods industry navigates its worst downturn in years. The company Thursday said sales rose 3.2% in the first quarter, driven by sales of its handbags, wallets and other small leather goods. It's now cashing in as it fills orders that were made up to several years ago for its most popular handbags, helping it compensate for a drop in sales in its other divisions, including jewelry and watches, as consumers generally spend less.

"No one is immune to the crisis but Hermès looks like it will weather it better than most," said Erwan Rambourg, a luxury analyst at HSBC. "Their clients are very faithful." Hermès doesn't report quarterly profit figures.

How Hermès fares amid the economic crisis could become an important point of reference for the rest of the industry. The French fashion house, which was founded in 1837 as a saddle maker, has eschewed many of the strategies followed by others in the industry.

While bigger designer brands such as Louis Vuitton, Gucci and Armani have pursued fast growth, expanding rapidly in emerging markets and reaching out to a younger, hipper clientele with trendy products and advertising, Hermès has taken a sleepier approach to the business—even in times of economic prosperity.

"We are not fashionable, and we avoid being fashionable," says Hermès Chief Executive Patrick Thomas.

The company is wary of products that could hurt its upscale image. In 2005, for example, Hermès pulled its so-called Fourre-Tout canvas bag off the shelves even though it was accounting for 10% of overall accessories sales. "We didn't want to make the brand too accessible. Suddenly Hermès bags were being associated with canvas, which is not what we wanted," says Mr. Thomas.

The strategy has crimped growth in good times. Between 2005 and 2006, for example, sales at **PPR** SA's Gucci Group and **LVMH Moët Hennessy Louis Vuitton** SA's fashion and leather division—of which Louis Vuitton is the biggest brand—grew over 10%. Hermès' revenue growth was slower, at between 6% and 7%.

"Hermès has not grown as fast as some of its competitors during the good years, but tends to do better during the tough times," says Antoine Belge, an analyst at HSBC.

Group sales at LVMH in the quarter grew 0.4%, while sales at Gucci Group were up 5%. Sales in China have offset some losses in the high end of the luxury-goods market, but consultancy firm Bain & Co. estimates that luxury-market revenues will contract as much as 20% in the first two quarters of the year as a result of falling demand.

The largest division by revenue at Hermès is its leather goods division, which makes purses, wallets and handbags. This unit accounted for 43% of Hermès' sales in 2008. The company relies in particular on two handbags—the so-called Kelly and Birkin bags. The bags are hand-stitched and made from start to end by one artisan. Depending on the colors and leathers ordered they can be priced from $7,000 to more than $100,000 and can take years to be delivered.

Waiting-list customers pay for goods when they receive them, not when they order them. Since waiting lists can reach up to three years, the orders can serve as a sort of hedge against bad times, analysts say. "These orders account for around half of all [Hermès'] leather goods sales," estimates René Weber, a luxury goods analyst at Bank Vontobel AG.

Hermès says that it makes no particular effort to create waiting lists. If a customer orders a handbag made from a rare leather or in an exotic color it takes time to find the appropriate skins, the company says.

The company declined to give details on whether orders have been canceled more recently, or on the rate of new orders. Customers aren't asked for a deposit when they make an order, so could walk away at any time.

Hermès has fared well in previous downturns. During the SARS respiratory disease outbreak in 2003, Hermès' revenue fell less than its major competitors as high-spending tourists stopped traveling. Sales at Hermes decreased by 1% compared to 5.8% for French luxury giant LVMH.

GLOBAL BUSINESS BRIEFS

Luxottica Group SpA

High-end eyewear group reports profit fell 22%

Luxury eyewear maker **Luxottica Group** SpA on Thursday reported a better-than-expected 22% drop in first-quarter net profit, helped by cost-cutting efforts, but declined to give a forecast for the full year. Milan-based Luxottica said its net income fell to €80.4 million ($107.2 million) in the three months ended March 31 from €103.7 million a year earlier. The world's largest eyewear maker by sales said revenue fell to €1.31 billion from €1.4 billion. April sales results were better than in the year-earlier period, Luxottica said. "In March and April our results have stabilized in North America, while improving in nearly all other markets," said Chief Executive Andrea Guerra. Luxottica shares have shed 25% of their value over the past 12 months amid worries over how slowing consumer spending is hurting the retail and luxury-goods sectors.

Daimler AG

Daimler AG said sales at its Mercedes-Benz Cars division fell 24% in April to 90,900 vehicles from a year earlier as demand for luxury vehicles remained weak. Despite the decline, a Daimler spokeswoman said the company cut its inventories faster than planned last month and now has the lowest inventory level since 2002. The division's core Mercedes-Benz brand posted a 23% sales drop to 80,700 cars in April. Usually Daimler's cash-cow, with its Mercedes-Benz and Maybach brands, the division reported a first-quarter loss of €1.12 billion ($1.49 billion) at the earnings-before-interest-and-tax level, compared with a year-earlier profit of €1.15 billion.

Diageo PLC

Diageo PLC said its fiscal third-quarter comparable sales fell as markets weakened in the second half of 2009 but the company stuck to its full-year forecast. The world's biggest alcoholic-drinks producer by volume said core sales—which strip out the effect of acquisitions and disposals—fell 7% in the quarter ended March 31 from a year earlier. The drop was largely due to planned stock reductions at Diageo's U.S. spirits and wine distributors. Chief Executive Paul Walsh said there has been a "significant decline in the Russian market from the beginning of January." The maker of Guinness stout and Smirnoff vodka maintained its fiscal 2009 forecast for core operating-profit growth of 4% to 6%. Total net sales rose 11% in the third quarter from a year earlier, mainly thanks to exchange-rate movements.

TNK-BP Ltd.

A former employee of U.K. oil major **BP** PLC's Russian joint venture was convicted of attempting to steal commercial secrets from gas giant OAO **Gazprom**, Russian authorities said. Ilya Zaslavsky, an adviser on regulatory affairs at the joint venture, TNK-BP Ltd., and his brother Alexander, an independent energy consultant who headed the British Council's Alumni Club, were charged last March with industrial espionage by Russia's Federal Security Service. The brothers, who hold dual Russian-U.S. citizenship, were given one-year suspended sentences by a Moscow court, an FSB spokesman said. The FSB said the brothers tried to bribe an employee of state-owned Gazprom for company information.

News Corp.

The publisher of The Wall Street Journal and Japanese financial services firm **SBI Holdings** Inc. said Thursday they would set up a joint venture to create a Japanese edition of the newspaper's Web site. The venture, Wall Street Journal Japan K.K., plans to launch the site later this year. It will primarily feature Japanese translations of news articles and other content, including video and other multimedia, from all print and online editions of The Wall Street Journal and those of other Dow Jones & Co. publications, which are owned by **News Corp.** Wall Street Journal Japan K.K. also plans to develop mobile products and services in conjunction with the new site. This will be The Wall Street Journal's second non-English site in Asia. The Journal's Chinese-language Web site, Chinese.WSJ.com, launched in 2002.

Warner Music Group Corp.

Warner Music Group Corp.'s fiscal second-quarter loss widened sharply on write-downs of its investments in two digital music start-ups, while consumers continue to eschew nondigital recordings. Overall U.S. music sales fell for the seventh time in eight years in 2008 as increases in digitally downloaded albums and songs weren't enough to offset a nearly 20% plunge in compact-disc sales. Warner, one of the world's four largest music labels, said its quarterly loss widened to $68 million, or 45 cents a share, for the period ended March 31, from $37 million, or 25 cents a share, a year earlier. The company booked $33 million in write-downs related to online music store lala.com and imeem, a social-music service. Revenue fell 17% to $668 million, or 9.7% on a constant-currency basis.

Sotheby's

Sotheby's posted a wider first-quarter loss amid a sharp decline in auction sales. The global slowdown has reined in bidding, keeping top art off the block and forcing auction houses to rely on individuals selling items for personal reasons. Sotheby's, however, has been limiting minimum-price guarantees and last month said it would expand last year's restructuring plan and lay off additional employees. Sotheby's posted a loss of $34.5 million, or 53 cents a share, compared with year-earlier loss of $12.4 million, or 19 cents a share. Revenue fell 58% to $54.4 million as auction sales tumbled 71%. Sotheby's auctioned $61.3 million of art at a disappointing sale in New York Tuesday as two high-profile works by Pablo Picasso and Alberto Giacometti went unsold.

Thomson Reuters Corp.

Thomson Reuters Corp. reported flat results for its financial-markets division, while overall profit and revenue rose following Thomson's purchase of Reuters last year. The markets division, the company's biggest business, has been a concern. In April, Thomson Reuters acknowledged that revenue from desktops, one of its top-earning businesses, may fall this year, as widespread job cuts at financial firms curb demand. The segment's revenue edged up 0.4% in the first quarter, while operating profit remained flat. Thomson's overall earnings rose to $228 million from $194 million. But per-share earnings fell to 27 cents from 30 cents as shares outstanding jumped 30% on the merger. Revenue jumped 70% to $3.12 billion.

Boeing Co.

Boeing Co. on Thursday reported a sharp drop in orders for its commercial jetliners in April, as the troubled global economy continued to hurt demand from airlines and cargo services. The Chicago aerospace company received orders for 17 jetliners last month, down from 58 planes ordered during the same month last year, according to figures posted on the company's Web site. Boeing said it delivered 39 planes in April, down slightly from 40 delivered during the same month in 2008. Boeing, the world's No. 2 commercial plane maker after France-based Airbus, has grappled with weaker demand in recent months as the world financial crisis has forced airlines to cancel or postpone plans to buy new planes. Limited access to credit has made it more difficult for potential customers to finance new aircraft purchases.

DuPont Co.

DuPont Co. expects to cut another 2,000 jobs as part of a restructuring plan it unveiled in April, when the chemical giant warned 2009 was shaping up worse than expected. The company said Thursday it will continue to aggressively cut costs and capital spending, while continuing to invest in high-growth, high-margin areas such as its seed business and solar energy products. It plans to take restructuring-related write-downs and charges of $340 million to $390 million in the second quarter. DuPont expects to save $70 million this year, and $225 million a year by the end of next year from the moves. The effort is DuPont's second restructuring plan since last year, when a steep drop in fourth-quarter demand pummeled the chemical industry, leading to plant closings, massive layoffs and some companies filing for bankruptcy.

Giorgio Armani SpA

Italian fashion company **Giorgio Armani** SpA said its sales increased to €1.62 billion ($2.16 billion) in 2008, up 1.5% from the year before. It didn't disclose its profit for the year. The maker of Giorgio Armani jeans, cosmetics and haute couture said that sales growth had been particularly strong in Greater China, where revenue increased 30%. By contrast, revenue in Japan declined 4%. The Milan company said sales of cosmetics, jewelry and watches remained flat. However, revenues from its clothing brands, which include Emporio Armani and Armani Jeans, rose 8%. The brand's eyewear division recorded a 10% drop in sales.

—Compiled from staff and wire service reports.

SPECIAL ADVERTISING SECTION

GREECE

LOUISA GOULIAMAKI/AFP/Getty Images

Greece owns about a fifth of the world's shipping fleet. Last year, annual transport receipts rose 13%, after an 18% increase in the previous 12 months.

Government measures aim to bolster the economy

Country may post a modest growth because of public investments and a bank liquidity program; tourism, shipping seen as key

UNDER the weight of the global economic crisis, Greece's economic growth is heading for a sharp slowdown, but the country may avoid tipping into recession thanks in part to the government's bold spending program and its bailout of the country's troubled banks.

The economy grew at an average of 4% a year during the past seven years, but now investments and exports are falling and rising unemployment is dampening consumer spending. However, the Finance Ministry expects the country's €250 billion economy to grow 1.1% this year, from 2.9% in 2008, ranking Greece among the few European states, such as Cyprus and Slovakia, likely to have an expanding economy in 2009, according to the European Commission's spring forecast. According to the forecast, total GDP output in the 16-member euro zone will shrink 4% this year and fall 0.1% in 2010.

Public investments and the government's €28 billion bank liquidity plan, which aims to keep credit flowing to businesses and households, are among the key factors expected to significantly contribute to economic growth, says Finance Minister Yiannis Papathanassiou.

And the state investment program, partially backed by European Union funds to improve infrastructure among member states, is set to continue this year, budgeted at €8.8 billion (3.5% of GDP), down from €9.6 billion in 2008.

The government's Public Private Partnership (PPP) programs — initiatives that award the construction of state buildings to private companies which later recover their fees on an annual basis while the state occupies them — are also expected to contribute to investment activity this year. The Finance Ministry plans to increase the amount of approved PPP contracts in 2009 to between €1.7 billion and €2 billion, from €1.3 billion in 2008, in projects such as fire stations, schools and hospitals.

Despite the cutback in state investments, government projects and PPP programs will help soften the impact of the crisis, said the Bank of Greece, the country's central bank, in an annual report last month. However, the bank concedes it won't be enough to keep the economy growing due to falling consumption and private investments. According to Giorgos Provopoulos, governor of the Bank of Greece: "It's possible to have negative GDP rates within the year."

This sentiment is echoed by Chris Pryce, a director at New York-based Fitch Sovereigns Group, a company that assigns ratings to government debt. He has a "tentative estimate of negative 0.1%" for Greece's GDP expansion this year.

In the last quarter of 2008, GDP growth cooled to 2.4% year-on-year, from 2.7% in the previous quarter, its slowest pace since the country joined the euro zone in 2001. Investments fell at an annual rate of 5.3% to €10.1 billion, declining for a fifth straight quarter, led by a steep drop in the building of residential housing. And exports, the majority of which go to the EU, dipped 1.6% year-on-year to €10.9 billion, after rising 0.8% and 2.4% in the third and second quarters consecutively.

REUTERS/Yiorgos Karahalis

Greek Finance Minister Yiannis Papathanassiou sees public investment as key to economic growth.

On the equities front, the Athens bourse made a good start this year, outperforming its European peers. The benchmark general index has risen 15% since Jan. 1, vs. a drop of close to 1% in Germany's DAX and a 4.3% fall in London's FTSE 100.

Finance Minister Papathanassiou says it is too early to move ahead with any possible revision to the GDP estimate as "it will also depend to a large extent on tourist traffic, which has yet to start [for the season]."

However, Greece's tourism industry, which accounts for about 17% of the economy, is braced for a difficult year. Deteriorating labor markets world-wide and weakness in several currencies against the euro, have made a trip to a euro zone country more expensive for cautious consumers. According to Giorgos Drakopoulos, director-general at Athens-based SETE, a group representing more than a dozen tourism associations, including hotels and ferry operators, visitor arrivals will decline as much as 20% this year from 2008 in what he describes as a "bad-case scenario."

In a bid to help its important tourist industry, the Greek government introduced a series of measures in December, including a property tax break and lowering local levies on hotels and restaurants. The move enables the sector to offer discounts averaging between 15% and 20%, according to SETE.

Along with tourism, Greece is exposed to the headwinds of the global economic crisis through its substantial shipping industry — it owns about a fifth of the world's fleet. Greece's annual transport receipts, the majority of which come from shipping, rose 13% last year to €19.1 billion after an 18% increase in the previous 12 months, according to the Bank of Greece. But shipping revenues are likely to shrink this year as slumping global trade cuts into demand for transportation services and reduces cargo rates.

Nikos Magginas, an economist at Athens-based National Bank, Greece's largest lender, expects shipping revenues to fall 20% to 30% this year from 2008. "This could cut up to half a percentage point from [Greece's] annual [economic] growth rate," he says.

Shipping companies are slashing investment plans to weather the storm. Data from Allied, an Athens-based shipping brokerage, shows that global shipping companies placed orders for seven new vessels at the end of March. The number stood at about 230 a year earlier.

Today's changing global conditions are also impacting Greece's labor market, prompting the government to launch a €2.5 billion program to stem rising jobless numbers.

Unemployment in January rose to 9.4%, from 8.9% in December, according to Greece's National Statistics Service, well above the euro zone's average 8.3% jobless figure for the same period.

Young Greeks are among the hardest hit, with 12% of those aged 25 to 34 looking for work. And a number of islands, including Crete in southern Greece, have unemployment rates well above the national average.

Constantinos Michalos, president of the Athens-based Chamber of Commerce and Industry, which represents 102,500 businesses, expects jobless queues to get longer in coming months. "We see a worsening of the labor market from April until the end of September, this takes into account the projected crisis in tourism," he says. Tourism employs one in five of Greece's 4.5 million work force. The government intends to subsidize existing jobs and public-sector hirings, in a bid to support the young and those working in tourism, construction and small businesses. About 500,000 people will benefit from the measures, according to Labor Ministry estimates. "Our aim is to minimize the impact of the crisis," says Labor Minister Fani Palli Petralia.

SPECIAL ADVERTISING SECTION

GREECE

Country seeks to bridge its green-energy gap with rest of the EU

CHANGES to rules concerning Greece's renewable energy sources (RES) are likely to speed up investments in the sector, helping the country narrow the green-power gap separating it from its European Union peers.

Last December, the Greek Environment Ministry clarified a 1999 law on land planning and sustainable development to make it clearer where RES facilities can be built. The changes, expected to help reduce red tape and lower administrative expenses, are likely to reduce the number of legal challenges local residents or municipalities pose against the construction of RES, so overcoming what is seen as a major obstacle.

We will see the benefits of the change of rules within the year, says Ioannis Agapitidis, president of the Athens-based Center for Renewable Energy Sources (CRES), a state body which advises the government on energy issues.

Evangelos Lekatsas, president of Greece's electricity-grid regulator Athens-based Hellenic Transmission System Operator (HTSO), says the new rules may result in cutting the time investors need to launch a RES project to an average of about one year from 1.5 to two years currently.

Greece's operating renewable-energy plants had a capacity of 1,056 megawatts in March, the majority from wind parks, versus 1,042 megawatts in February, according to HTSO data.

> With energy producers offered 20-year contracts to sell their electricity, and guaranteed tariff rates, there is a predictable and low-risk environment for investors.

The annual growth rate in wind energy in Greece, which produced 985 megawatts at the end of 2008, reached 13% in 2008 against 10% in Spain and 37% in Italy, according to the European Wind Energy Association, a Brussels-based industry group representing 550 members world-wide. In 2007, the sector grew 16%.

The backlog of RES project licenses waiting for approval from authorities in Greece remains large.

In March, projects able to produce 5,418 megawatts were on hold, waiting for approval by local municipalities, the Environment Ministry, town-planning offices and others.

Despite being one of the EU's sunniest and windiest countries, Greece has been a laggard in adopting environmentally friendly power.

Figures from Luxembourg-based Eurostat, the EU's statistical office, show the percentage of electricity generated by renewable energy in Greece stood at 6.8% in 2007, compared with an average of 15.6% for the EU's 27 member states.

According to goals set by Brussels to help curb greenhouse-gas emissions, Greece needs to supply 18% of its power from renewable energy by 2020. The figure currently stands at around 8%.

ARIS MESSINIS/AFP/Getty Images

Last year, Greece's annual growth rate in wind energy reached 13%.

Greece is likely to meet these long-term goals, says Mr. Agapitidis of CRES, pointing out that the sector is in need of more innovative technologies to develop further, such as the introduction of offshore wind parks.

With energy producers offered 20-year contracts to sell their electricity, and guaranteed tariff rates, there is "a predictable and low-risk environment for RES investors," says George Vitorakis, analyst at Athens-based brokerage National P&K Securities.

Some of Europe's leading power companies have entered the Greek market with an eye on the renewable-energy pie, including Spanish utility Iberdrola and its Italian peer Enel.

Athens-based Terna Energy, whose wind parks have a total capacity of 143 megawatts, is among the largest players in the domestic market and intends to move ahead with investment plans to boost capacity to 450 megawatts by the end of 2010.

"Based on our revised investments plans… we expect to invest €264 million of capital between 2009 and 2011, versus our initial forecast of €229 million," says Manolis Maragoudakis, Terna Energy's CEO.

The text of this Special Advertising Section was written by Stelios Bouras, a freelance journalist based in Athens

ECONOMY & POLITICS

Rivals in Iran take aim at Ahmadinejad

Three major challengers in June election criticize president's hard-line approach, reflecting rift in establishment

By Farnaz Fassihi

TEHRAN, Iran—The three major challengers to President Mahmoud Ahmadinejad in the June presidential elections hail from different political backgrounds but share a common view: If Mr. Ahmadinejad is re-elected, he will lead Iran toward disaster.

As campaigning has kicked off, they have sharply criticized Mr. Ahmadinejad. While they broadly support Iranian policies such as pursuing a nuclear program and refusing to recognize Israel as a state, they seek to distance themselves from Mr. Ahmadinejad's tough-talking style.

"If Ahmadinejad's path continues, we are heading for the edge of the cliff," Mohsen Rezaei, a hard-line conservative and former head of Iran's Revolutionary Guards, said at a news conference on Sunday. Mr. Rezaei, who announced his candidacy last week, said he favors a foreign policy that best serves the national interests of Iran, not one that is "provocative" and "adventurous."

Mr. Rezaei's strong words underscore the deep divisions within Iran's conservative establishment, who favor ideological politics, on whether to support Mr. Ahmadinejad's bid for four more years in office.

The president hasn't officially announced his candidacy, but he has set up a campaign team and his advisers routinely make comments that suggest he will run.

Iran this week began registering candidates for the Islamic Republic's June 12 election. But it's already clear that four major contenders will emerge with the backing of political groups and the country's leadership.

In addition to the conservative Mr.Rezaei, two others have announced campaigns, both "reformists" who lean toward greater social freedom and flexibility: Mir Hossein Mousavi, prime minister in the 1980s, and Mehdi Karroubi, a cleric who served as speaker of parliament in the early 2000s.

Iranians elect their president for four years, with a maximum of two terms.

The election is deemed the most important political event in the region this year as the country's influence rises—particularly in Iraq and Afghanistan, where the U.S. is seeking stability and cooperation from neighboring states.

Iran's broader policies, such as its standoff with the West over its nuclear program and talks with the U.S., won't likely change with a new president because Supreme Leader Ayatollah Ali Khamenei has the final word on all state matters. Under Iran's constitution, the appointed senior cleric oversees the judiciary, armed forces and broadcast media.

However, analysts say the president remains the public face of Iran, and whomever Iranians elect in June will affect the country's international standing.

"The overall policies of the government will remain the same, but a different president can determine the way these policies are discussed and acted out," says Mashallah Shamsolvaezin, a political analyst in Tehran.

Mr. Ahmadinejad has a good chance of being re-elected because of his popularity with rural voters as well as the urban poor and middle class. But if the less-conservative rivals can strike a chord among urban voters, that could lead to a tighter race.

With his folksy banter and tough talk about the West, Mr. Ahmadinejad draws big crowds in the provinces. His critics complain that he is using state funds for his campaign travel. Local newspapers have reported that his government has distributed 400,000 tons of potatoes and doled out cash and gold-coin bonuses.

Mr. Ahmadinejad has addressed these allegations by saying he is sharing the country's wealth among citizens.

The state-owned radio and television networks openly back the president. To compete, his rivals are using novel campaigning techniques, such as sms text messages, Web sites, and DVDs.

Mr. Ahmadinejad's rivals are banking on the public's dissatisfaction with the economy. Unemployment and inflation have soared despite record-high oil revenues during Mr. Ahmadinejad's tenure.

Mr. Rezaei's candidacy could splinter Mr. Ahmadinejad's votes among the rank-and-file of security forces as well as conservatives who are unhappy about the government's performance.

Mr. Karroubi has vowed to get rid of the morality police task force, work toward equal rights for women, and free political prisoners. Drawing a distinction with Mr. Ahmadinejad, who has denied the Holocaust, Mr. Karroubi said last week that "the Holocaust is a fact. Whether the number of people who perished is six million or 6,000, denying it is of no benefit to Iran."

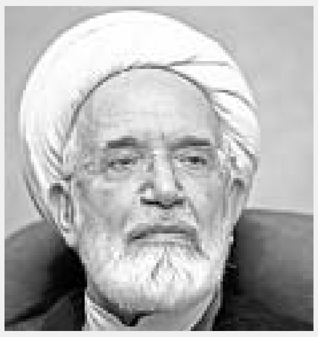
Mr. Mousavi is viewed by many as Mr. Ahmadinejad's most serious competition. Backers include Mohammad Khatami, who as president from 1997 to 2005 pushed to reform the system and open Iran to the world. Mr. Khatami initially entered the race but withdrew to avoid taking away votes from Mr. Mousavi.

At a rally of several thousand university students, Mr. Mousavi said Mr. Ahmadinejad's government has created such taxing living conditions that people have no time to think about freedom.

"Our people are looking for stable management skills and stable policies that can bring them a sense of relief and freedom," Mr. Mousavi said. The crowd, waving flags in green, his campaign color, chanted "freedom, freedom."

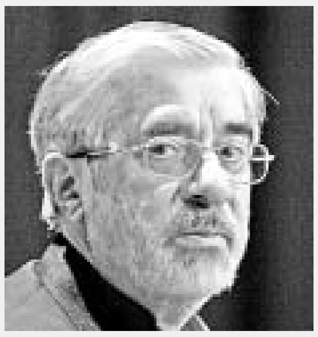
Iran's race takes shape

The main contenders in June's presidential election broadly support the country's current policies, such as pursuing a nuclear program. But Mahmoud Ahmadinejad's rivals are trying to differentiate themselves in language and tone, for instance criticizing his denial of the Holocaust.



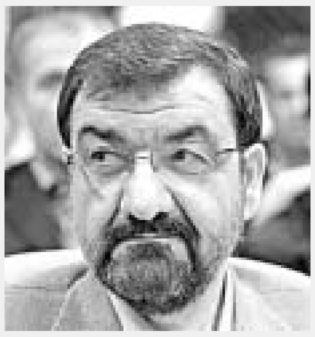
Mehdi Karroubi

- Speaker of the parliament under President Mohammad Khatami in the early 2000s.
- Founded Etemad-e Melli party (National Trust Party) after his defeat to Mr. Ahmadinejad in the 2005 presidential race.
- Supports human rights and women's rights. Says he will use a team of experts to manage the country.



Mir Hossein Mousavi

- Prime minister in the 1980s.
- Now president of the Iranian Academy of Arts.
- Influential backers include Mr. Khatami.
- Says he will put scientific methods ahead of ideology in handling the economy and foreign policy. Favors improving relations with the West. His wife, a scholar and artist, campaigns by his side.



Mohsen Rezaei

- Former commander of Iran's Revolutionary Guards.
- Now secretary of the Expediency Council, an assembly that advises the Supreme Leader.
- Says he will work to improve living conditions. Promises to name the most qualified people to his cabinet, regardless of their political leanings.

Mahmoud Ahmadinejad

- Populist ultraconservative president of Iran.
- Harsh critic of U.S. and Israel.
- Promised to 'bring oil income to people's tables' but his injection of cash into the economy led to inflation of 25% and high unemployment. Has support among rural voters, the urban masses and ultra-conservatives.

Reuters (3); Associated Press (Ahmadinejad)

Searching for hidden gems amid U.S.'s barrels of red ink

By Gerald F. Seib

CAPITAL JOURNAL

Ronald Reagan used to tell the story of the optimistic young boy who, when shown a room filled with a pile of manure, smiled and started happily digging into it. If there's that much manure, the boy said, there must be a pony in there somewhere.

That story is worth recalling while looking at the red ink in the broad budget plan U.S. President Barack Obama formally presented to Congress Thursday. The budget includes a pile of federal budget deficits over the next decade, at least. Could there possibly be anything good hidden in there?

Perhaps. Here's how: If the government is going to be stuck with big deficits as far as the eye can see, maybe all that red ink can be used to convince Congress that it's finally time to deal with the underlying problem of mushrooming costs of entitlement programs, specifically Medicare and Social Security.

Using deficits as a lever to fix entitlements would simply be a logical extension of the broader philosophy the administration has used to deal with today's economic mess. That approach was famously summed up by White House Chief of Staff Rahm Emanuel at a Wall Street Journal conference for business executives during the transition, where he declared: "You never want a serious crisis to go to waste."

In other words, if the administration was going to have to spend billions trying to fire up a sputtering economy, it would try to enact some of its agenda—in health, energy and education—in the process.

By the same token, the combination of a sluggish economy, financial-industry bailouts and big stimulus spending is producing big deficits that are getting everyone's attention. The Obama budget estimates federal deficits will total almost $7 trillion over the next 10 years; the Congressional Budget Office estimates the total at more than $9 trillion. Either way, that ought to make this a good time to remind everybody in Washington that if there were a plan to lower the cost of Medicare and Social Security, those long-term deficit lines would start to look a lot better.

One leading Democrat starting to make the case that this is a good time to tackle entitlements is Rep. Steny Hoyer, the second-ranking Democrat in the House. He pointed out Wednesday that, without action, interest on the national debt, Social Security, Medicare and Medicaid would together consume 18.5% of the country's total economic output by 2025.

He thinks Mr. Obama is prepared to respond. "There is a sense in the administration that you need to pursue both the investments we need to make now, which are going to cause substantial debts, but at the same time give Americans and our creditors confidence that we're going to pursue fiscal responsibility as a policy, long term," he said in an interview. "So I think it is a good time" to act.

It's worth pausing to note that using deficits as a lever to force spending reductions hasn't worked all that well in the past. Still, there was one time it did work. In 1981, Mr. Reagan and Congress, mindful that the Social Security system was heading for deficits of its own, appointed a commission to figure out what to do. They put the commission into the hands of one Alan Greenspan, then Republican wise man on economic matters, later chairman of the Federal Reserve.

The commission suggested a series of changes too sensitive for lawmakers to undertake on their own, including raising some Social Security taxes, limiting some benefits and lifting the retirement age. Congress bought in, and Mr. Reagan signed the changes into law in 1983. That left the Social Security system in good—even robust—shape for years.

Now, time is running out on those Social Security fixes, and the cost pressures will become even more acute in coming years for Medicare. Meanwhile, polls show the deficit emerging as perhaps the leading cause for doubt about the Obama agenda.

The question is how to get Washington to move beyond platitudes about the long-term problem and toward action. Mr. Hoyer argues for starting with Social Security. But because it's "difficult" to get politicians to agree on sensitive changes, he likes the idea of an independent commission, in the 1983 Greenspan model, to tackle the question.

Ultimately the question of whether and how Democrats use this moment to deal with entitlements will fall, as such questions usually do, to the president. Mr. Obama has talked privately of leading a "grand bargain" in which all sides agree to endure some pain to make a big fix to the nation's finances. Budget week is a good time to let the bargaining begin.