Corporate News: Activision's 'Call of Duty' game breaks sales records

THE WALL STREET JOURNAL.

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Breaking news at europe.WSJ.com

Darling criticizes bank owners

British chancellor says shareholders had a responsibility to check out-of-control expansion

By Patience Wheatcroft

Alistair Darling, the U.K.'s Chancellor of the Exchequer, lambasted the former shareholders of Britain's failed banks Thursday for what he said was the failure to exercise their responsibilities as owners.

Citing Royal Bank of Scotland Group PLC and HBOS, he said: "Their shareholders clearly didn't ask the right questions. They didn't take their stewardship seriously," and that, "There are huge questions to be asked about the role of the shareholders in these businesses."

Both HBOS, now part of Lloyds Banking Group PLC, and RBS have had to be bailed out with public money, leaving the U.K. taxpayer as a major shareholder in both groups. The government now holds 84% of RBS and 43% of Lloyds after putting a further £31.3 billion ($51.9 billion) into the two banks earlier this month.

Criticism of the failed banks has until now been largely directed at their boards and the policies they endorsed, particularly on risk and remuneration.

Mr. Darling made clear, in an interview with The Wall Street Journal, that he also held the owners of the businesses accountable.

"There is a difference between the mindset of an investor and the mindset of an owner," Mr. Darling said. "In too many cases, the responsibility of ownership seems to have been ignored."

The failure of investors to properly supervise the banks was also highlighted Thursday by the European Commissioner for competition, Neelie Kroes. Speaking of the Royal Bank of Scotland, she said the bank had tripled its balance sheet in the two years from 2006, growing to be only slightly smaller than the German economy. "It was simply too big to operate and supervise. And it should have set off investors' alarm bells," Ms. Kroes said.

Mr. Darling said that legislation wouldn't bring about

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Medvedev urges economic and political change

Agence France-Presse/Getty Images

In an annual address to parliament and top government officials, Russian President Dmitry Medvedev renewed his calls to modernize his country's oil-dependent economy and open up the political system but gave no sign the Kremlin plans to loosen its tight control. **Page 3.**

Intel to pay AMD $1.25 billion

By Don Clark
And Jerry A. DiColo

Chip rivals **Intel** Corp. and **Advanced Micro Devices** Inc. declared peace, announcing a far-reaching legal settlement Thursday that includes a $1.25 billion payment by Intel to AMD and a new set of rules for how Intel conducts its business. The agreement, which also includes a renewed five-year pact to cross-license the companies' patents, follows harsh scrutiny and adverse rulings regarding Intel's practices by regulators in Asia, Europe and the U.S.

AMD sparked a European Union probe that resulted in May in a $1.45 billion fine against Intel, the largest in the history of the antitrust authority, for alleged anticompetitive practices. Intel paid that fine while appealing the ruling.

AMD is now withdrawing its complaint in Europe, as well as complaints in U.S., Japan and South Korea. But its withdrawal has little procedural impact because the EU has already made its ruling and gathered hundreds of thousands of pages of evidence from AMD and others that it can continue to use in the court proceedings.

In a statement, the EU's competition commission said it will continue to "vigorously monitor" Intel's behavior. Indeed, EU regulators continued to press their antitrust case against Microsoft Corp., for years after the software giant agreed to pay billions of dollars to settle with adversaries, like Sun Microsystems Inc. and RealNetworks Inc.

The AMD settlement also comes as Intel selected A. Douglas Melamed as its new general counsel, according to people familiar with the matter. Mr. Melamed, a partner at WilmerHale in Washington, has decades of antitrust experience. Neither Mr. Melamed nor Intel would comment.

Intel, as part of the settlement, agreed not to use inducements to stop competitors from dealing with AMD. But Intel has long denied doing that, so it remained unclear how dramatically Intel's actions will change under the pact or how it will ultimately affect computer prices.

Intel and AMD make nearly all the microprocessor chips that provide calculating power to run most computers, though the much larger Intel controls roughly 80% of the market. AMD has long alleged that Intel used illegal tactics to maintain a monopoly in the market, including using discounts and rebates to

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Design destination

Poland has become a hot spot for contemporary art
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Markets

4 p.m. ET

MARKET	CLOSE	PCT CHG
DJIA	10197.47	-0.91
Nasdaq	2149.02	-0.83
DJ Stoxx 600	246.61	+0.16
FTSE 100	5276.50	+0.19
DAX	5663.96	-0.08
CAC 40	3808.07	-0.17
Euro	$1.4883	-0.71
Nymex crude	$76.94	-2.95

Iberia and BA approve merger

A WSJ News Roundup

British Airways PLC and **Iberia Lineas Aereas de Espana** SA approved a merger they have been negotiating for more than 15 months that will give the U.K. carrier a majority stake.

Iberia called it a "binding agreement" aimed at creating one of the world's largest airline groups.

It said the deal for a definitive tie-up is expected to be signed in the first quarter of 2010, though it would still need regulatory and shareholder approval.

Iberia said it also would be able to pull out of the agreement if it deems any final deal between British Airways and the administrators of its deficit-ridden pension fund unsatisfactory.

Iberia's chief financial officer said in a regulatory filing that the companies were studying a split under which 55% of the new company would be owned by current BA shareholders, with the rest held by Iberia shareholders.

The talks have dragged on since July of last year as both carriers grappled with the worst crisis in global aviation in years.

The merged company's financial headquarters would be in London, and the chairman would be Antonio Vazquez, who currently is chairman at Iberia. The chief executive would be Willie Walsh, now the CEO of British Airways.

The merger could yield synergies of €400 million, or about $600 million, a year after the new company's fifth year of operation, Iberia said.

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LEADING THE NEWS

Glasgow vote a gauge for Labour

Contest for open seat offers test of strength before general election

By Alistair MacDonald

A special election in Glasgow on Thursday for a parliamentary seat held by the U.K.'s Labour Party for the past 74 years is being watched as a gauge of the threat the Scottish National Party poses to Labour in the next general election.

The seat in Glasgow's North East constituency was vacated in June by Michael Martin, who stepped down from his role as House of Commons speaker after criticism of his handling of a scandal over misuse of parliamentary expenses. Labour candidate Willie Bain is expected to prevail in the election.

But the special election is focusing attention on the area's economic deprivation and how it is impacting traditional Labour voters ahead of a U.K. general election that must be held by next June. Glasgow North East's high rate of unemployment is feeding the Conservative Party's assertions that a decade of spending by Labour has done little to weed out poverty.

The economic turmoil also creates an opportunity for the SNP, which has made major strides in recent years. The party, which advocates Scottish independence from the U.K., won an election to head Scotland's Parliament in 2007, leading to predictions that it would pose headaches for Labour in the next U.K. election.

The performance of SNP candidate David Kerr in this election will provide a clue as to whether the party will siphon votes from Labour next year in Scotland. Labour has defended its economic record in the area, and has sent big guns such as Treasury Chief Alistair Darling to campaign for the seat.

The election features another noteworthy candidate: John Smeaton, the former Glasgow Airport baggage handler who gained world-wide fame in 2007 for helping to stop a man who was attempting to set off an explosive-laden Jeep at the airport. Mr. Smeaton is running as an independent.

Separately, in a speech on Thursday Mr. Brown sought to tackle concerns over high immigration into the U.K. Immigration is likely to be a major issue in the general election, and the British National Party, which advocates a policy of "resettling" immigrants and their descendants outside Britain, is expected to take some votes away from Labour.

Mr. Brown said talking about the issue of immigration shouldn't be a taboo. "I have never agreed with the lazy elitism that dismisses immigration as an issue, or portrays anyone who has concerns about immigration as a racist," Mr. Brown said.

Mr. Brown announced a number of initiatives, including making it harder for all but the most skilled of applicants to get into Britain by tightening the points-based system that controls immigration and setting up a "Migration Impact Fund" in which newcomers into areas with high immigration will pay a "charge" to help with local costs of public services like schools and health.

Repossessions of U.K. homes have slowed pace

By Ilona Billington

LONDON—The rise in U.K. home repossessions slowed in the third quarter, but strains on household finances are expected to drag on consumer spending and economic recovery in coming months.

The Council of Mortgage Lenders said Thursday that mortgage repossessions rose by 300 to 11,700 in the third quarter of the year from the second quarter, after falling 1,300 to 11,400 in the second quarter from the first.

The number of home owners in mortgage arrears of more than 10% of the balance of the loan rose to 26,300 from 26,100.

The figures indicate that once households do fall behind, they struggle to get back on track, according to Ed Stansfield, property economist for Capital Economics.

CML now forecasts a rise in repossessions to 53,000 in 2010 from an estimated 48,000 for this year. Both are below the CML's earlier forecast for 65,000 property repossessions in 2009.

The news from British households supports the Bank of England's prediction Wednesday that the U.K. economic recovery will be long and slow.

Muted bank lending, planned cuts in government spending and the threat of rising unemployment add to pressure on homeowners' pocketbooks.

Separately, the European Commission has recommended that some member countries get an extra year to cut their budget deficits, but pushed Greece to repair its public finances immediately.

The commission fears some states could struggle to reduce growing budget gaps.

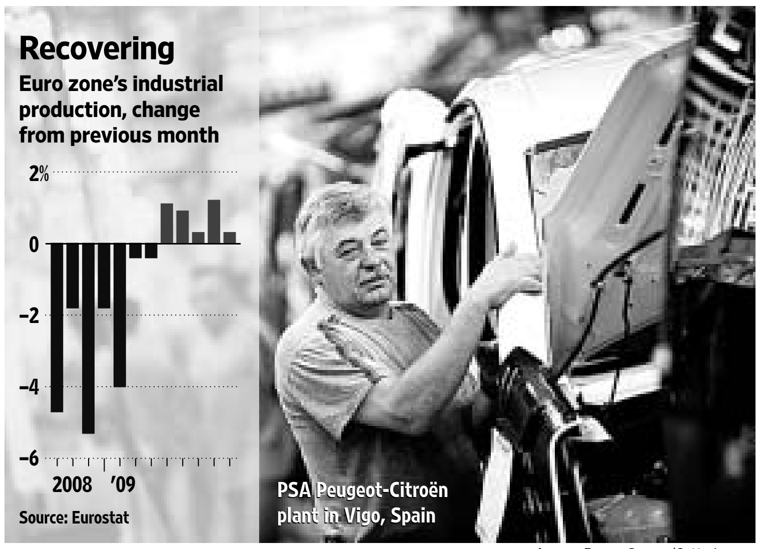
Euro-zone industrial production rises 0.3%

By Brian Blackstone

An increase in euro-zone industrial production signaled a strong return to economic growth in the third quarter, but bleak news from Spain and cautionary words from the European Central Bank suggest the recovery could be very weak.

Euro-zone production rose 0.3% in September from August, the European Union's statistics agency said Thursday. Though the increase was smaller than economists had expected, it still points to strong production gains for the third quarter as a whole, supporting forecasts for gross domestic product growth in the 2% to 3% range, on an annualized basis. GDP data for the euro zone are due out Friday.

The region's fourth-largest economy, Spain, said Thursday that GDP shrank last quarter, by 0.3% on a quarterly basis, from the second quarter. It was Spain's sixth consecutive contraction, reflecting the severity of the hit its economy took from both the global recession and the bursting of its housing bubble. Finance Minister Elena Salgado said following the report that Spain will probably contract again this quarter, although at a slower rate.



PSA Peugeot-Citroën plant in Vigo, Spain

Agence France-Presse/Getty Images

Spain's continuing recession shouldn't keep the region as a whole from expanding, thanks to expected strong third-quarter growth in Germany, France and Italy. But it does raise questions about 2010 and beyond. Spain, along with countries like Ireland and Greece that are smaller than the Big Three, has been "punching above its weight" by generating a good chunk of the region's growth, said James Nixon, chief European economist at Société Générale.

The ECB on Thursday outlined a fresh risk: Employment in the euro zone may continue to weaken after the economy recovers. Officials noted in their November bulletin that while the current recession is the worst since the 1930s, employment cuts have been muted by businesses reducing hours worked and "hoarding" labor.

"While this may contain the employment adjustment in the short term, experience of past crises suggests that large employment corrections tend to follow a financial crisis," the ECB said.

Officials also warned not to expect much of a direct boost in the euro zone from any U.S. recovery until as late as 2011. Although on average U.S. recessions tend to filter quickly to the euro zone, "it takes six quarters for an upturn to spill over," the ECB said.

—Daniel De la Puente contributed to this article.

CORRECTIONS & AMPLIFICATIONS

Volkswagen AG's preferred shares fell 16% on Tuesday. The European Stocks column Wednesday incorrectly quoted the common-share price, which was down 8%.

Saudi Arabia's Saad Group said in June it was restructuring debt amid a liquidity squeeze. A News in Depth article in the Oct. 23-25 issue incorrectly stated that Saad said it had defaulted amid liquidity problems. A Geneva prosecutor, not a court, has frozen some Saad assets. Lawyers for Ma'an al Sanea say that Saad National Schools, in addition to not being owned by Saad Group, isn't owned by Mr. Sanea. Sana'a al Gosaibi is the fourth daughter by one of her father's wives, not the eldest, and she owns stakes in a significant Saad division, not the group as a whole.

INDEX TO BUSINESSES

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

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INDEX TO PEOPLE

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

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

Medvedev urges economic, political change

Skepticism greets Russian leader's annual address

BY GREGORY L. WHITE

MOSCOW—Russian President Dmitry Medvedev renewed his calls to modernize his country's oil-dependent economy and open up the political system but gave no sign the Kremlin plans to loosen its tight control.

"The strengthening of democracy does not mean the weakening of law and order," Mr. Medvedev said Thursday in his annual address to parliament and top government officials. "Any attempts to rock the situation under democratic slogans, to destabilize the state and split society will be stopped."

On foreign policy, Mr. Medvedev struck a less confrontational tone than in last year's speech, which came shortly after Russia's war with Georgia and included threats to deploy new missiles on Russia's borders to counter a planned U.S. missile-defense system.

Calling for a "pragmatic" foreign policy, he said Russia needs to attract foreign capital, technology and ideas. "There's no point in puffing up our cheeks," he said. At the same time, he promised to buy a slew of new missiles, submarines and other weapons to upgrade Russia's military.

Associated Press

Russian President Dmitry Medvedev's annual address was broadcast to the nation, and in this Moscow store, Thursday.

The bulk of the 100-minute address was devoted to his calls for modernizing Russia's aging economy, a central theme of his rhetoric since he took office in the spring of 2008. "We still haven't gotten rid of the primitive structure of the economy," he said.

But even senior members of the ruling party are skeptical that the pledges to reduce dependence on the oil and other commodities that fueled Russia's recovery in the last few years will be backed up by real steps.

"We expected more," said an official of the ruling United Russia party. "What he said showed no sign that real actions will follow."

On economics, Mr. Medvedev pledged to reduce the state's role in the economy, but assigned the details of that work to the government of Prime Minister Vladimir Putin, who presided over a big increase in the state sector when he was president.

Polls show few Russians believe the annual addresses, which are covered live on state TV and heavily reported on the national news, have major policy impact.

Some analysts have interpreted Mr. Medvedev's sometimes-frank statements of Russia's problems as implicit criticism of his patron and predecessor, Mr. Putin. Aides to both men deny that.

Senior officials say Mr. Putin picked Mr. Medvedev as his successor to conduct a gradual and modest easing of control aimed at ensuring the system the two created will endure for years. Mr. Putin, who leads the United Russia party, hasn't ruled out a return to the presidency when Mr. Medvedev's term ends in 2012. One of Mr. Medvedev's first initiatives as president was to extend the presidential term for whomever is elected in 2012 to six years from four.

In his speech, Mr. Medvedev called for some limited changes to electoral rules he said were aimed at boosting political competition. But in recent weeks, he has also defended the results of regional elections held last month that even usually loyal opposition parties denounced as rigged in favor of the ruling party.

"We're talking about the systematic theft of votes at elections on all levels," said Sergei Mitrokhin, leader of the Yabloko opposition party. "The lack of a clear statement by the president on this essentially gives his blessing to falsifiers across the country."

Second legislative salvo could rescue Berlusconi

BY STACY MEICHTRY

ROME—Allies of Italian Prime Minister Silvio Berlusconi proposed a controversial bill that would establish time limits for criminal trials, a change that would help the premier with his legal troubles.

If the bill is approved by Parliament, where Mr. Berlusconi's party and its allies have the majority needed for passage, trials that don't reach a definitive verdict in six years would end automatically, according to a copy of the bill submitted to the Senate on Thursday.

Lawmakers in Mr. Berlusconi's People of Freedom Party say the bill will help speed up Italy's notoriously slow justice system. Criminal convictions here aren't considered definitive until a trial has been reviewed by three courts—a court of first instance, an appeals court and a high court—a process that can take more than a decade.

The proposed bill seeks to place a two-year time limit on each of the three trial phases. If approved, the legislation wouldn't apply to repeat offenders, crimes such as child pornography, and those that carry prison sentences of more than 10 years, such as murder.

It would mean that two criminal trials facing Mr. Berlusconi— which are expected to resume this month—would face automatic termination, according to Piersilvio Cipolotti, one of the premier's lawyers.

Critics called the bill part of Mr. Berlusconi's long-running efforts to challenge the authority of Italy's judiciary. The premier and his political supporters accuse prosecutors and judges of overstepping their powers in a politically motivated pursuit of Mr. Berlusconi.

"We cannot accept a reform tailor-made for the judicial needs of Berlusconi," said Rosy Bindi, a lawmaker with the left-leaning Democratic Party.

Italy's National Association of Magistrates said, "This reform will have devastating effects on how the criminal justice system functions."

Mr. Berlusconi has been indicted on allegations of corruption and tax fraud in two trials that began before his election to a third term in 2008. He has long denied the charges.

His government passed a law in July 2008 shielding the premier and other top state officials from criminal prosecution. Last month, however, Italy's Constitutional Court struck down the immunity bill, paving the way for Mr. Berlusconi's criminal trials to resume.

Earlier this week, an ally of Mr. Berlusconi's proposed a constitutional amendment that, if approved by Parliament, would reinstate immunity for all members of Parliament, including Mr. Berlusconi. The proposed amendment is unlikely to pass, however, because it requires a two-thirds majority vote in both the Senate and the lower house of Parliament, where the left-wing opposition commands enough votes to block the bill.

The measures introduced Thursday, however, only require a simple majority vote in both chambers to become law.

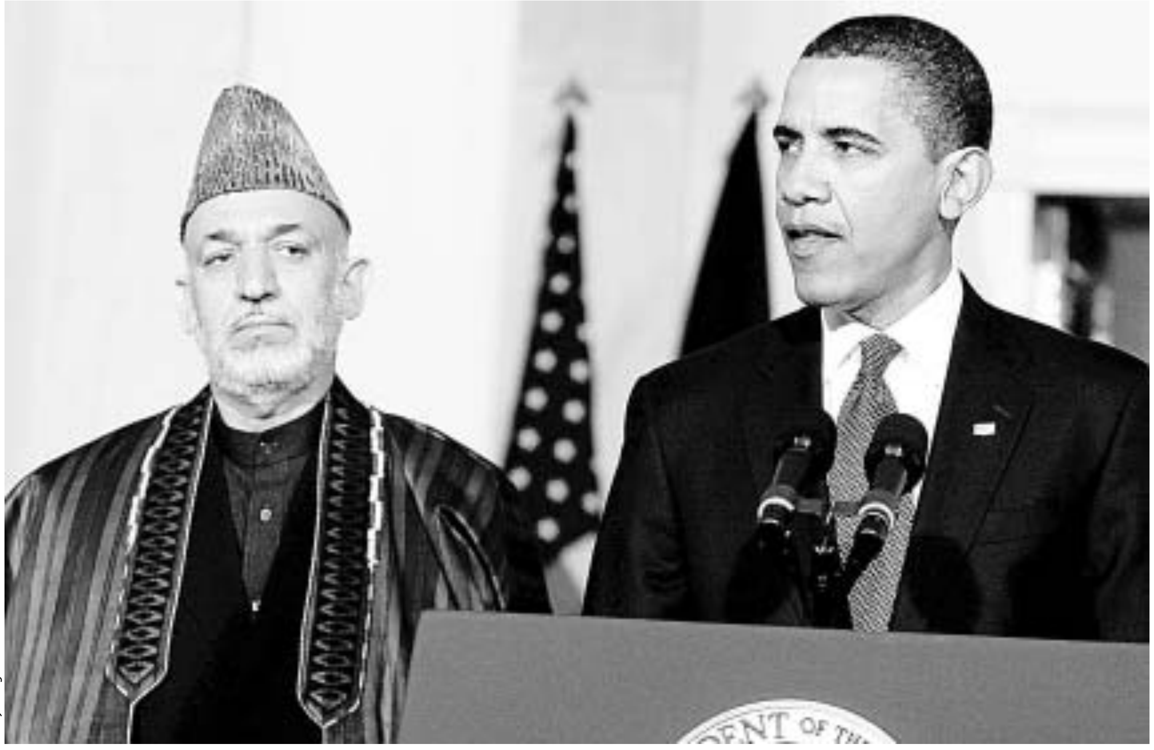
U.S. envoy opposes Afghan buildup

Cables that criticize Karzai complicate Obama's decision

By Peter Spiegel

U.S. President Barack Obama expressed fresh doubts about the credibility of Afghanistan's government in high-level discussions Wednesday over what troops to send there, after his ambassador to Kabul warned against any reinforcements until the Afghan regime cracks down on corruption.

U.S. Ambassador Karl Eikenberry sent two classified cables to Washington in recent days raising serious concerns about the military's recommendation to increase troop levels, according to three U.S. officials. Mr. Eikenberry criticized Afghan President Hamid Karzai's recent behavior as well as corruption in the top ranks of his administration, according to an official who saw the memos. Mr. Karzai has in recent interviews lashed out at the U.S. and blamed corruption on international organizations working in his country.



Getty Images

President Barack Obama expressed fresh doubts about the credibility of the government of Afghan President Hamid Karzai, left.

In Wednesday's meeting, which Mr. Eikenberry attended via videoconference, Mr. Obama discussed four options for adding troops for nearly 2½ hours. Two of the options were previously proposed by his top commander in Afghanistan, Gen. Stanley McChrystal. A new "hybrid" option has recently gained momentum at the Pentagon, and would send 30,000-35,000 troops including up to 10,000 trainers to improve Afghan forces' capability to secure the country themselves. A smaller compromise plan also would focus heavily on training, but with around 20,000 troops in all.

A White House official said Mr. Obama made requests that could lead to significantly altering any or all of the choices, changing the number of troops involved and the length of their deployment. The official said Mr. Obama asked for specific timelines in each scenario for when U.S. troops would turn over security to Afghan forces. In the past, senior military officials have resisted such timelines.

The key points of contention, the official added, were the timelines and questions about the credibility of the Karzai government—issues raised by Mr. Eikenberry and others. The ambassador has warned that an increased U.S. presence could take pressure off the Afghan government to take over security. Mr. Eikenberry's cables were first reported by the Washington Post on its Web site.

Mr. Eikenberry is a retired three-star general who commanded U.S. forces in Afghanistan from 2005 to 2007, so his views on troop levels are likely to carry weight. But Mr. Eikenberry is known to have a prickly relationship with Mr. Karzai dating back to that period, and earlier this year that forced Sen. John Kerry to become the U.S. go-between with the Afghan president.

Wednesday's meeting was the last of several of Mr. Obama's war council before he left for an Asia trip; some officials have said he aims to make a decision soon after he gets back Nov. 19, though deliberations could continue into next month.

Other administration officials have begun to fan out to get feedback from allies: According to officials familiar with the effort, James Jones, the White House national security adviser, is expected to visit Pakistan this week to discuss U.S. deliberations over troop levels.

Mr. Eikenberry's concerns come late in the process, and it is unclear how they will ultimately affect Mr. Obama's decision making. Defense Secretary Robert Gates recently has backed the "hybrid" plan for 30,000 to 35,000 troops, and has emerged as the key adviser within the administration.

Senior officers at the Pentagon including Adm. Mike Mullen, chairman of the Joint Chiefs of Staff, continue to back Gen. McChrystal's recommendation to send more than 40,000 troops. But according to a military official, they are increasingly throwing their weight behind the hybrid plan backed by Mr. Gates, as a way to get Gen. McChrystal most of what he needs.

Many of Mr. Eikenberry's concerns about Mr. Karzai have been raised by others involved in the White House deliberations, including by Mr. Obama.

Administration officials have pushed hard to get Mr. Karzai to come up with a checklist of "deliverables" that would illustrate he is cracking down on corruption after his inauguration, scheduled for Nov. 19.

According to a senior administration official familiar with the efforts, they have included a push for the Afghan president to fill top cabinet positions with competent technocrats, rather than rewarding warlords who backed Mr. Karzai's re-election, such as Uzbek strongman Abdul Rashid Dostum.

"The president believes that we need to make clear to the Afghan government that our commitment is not open-ended," said a White House official briefed on Wednesday's meeting. "After years of substantial investments by the American people, governance in Afghanistan must improve in a reasonable period of time to ensure a successful transition to our Afghan partner."

—Jay Solomon, Alan Cullison and Siobhan Gorman contributed to this article.

Allies to send more resources to Afghanistan

Associated Press

LONDON—Allied countries are pledging to send more help to Afghanistan before a much anticipated decision from U.S. President Barack Obama on whether to send more troops, according to the secretary-general of the North Atlantic Treaty Organization.

Anders Fogh Rasmussen agreed with British Prime Minister Gordon Brown that handing over parts of the volatile Helmand province to Afghan national forces could start as early as June, but he said more resources and help from the Afghan government were needed.

"We need to train and educate Afghan soldiers and police with the aim to hand over responsibility to the Afghans themselves—province by province as capacity develops," Mr. Rasmussen said.

Britain has offered to add 500 troops to its 9,000 contingent if the Afghan government cleans up corruption and other allied countries provide resources. Turkey has already boosted troops but in a humanitarian capacity, not combat.

Waning public support for the mission has kept other allied nations from publicly committing to more troops, but Mr. Rasmussen said private pledges were being made. "We have already received quite a number of pledges, and I would also encourage allies to follow suit and welcome the British decision to add troops," he said. "Based on this principle of solidarity, I think all allies will follow suit."

It was unclear how many countries had made commitments or whether pledges would be in the form of troops or training personnel. NATO commanders in Afghanistan have called for an additional 30,000 troops, but Mr. Rasmussen said numbers hadn't been finalized.

He said allies understood the importance of the mission. "I think that all governments realize that we are in Afghanistan to prevent the country from once again becoming a safe haven for terrorists. If we leave Afghanistan behind, terrorism would easily spread from Afghanistan through central Asia and further to destabilize Pakistan—a nuclear power—and that would be a very dangerous situation."

Abbas gets a way to retain power

By Charles Levinson

JERUSALEM—Palestinian election officials said they can't hold planned elections in January, which would give President Mahmoud Abbas a way to stay in office despite his threat to stand down, but which could further roil Palestinian and Israeli politics.

Mr. Abbas's threat and a wider breakdown of U.S.-led peace efforts are beginning to take a toll, both in the Palestinian territories and on Prime Minister Benjamin Netanyahu's government in Israel, which has come under fire, including from within the Israeli leader's ruling coalition, for not making headway toward peace.

Speaking at a televised news conference in Ramallah, the election officials blamed Hamas's opposition to the polling as their main obstacle. Hamas has rejected holding new elections until after reaching a long-stalled reconciliation accord with Mr. Abbas's Fatah Party.

"We planned to go to Gaza to figure out how we can conduct elections there," said Hanna Nasser, head of the Palestinian Elections Commission. "We received an answer from Hamas that we are not welcome in Gaza. It is clear now that we cannot hold an election in Gaza."

If Mr. Abbas accepts the commission's recommendation, it could allow the embattled Palestinian leader to remain in office. Last week, he threatened not to stand for re-election due to frustrations over the stalled peace process.

Calling off elections could present a mixed blessing for U.S.-led peace efforts, analysts say. A Palestinian government that remains in power without scheduled elections could appear to have less legitimacy to make concessions in peace negotiations with Israel.

Still, there is no obvious candidate to replace Mr. Abbas at the helm of the Palestinian Authority, and were he to stand down, it could throw the Obama administration's peace efforts into further disarray.

A senior administration official said cancelling elections wouldn't have a significant impact on U.S. peace efforts.

Another option available to Mr. Abbas would be to call for elections only in the Fatah-controlled West Bank, Abbas' Chief of Staff, Rafiq al-Husseini, said.

"He doesn't have to accept the recommendation," Mr. Husseini said of Mr. Abbas. "We should not be held hostage by Hamas and allow them to stop our democratic process."

Many Palestinian officials, however, fear holding elections only in the West Bank would further entrench the two-year-old split between the Hamas-ruled Gaza Strip and the West Bank, where Fatah is in control.

Getty Images

Palestinian President Mahmoud Abbas in Hebron, Sunday. After he said he won't seek another term, election officials recommended canceling a January vote.

The floundering peace process is posing problems for Mr. Netanyahu as well. Following a frosty reception at the White House on Monday, the Israeli leader returned home to Israeli newspapers proclaiming relations with Washington in crisis. They widely circulated reports that U.S. officials voiced disappointment with Mr. Netanyahu because his speech to an assembly of Jewish Federations earlier on Monday hadn't included any new concrete steps to advance peace efforts.

LEADING THE NEWS

U.K. investigates hedge-fund group

Move underscores Serious Fraud Office's growing interest in the investment industry

By Cassell Bryan-Low

LONDON—The U.K.'s Serious Fraud Office said it has opened an investigation into hedge-fund manager **Dynamic Decisions Capital Management** Ltd., underscoring the agency's increased focus on hedge-funds.

The SFO said Thursday that the investigation followed complaints made to the agency and regulators at the Financial Services Authority in connection with the firm's flagship fund, Dynamic Decisions Growth Premium Master Fund Ltd. The Cayman Islands-registered fund, which went into liquidation earlier in the year, includes among its directors a member of the Nobel family.

Dynamic Decisions Capital Management, in a statement, said the events that led to the liquidation were "a reasonable response to unprecedented [market] conditions." The management company previously has said that its founder, Alberto Micalizzi who ran the flagship fund, believes he acted in the best interests of investors and that he believes that complex bonds held by the fund "are genuine and have value."

Mr. Micalizzi, a 41-year-old Italian finance academic who lives in London and Milan, launched the fund in 2005 focusing largely on equities but switched its focus in late 2008. Mr. Micalizzi, who continues at the management company, said in an interview Thursday that the FSA told him in early March that the firm was "under supervision" and that he has been co-operating with them. He added that the SFO's move, which he became aware of Thursday morning when he saw the SFO's announcement, came as a surprise. The SFO said it started its inquiry following an FSA referral.

Investor complaints have focused on a significant investment in bonds by the fund late last year, people familiar with the matter said. Investors were caught off guard by the sudden change in investment strategy and were nervous about the complicated structure of the bond investments, the people said.

Mr. Micalizzi said that following the turmoil in the financial markets in the fall of 2008, he decided to switch the fund's focus to bonds from stocks. He invested principally in asset-backed bonds that were convertible into oil, which he says was a bid "to protect the fund against this unpredictable volatility." The guarantor was a private Australian company that owned an allocation in Russian-sourced oil pledged to the bond, Mr. Micalizzi said.

> **Mr. Micalizzi launched the fund in 2005 to focus largely on equities, but switched focus in late 2008.**

Investors clamored for the exit. They requested withdrawals of at least 40% of the fund's roughly $500 million in value as of the end of 2008, according to Mr. Micalizzi. At the time, he held mostly hard-to-sell assets, namely the bonds.

Mr. Micalizzi said he had found a potential buyer for the bonds but that the board rejected the offer. "My own interpretation is that one or two directors became particularly concerned when one or two investors sent complaint letter complaining about the delay in redemptions," he said.

Among the fund's four directors is Michael Nobel, a descendant of the 19th century Swedish chemist and investor Alfred Nobel, whose will established the Nobel prizes. Mr. Nobel and the fund's three other directors couldn't immediately be reached.

The board asked Mr. Micalizzi to resign from the fund's board, which he did in late February, Mr. Micalizzi said Thursday. Soon after, the board held a conference call with investors and said they weren't able to provide an accurate value of the bonds, according to Mr. Micalizzi, who wasn't on the call but says he heard about it through others and has viewed a transcript of the call.

Mr. Micalizzi said he has been working with the court-appointed liquidators and believes he has found a potential buyer for the bonds.

Grant Thornton UK LLP, which was named the fund's official liquidator by a Grand Cayman court in May, said in a statement that allegations have been made that "these bonds not only fell outside the parameters of the mandated investment strategy of the Fund, but that the bonds had no real value." It confirmed that there have been talks with a potential buyer "at a substantial portion of face value," but that a deal hasn't yet been completed.

Grant Thornton has said the fund had about $550 million in unaudited assets on Dec. 31. The Dynamic Decisions Growth Premium Master Fund delisted its shares from the Irish Stock Exchange a year ago.

—Devon Maylie contributed to this article.

CORPORATE NEWS

Peugeot-Citroën's profit strategy

French car maker to cut costs, target high-growth markets to bolster its net

By David Pearson

VELIZY-VILLACOUBLAY, France—French car maker **PSA Peugeot-Citroën** on Thursday unveiled a three-year, €3.3 billion ($4.94 billion) plan to improve its profitability that relies on cost savings and increasing sales in high-growth markets.

Chief Executive Philippe Varin, in a presentation to analysts and journalists, said the plan aims to close the profitability gap between Peugeot-Citroën and the five best players in the industry.

Europe's second-largest automotive group after Germany's **Volkswagen** AG estimates that its average operating margin lags those of the five top car companies by six percentage points. It aims to achieve a gain of €3.3 billion in operating profit between 2010 and 2012.

Chief Executive Philippe Varin, in a presentation to analysts and journalists, said 55% of the improvement will come from cutting production, development and overhead costs. A further 30% will come from sales and marketing efforts, and the remainder from sales in high-growth markets.

Peugeot-Citroën earlier raised its full-year operating-profit guidance to break even due to the success of its new models and the recent improvement in auto markets.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PSA Chief Executive Philippe Varin with a Peugeot 5008 last month. PSA has raised its full-year profit projection.

Analysts had been expecting the company to report a full-year operating loss of around €1 billion, in line with its earlier guidance. In the first half, Peugeot-Citroën reported an operating loss of €826 million and a net loss of €962 million.

The company's sales of smaller cars have been boosted this year by government incentives.

Over the first nine months of the year, Peugeot-Citroën's sales in Europe fell 6.6%, in line with the overall market. Sales rose 6.8% on a year-to-year basis in September. Peugeot-Citroën said output in the fourth quarter is now expected to be 17% higher than the third quarter and 30% higher than a year earlier.

—Geraldine Amiel contributed to this article.

Porsche reports $6.6 billion loss on VW options

By Christoph Rauwald

FRANKFURT—**Porsche** Automobil Holding SE said Thursday it swung to a €4.4 billion ($6.6 billion) pretax loss in fiscal 2009 related to its stake in **Volkswagen** AG.

Porsche said the loss in the 12 months ended July 31 was mainly because of a write-down recognized for the cash-settlement options on VW shares. The size of the write-down wasn't disclosed.

Cash-settled options are financial instruments where the owner doesn't receive the actual share when exercising the option, but instead receives the difference between the share's cash value and the price when the option is exercised.

Porsche reaped windfall profits over the options valuations since 2005, when it started building up the VW stake. But when Porsche's net debt ballooned in tightening credit markets, investors were increasingly questioning Porsche's ability to exercise the options.

The ill-fated attempt to gain full control of VW backfired earlier this year. Porsche was effectively forced to enter talks over a combined enterprise under VW's leadership. Porsche later sold many of the options to Qatar, which is set to be the third-biggest shareholder in the combined company.

BMW plans to build a second plant in China

BMW AG said it would build a second plant in China with its local joint-venture partner, making the German company the latest foreign auto maker to increase its presence in the rapidly growing Asian market.

By ***Christoph Rauwald*** *in Frankfurt and* ***Patricia Jiayi Ho*** *in Shanghai*

The German luxury-car maker said Thursday that it and partner **Brilliance Automotive Holdings** Ltd. plan to spend €560 million ($836.6 million) on the plant, which is to begin making cars in 2012. The factory will increase BMW's production capacity in China to 100,000 cars a year from 41,000.

China is poised to surpass the U.S. this year as the world's largest car market.

Foreign auto companies have seen rapid growth there this year, even as sales have plunged in more established markets.

Thursday, Dong Yang, executive vice chairman of the China Association of Automobile Manufacturers, said overall auto sales in the country could reach 13 million vehicles this year, up from 9.38 million last year.

Already, in the first nine months of 2009, China's vehicle sales rose 34% from a year earlier to 9.66 million, amid a faster-than-expected recovery in the world's third-largest economy.

Other foreign car companies have been expanding production in China. **General Motors** Co. last December opened a passenger-vehicle plant in northeastern China. **Ford Motor** Co. in September announced plans to build its third car-assembly plant in China.

Guangzhou Automobile Industry Group Co. said Thursday that it is considering expanding the capacity of its China joint venture with **Honda Motor** Co. "Our capacity usage at Guangzhou Honda has already reached 100%," Guangzhou Auto Chairman Zhang Fangyou said.

China already is the fourth-largest single market for BMW, the world's best-selling premium auto maker by sales. But BMW and Mercedes-Benz manufacturer **Daimler** AG are playing catch-up in China with smaller rival Audi. Audi's parent company, **Volkswagen** AG, was an early entry into the market, giving it a leg up.

BMW sold 71,952 vehicles in China in the first 10 months of the year, up 37% compared with 52,622 cars sold in the same period last year and exceeding the full-year sales volume from 2008 already.

The German company and its Chinese partner so far have invested about €450 million in the Chinese venture, which has produced approximately 150,000 vehicles since it was established in 2003.

The new plant will add around 1,000 jobs to the 3,300 existing jobs at the joint-venture site, in the northeastern city of Shenyang.

"Our plant has reached its capacity limit, so we are now taking the next step," BMW Chief Financial Officer Friedrich Eichiner said in announcing the new plant.

Maersk loss signals slow shipping recovery

Company lost $778 million in nine months as trade gained but excessive boat building kept taking toll

By John W. Miller

A.P. Moller-Maersk AS reported a hefty loss for the first nine months of the year, a sign that shipping will recover at a slower pace than trade as an excessive shipbuilding spree keeps taking a toll.

Copenhagen-based Maersk said Thursday it lost $778 million for the period. Maersk, the world's biggest shipping company by volume, posted a profit of $3.5 billion a year earlier. Analysts had forecast roughly a $700 million loss.

Maersk expects to lose $1 billion this year.

"This is a worse development in the container market than we expected," said Jacob Pedersen, an analyst with Denmark's Sydbank AS.

Revenue from Maersk's oil and gas units is expected to stay flat from last year.

Shipping usually tracks trade closely because 90% of goods are moved on the seas, but that's not the case now.

Trade is recovering: The International Monetary Fund expects a 2.5% increase next year after an 11.9% drop in 2009. But shipping revenue is expected to lag behind because of deflated prices charged for moving containers.

Maersk's prices have fallen 32% on average from last year as volume fell just 3%, said Maersk Chief Executive Nils Smedegaard Andersen.

The industry's average price to move a 40-foot container on the world's 42 main shipping routes was $2,040 in September, down 17% from a year earlier, according to Drewry Shipping Consultants Ltd., a London-based consulting firm.

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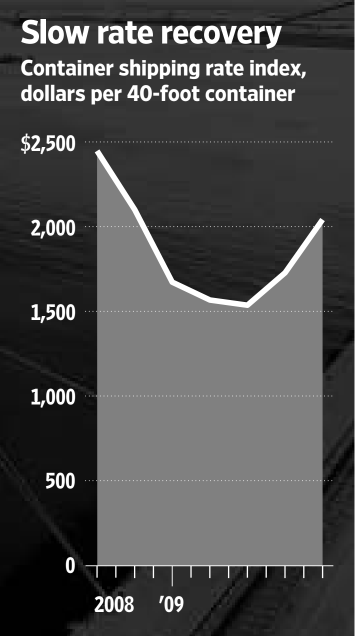

Note: Index compiled from rates on 42 major maritime routes
Source: Drewry Shipping Consultants Ltd.

Pictured, an A.P. Moeller-Maersk A/S container ship in Rotterdam

Maersk's ills are emblematic of an industry that bet heavily on the trade boom early this decade. Companies ordered so many vessels that shipyards still have to deliver the equivalent of 40% of the world's current fleet, according to analysts.

"There's just no way the market can absorb all that," said Drewry analyst Philip Damas. "People are losing serious money in the container business right now."

Maersk and other carriers have responded by laying off staff, circumnavigating the expensive Suez Canal and docking some ships while canceling orders for others.

But that's not enough. Mr. Andersen said he expects "the container market and the tanker market—the shipping industry in general—will remain under pressure in 2010." Even recent price increases will be cold comfort. "Rates are edging back up, but they are still below the entry level of 2009," he said, and they aren't rising faster than fuel costs.

Sydbank's Mr. Pedersen said it will take time for the effects of rate increases to trickle down to the bottom line. "Shipping companies often secure contracts months in advance."

Maersk isn't the only carrier experiencing major difficulties. **Neptune Orient Lines** Ltd., the world's fifth-biggest container carrier, projected a loss of $636 million this year. German container port operator **HHLA** AG said its 2009 container revenue would fall 30%.

Hyosung abandons Hynix bid

By Jung-Ah Lee

SEOUL—South Korean conglomerate **Hyosung** Corp. dropped its bid to buy a controlling stake in **Hynix Semiconductor** Inc. valued at $2.76 billion, forcing the chip maker's creditors to restart its search for a buyer.

Hyosung, a South Korean conglomerate with businesses in textile, chemicals and heavy machinery, said Thursday that because of rumors and speculation that it had received preferential treatment to buy Hynix, it had abandoned its offer for a 28% stake in the chip maker. At current prices, that stake is worth 3.2 trillion South Korean won.

Creditors will target a domestic buyer for Hynix, said **Korea Exchange Bank**, the chip maker's largest shareholder.

Shares in Hyosung surged by their 15% daily limit to close at 79,100 won on the news of the dropped bid.

Hynix shares closed 1.8% lower at 19,600 won.

In 2001, Hynix nearly collapsed under the weight of its debt after chip prices plunged.

It was bailed out by creditors including Korea Exchange Bank and Korea Development Bank, which became the company's shareholders via several debt-to-equity swaps.

Hynix declined to comment on Hyosung's withdrawal, but Chief Executive Kim Jong-kap said the chip maker will continue to work at improving its business.

Hynix posted a third-quarter net profit on a rebound in chip prices after seven consecutive quarters of losses and financial support from its shareholders, including loans, as well as extensive restructuring.

Hyosung's pullout came amid ongoing market speculation over whether the company had the management capability to control Hynix, which is about four times bigger by market capitalization.

Wal-Mart net rises despite weak sales

By Karen Talley
And Ann Zimmerman

Wal-Mart Stores Inc. executives Thursday forecast a particularly competitive holiday season for retailers as customers continue to worry about their finances and jobs.

The world's largest retailer is using discounts on everything from turkeys to Xbox 360 videogame consoles to increase visits ahead of Nov. 27, the traditional start of the U.S. holiday shopping season.

Wal-Mart's recent move to sell 10 hotly anticipated books and DVDs on its Web site at heavy discount resulted in "record hits" to Walmart.com, the company's treasurer, Charles Holley, said Thursday after the retailer released record results for its fiscal third quarter. He said the company doesn't expect to lose money on those sales.

Wal-Mart reported a 3.2% gain in earnings for its fiscal third quarter, but it offered a guarded holiday outlook, citing the effect of deflation in food and electronics. Its sales at U.S. stores open at least a year fell 0.4%, only the second quarterly decline in the last two years.

"We recognize that some customers may be more cautious in their holiday spending," Wal-Mart U.S. chief Eduardo Castro-Wright said in a conference call.

Wal-Mart projected fourth-quarter sales at U.S. stores open at least a year will be flat to down 1% for the current quarter. Such sales, a key measure of retail health, rose 2.4% in last year's fourth quarter.

The company, based in Bentonville, Ark., forecast fourth-quarter profit of between $1.08 and $1.12 a share.

Wal-Mart reported third-quarter profit of $3.24 billion, or 84 cents a share, up from $3.14 billion, or 80 cents a share, a year earlier. In August, the company projected earnings of between 78 cents and 82 cents a share in the third quarter.

Net sales increased 1.1% to $98.67 billion and rose 3.8% excluding currency-exchange effects.

Vivendi is still optimistic about growth this year

By Ruth Bender

PARIS—**Vivendi** SA posted a 78% drop in its third-quarter net profit following year-earlier results that included a hefty gain, but said it still expects to record strong earnings growth this year.

Chief Financial Officer Philippe Capron said 2009 has been proving more challenging than expected, even though the recession has been having only a slight impact on Vivendi because of its customers' preference for staying home to watch pay-TV and play videogames.

Mr. Capron declined to say whether Vivendi would sell its 20% stake in NBC Universal to parent **General Electric** Co. or whether the group is considering raising its offer for Brazilian telecoms operator GVT Holding, topics that have been at the heart of press speculation.

Sunday begins Vivendi's annual three-week window that allows it to sell its stake in television and movie company NBCU either on the market or to GE. But the conglomerate has been silent about its intentions. GE, which owns the remaining 80% of NBCU, is in advanced talks with **Comcast** Corp. for a deal to merge Comcast's cable networks with NBCU. The deal hinges on Vivendi's selling its stake.

For the latest quarter, the Paris-based entertainment-to-telecom conglomerate, which also owns Universal Music Group, said net profit came to €600 million ($892 million), compared with €2.76 billion a year earlier. Last year, net profit was boosted by a €2.32 billion financial gain stemming from how Vivendi's stake in its games division was accounted for after it merged with Activision Inc. to create **Activision Blizzard** Inc.

Vivendi's revenue, meanwhile, fell 2.5% to €6.35 billion.

Adjusted earnings before interest and tax, or Ebit, the figure analysts follow to gauge Vivendi's operating performance, rose 5.1% to €1.35 billion. Universal Music Group, the world's largest music publisher, reported adjusted Ebit of €58 million, down 61% mainly because of a sharp drop in recorded music sales.

CORPORATE NEWS

AB InBev reports a slide in sales

With weak spots around world, brewer's earnings get a boost from cost-cutting

By Matthew Dalton

Brewing giant **Anheuser-Busch InBev** said cost-cutting bolstered earnings in the third quarter, but its sales slowed in the face of the global recession, showing the company is still struggling to sell more beer following last year's takeover of Anheuser-Busch.

Sales volumes fell 5.1% from the year-earlier quarter. That number is coming under more scrutiny now that AB InBev has reached a number of milestones related to the merger: cutting costs, selling assets to pay down debt and refinancing short-term debt.

Net profit totaled $1.55 billion, up from $690 million a year earlier. The quarter included $414 million of one-time gains, mostly from selling Korean assets.

InBev executives hinted that AB InBev would now focus on boosting sales through one of the merger's long-term goals: selling more Bud brand beers outside the U.S.

"We clearly see the potential to bring that brand across the different markets where we operate and where we have a strong sales and marketing platform in place," said Chief Financial Officer Felipe Dutra in a conference call Thursday.

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AB InBev aims to sell more Bud brand beers outside the U.S. Above, a bartender poured a glass of Budweiser in Brussels.

Cost-cutting has always been a main goal of the merger, which executives said would succeed even if the company didn't sell an extra drop of Bud outside the U.S. The company said it is on track to cut $2.25 billion in costs by the end of 2010. Analysts say now is the time for InBev to invest in its most valuable brands—Bud, Stella Artois and Beck's—or risk losing market share.

Sales fell 10% to $9.76 billion, due to lower sales volumes and the impact of fluctuating currencies, particularly the Brazilian real against the dollar.

The lower sales were driven by weak results in the U.S. and Central and Eastern Europe. The performance in Russia, where sales volumes plunged 20% in the quarter, and Ukraine is particularly worrying, analysts said.

Earnings before interest, taxes, depreciation and amortization—adjusted for one-time items—were $3.55 billion, flat compared the year earlier. Cost-cutting kept profits from declining despite lower sales. Analysts were expecting adjusted Ebitda of $3.50 billion.

AB InBev didn't provide pro forma net profit figures for the third quarter of last year, which occurred before the Anheuser deal closed in November 2008.

Telefónica, BT trim costs as sales drop

By Jason Sinclair

MADRID—**Telefónica** SA and **BT Group** PLC Thursday capped off an earnings season notable for sharp cost cutting by telecommunications operators, as revenue remained under pressure, particularly in their moribund European home markets.

Telefónica, Europe's largest telecommunications company by market value, said net profit fell slightly in the three months ended Sept. 30 to €1.99 billion ($2.98 billion) from €2 billion a year earlier.

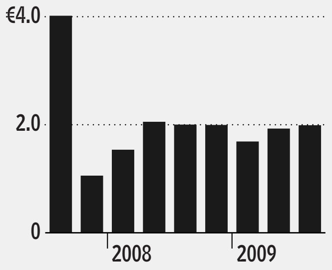
Revenue declined 5.7% to €14.13 billion from €14.99 billion, but the Madrid-based company slashed operating expenses by 6.5% to €8.73 billion. For the year's first nine months, capital spending dropped 19% from a year earlier to €4.38 billion.

Telefónica's move to cut expenditures and costs in order to keep its pledges to shareholders mirrors moves by other European rivals.

"The company's drop in capital expenditure is significant, and if Telefónica can keep it at this level for the rest of the year, it will be key in maintaining a strong cash flow," said Banco Español de Crédito analyst Juan Tuesta.

Calling in profits

Telefónica's net profit, in billions of euros



Source: the company

Newbury, England-based **Vodafone Group** PLC, the world's largest mobile operator, on Tuesday reiterated its forecast, thanks chiefly to cost cutting, and doubled its savings target, following similar cost restraint from Deutsche Telekom AG, France Télécom SA and others.

In October, Telefónica pledged to increase shareholder returns with higher dividends, but it has revised down its forecast for 2012 and has ruled out any new share buybacks in the near future.

In Spain, revenue dropped 9% to €4.9 billion as the company lowered prices and was hit by regulation that has cut the fees operators charge each other to connect calls.

In Europe, where Telefónica operates under the O2 brand outside Spain, revenue fell 5.5% to €3.48 billion.

Revenue in Latin American markets also fell in the third quarter, slipping 2% to €5.65 billion.

To maintain its foothold in key markets, Telefónica has been making selective acquisitions to beef up operations. This month, the company raised its bid for Brazilian telecommunications company GVT, topping an earlier offer from French media titan **Vivendi** SA, and it also bought German broadband operator Hansenet from **Telecom Italia** SpA.

Meanwhile, BT, also reporting earnings Thursday, raised its cost-savings target for the fiscal year ending March 31. Its fiscal second-quarter earnings beat expectations, rising 13% to £428 million ($716 million), thanks to lower operating costs and finance expenses. Revenue for the three months ended Sept. 30 fell 4.3% to £5.07 billion.

London-based BT increased its cost-saving target by about one-third to at least £1.5 billion, and now expects revenue to drop 3% to 4%, compared with its original forecast for a decline of 4% to 5%. It also expects capital expenditure to fall to around £2.6 billion, less than its previous £2.7 billion estimate.

Telekom Austria AG was also a tale of cost restraint—the company Thursday missed views because of a write-down and now has to cut capital spending to meet its cash-flow target. Telekom Austria's net loss for the three months ended Sept. 30 was €136.2 million, compared with a net profit of €162.9 million in the year-earlier quarter.

—Lilly Vitorovich in London and Flemming Hansen in Vienna contributed to this article.

'Call of Duty' game rakes in $310 million in one day

By Yukari Iwatani Kane

The videogame market has a new high scorer: "Call of Duty: Modern Warfare 2."

Activision Blizzard Inc. said first-day sales of the game, its much-anticipated shoot-'em-up title released Tuesday, hit 4.7 million copies in the first 24 hours in North America and the United Kingdom.

That topped the previous record holder, **Take-Two Interactive Software** Inc.'s "Grand Theft Auto IV," which reported 3.6 million units world-wide on its first day of sales last year. Activision said first-day sales of its game were $310 million in North America and the U.K.

Modern Warfare 2's strong initial sales are a bright spot in an industry that has been suffering from weak consumer demand so far this year. Evan Wilson, an industry analyst for Pacific Crest Securities, estimated that Activision, which distributes the game developed by Infinity Ward, sold 6.5 million copies of Modern Warfare 2 world-wide on opening day.

Still, Mr. Wilson said, it would be impossible to generalize about overall holiday videogame sales based on this single game. "This is one of those titles that will sell in any economic environment," he said.

Modern Warfare 2 features Russian ultranationalists who want to wreak havoc on the world and is the latest in the Call of Duty series, which was first released in 2003.

The early games took place during World War II. But the developer changed the setting to current times in "Call of Duty 4: Modern Warfare," released two years ago. That switch resounded with game players, many of whom still play it now.

Part of the game's appeal is that players take on different roles as they experience a realistic conflict from many perspectives, such as that of an American or British soldier who fights the enemy with an array of modern weapons.

The first Modern Warfare had sales of six million copies in its first quarter on the market, according to research by Wedbush Morgan, a brokerage firm. Modern Warfare 2 is its sequel. Retailers have been competing heavily for sales of the game as they head into what is expected to be a tough holiday season.

TeliaSonera, Alfa seek tie for MegaFon and Turkcell

By Gustav Sandstrom And Will Bland

MOSCOW—Russia's **Alfa Group** and Sweden's **TeliaSonera** AB agreed Thursday to combine stakes to create a U.S.-listed company with control over two of the largest mobile firms in Russia and Turkey.

If approved, the deal will mark a victory for the Russian conglomerate and the Swedish telecom operator, which will join forces in a battle with Turkey's **Turkcell** AS co-investor Cukurova Group, and also seek to unlock the value of their multibillion stakes in privately held Russian operator OAO **MegaFon**.

The agreement comes a month after Alfa ended a five-year legal battle with Norway's Telenor ASA with a similar merger of mobile business. Alfa, which has a reputation for aggressive negotiating, has fought against TeliaSonera in the past, and analysts warned that Thursday's proposal might be opposed by other major shareholders in Turkcell and MegaFon.

Alfa and TeliSonera own a combined 69% in MegaFon, Russia's third-largest operator, and 42% of Turkey's largest operator, but the two investors are in legal disputes with their Turkish co-investor over other shares.

TeliaSonera Chief Executive Lars Nyberg told Dow Jones Newswires the agreement will make it possible to agree on a dividend policy for both MegaFon and Turkcell. The Russian operator has never paid dividends and at the end of 2008 held $1.4 billion in cash and equivalents.

The new company will be listed on the New York Stock Exchange within one to two years, Mr. Nyberg said, adding that Turkcell's and MegaFon's operations will be largely unaffected by the agreement.

The chief executive of Alfa's telecoms unit, Alexei Reznikovich, said there is much left to negotiate before the stakes can be merged, in contrast to the recent deal with Telenor. "This is more of a framework agreement," he said, adding that the most significant step with TeliaSonera is the decision to coordinate legal strategy.

Russian regulators monitor closely any changes in ownership in the telecom sector, and may want to stop Megafon coming under the control of a company based outside Russia. Mr. Reznikovich said that Russian regulators have been consulted about the proposal, but that they won't be able to approve it until TeliaSonera and Alfa sign a definitive agreement on the combination of their stakes.

TeliaSonera owns 44% of MegaFon and 37% of Turkcell. These non-controlling stakes "have been a bugbear of [TeliaSonera's] investment case for a long time," said Societe Generale, noting Thursday's agreement was complicated but "a major positive step."

"The purpose is to create a leading international operator, with over 90 million subscribers in Russia, Turkey and the CIS countries, and with well functioning corporate governance," TeliaSonera said.

MegaFon's second-largest shareholder, **AF Telecom**, has told Russian media it isn't keen on a merger between MegaFon and Turkcell.

Fed seen lifting rates around September

Survey of economists points to move before U.S. election, a politically sensitive time; continued high joblessness projected

By Phil Izzo

Economists in the latest Wall Street Journal survey on average expect the Federal Reserve to raise interest rates around September 2010, a politically sensitive time in the U.S. considering midterm elections will be right around the corner, and unemployment is forecast to still be over 9.5%.

The 52 surveyed economists—not all of whom answer every question—on average expect the unemployment rate to rise to 10.3% by the end of this year from its current 10.2%, and they expect it to stay above 9.5% through 2010. The respondents expect job growth to return over the next 12 months, but the forecast calls for an average of about 50,000 jobs to be added per month over that period. The economy needs to add about 100,000 jobs a month just to keep up with new entrants to the labor force.

"The small-business sector is still under pressure, and larger companies are still focused on bolstering current results rather than preparing for the future," said Lou Crandall at Wrightson ICAP. Productivity gains and cost cuts have allowed companies to boost their bottom line without adding staff.

The economists expect gross domestic product to expand around 3% at a seasonally adjusted annual rate through 2010, slightly slower than the 3.5% recorded in the third quarter. The forecast represents solid growth but remains at a level too low to add the number of jobs needed to make up for the eight million cuts recorded so far in this recession.

The last time the unemployment rate topped 10%—in the 1980s—the following six quarters posted average growth of more than 7%, but only managed to bring the jobless rate down by about three percentage points.

Despite the challenges, confidence is running high in the Fed to manage the economy. Thirty of 50 economists who answered the question said that the central bank will raise interest rates at the right time, while 18 said the Fed will be too slow. That contrasts with widespread criticism of the Fed's timing in the past. In the March 2008 survey, 80% of respondents said the central bank was too slow to raise rates in 2003, and Fed Chairman Ben Bernanke has been accused of being slow to cut rates at the start of the financial crisis.

But that doesn't mean an increase in rates is imminent. Most economists said the Fed won't raise rates until the third quarter of 2010 at the earliest. Futures markets are putting 90% odds of a rate increase in August next year.

"After a year of growth, the portion of the easing meant to curtail depression will be taken away," said Dean Maki of Barclays Capital. But "the Fed is unlikely to raise rates until the unemployment rate is on a decisive downward trend."

If the Fed raises rates in September, it would come just six weeks before the midterm election. The central bank values its independence from the political process, especially on monetary policy, but it could be feeling pressure to maintain its easy stance amid high joblessness.

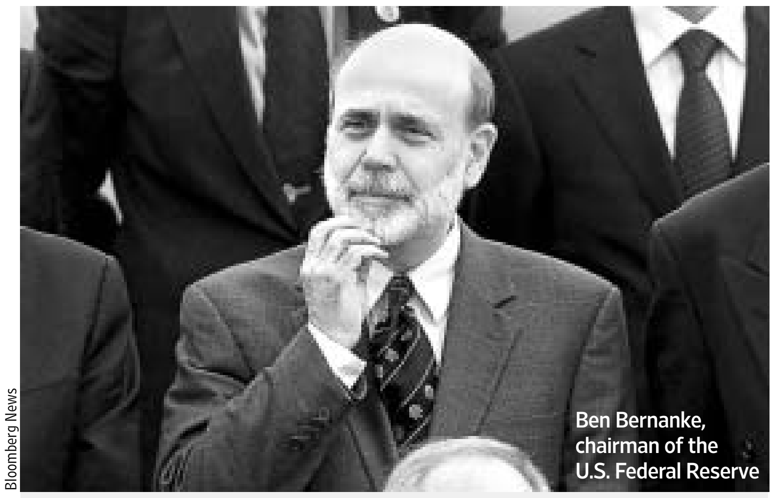
"I don't think the [rate-setting Federal Open Market Committee] is influenced by the political calendar," Mr. Maki said. But "the Fed doesn't want to become a main topic of the election either. I could imagine it being a mild disincentive [to act]." He notes that increasing the federal-funds rate to 0.5% from its current 0%-0.25% range would still keep the rate at an extremely low level.

No matter how much the Fed wants to stay out of politics, the decision to change rates could come amid a highly charged battle in Congress over the central bank's future. Senate Banking Committee Chairman Christopher Dodd (D., Conn.) this week introduced legislation that would curtail the Fed's powers. His counterpart in the House, Barney Frank (D., Mass.), wants to expand them. The debate could drag on well into 2010.

Among the findings of the survey:

■ Emerging markets and commodities are the most likely places for another bubble to develop, according to economists, but they only put slightly better than 1-in-3 odds of such an unsustainable run-up in asset prices occurring in the next two years.

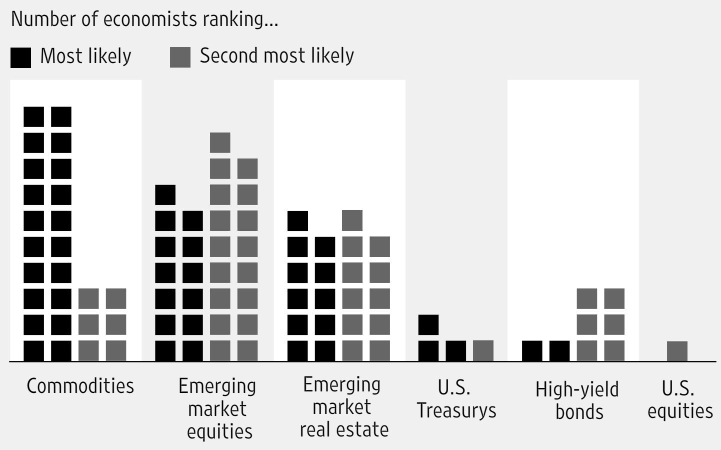
■ More than half of the respondents see a U-shaped recovery with some slowness followed by solid growth, and 31% forecast a stronger, V-shaped recovery. Just 11% expect an L-shaped rebound where economic activity stabilizes at a low level, and only 7% see a double-dip recession—another GDP drop after a short rebound—as the most likely scenario.



Ben Bernanke, chairman of the U.S. Federal Reserve

Emerging risk

Responses to the survey question: Please rank the potential asset bubbles from most likely to least likely.



Source: The Wall Street Journal survey of economists

Demand for Chinese workers strengthened last quarter

By Andrew Batson

BEIJING—Demand for workers in China picked up sharply in the third quarter of the year, a new official survey shows, adding to recent signs that the nation's economic recovery is improving conditions for consumers.

Much of China's data on jobs and unemployment are notoriously unreliable, which has made it hard to track the impact of the financial crisis on the world's third-largest economy. The nation's headline unemployment rate has barely changed over the past year, even though a separate government survey estimated that at one point early this year 20 million migrant workers were jobless.

But a quarterly survey by an arm of the labor ministry offers a more detailed picture. The latest results, released this week, show employers' demand for workers rising 14.2% in the third quarter from a year earlier, the first increase after four straight quarters of decline. The survey typically covers about 100 cities, capturing around half of the working population in China's major urban centers.

"China's labor-market situation is actually quite OK at the moment," said Louis Kuijs, an economist in the World Bank's Beijing office. "The third quarter seems to be better than earlier in the year."

The current situation is a big contrast to the beginning of 2009, when there were fears that the collapse in China's exports would lead to mass unemployment of rural migrant workers. Since then, government surveys have reported that most migrants have found new work. China's purchasing managers' index survey also has shown manufacturers adding jobs every month since June. Many factory managers are even complaining now that it's getting hard to find employees.

The two big employers of migrant laborers—construction and export manufacturing—both have recovered somewhat from the worst of the downturn. China's exports rose a seasonally adjusted 1.5% in the third quarter from the previous quarter, according to a central-bank estimate, the first gain this year. And the area of new buildings under construction is nearly 50% higher this year than last year.

There were 94 open positions for every 100 applicants in the third quarter, the survey says, up from a low of 85 last year and approaching the pre-crisis average of 97.

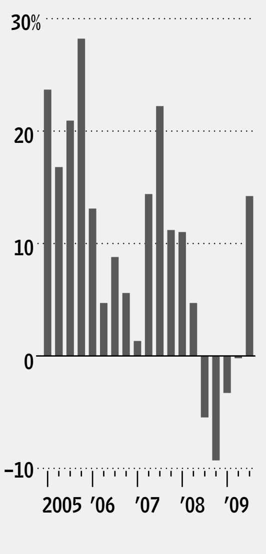
If that trend continues it could push up incomes and help support consumer spending. The National Bureau of Statistics reported this month that the average wage for migrant workers rose 2.8% in the third quarter from the previous quarter, to 1,444 yuan, or about $210, a month.

"If the economy continues to grow like it is now, then wage pressures will emerge, which is good for consumption," said Paul Cavey, an economist for Macquarie.

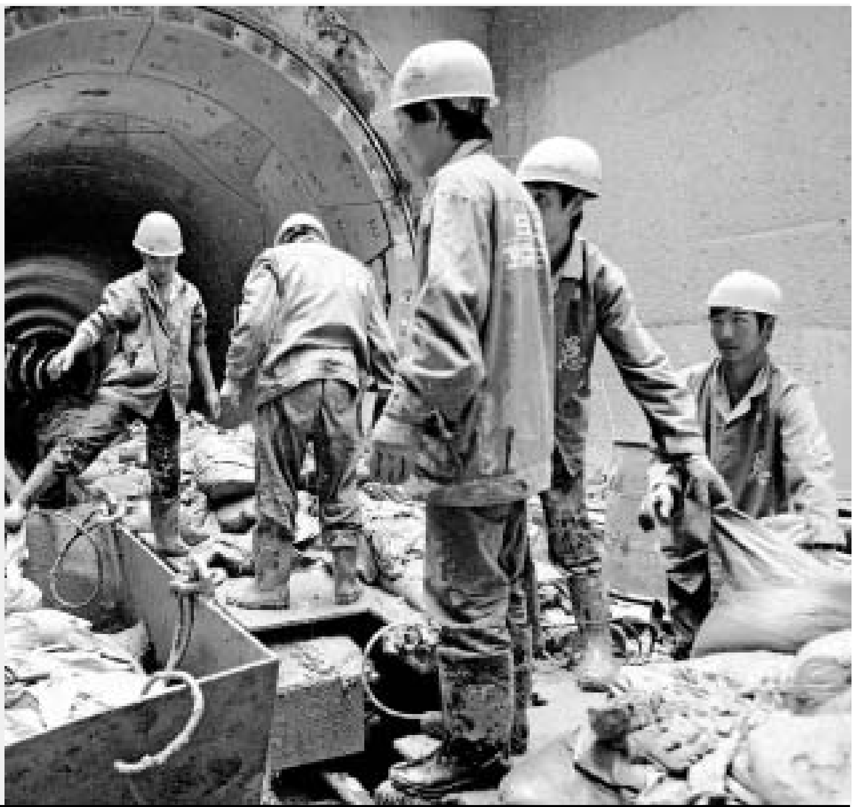
In an important shift, overall rural and urban incomes so far this year are both up around 9% from last year. Though slower than in years past, that gain is actually faster than current economic growth. For several years, China's households income have lagged behind increases in headline indicators such as gross domestic product. That gap is one of the factors many economists think has constrained consumer spending and thus its ability to move beyond reliance on exports and investment.

Help wanted

Chinese employers' demand for workers, change from a year earlier



Sources: China Labor Market Information Center; Bloomberg News (photo)



Workers unload bags of mud in a section of the Xian subway system in China's Shaanxi province earlier this year.

U.S. looks at TARP cash in bid to cut deficit

Proposal under debate inside White House; move's impact unclear

BY DEBORAH SOLOMON AND JONATHAN WEISMAN

WASHINGTON—The Obama administration, under pressure to show it is serious about tackling the U.S. budget deficit, is seizing on an unusual target to showcase fiscal responsibility: the $700 billion financial rescue.

The administration wants to keep some of the unspent funds available for emergencies, but is considering setting aside a chunk for debt reduction, according to people familiar with the matter. It is also expected to lower the projected long-term cost of the program—the amount it expects to lose—to as little as $200 billion from $341 billion estimated in August.

The idea is still a matter of debate within the administration and it is unclear how much impact it would have on the nation's mounting deficit levels. Still, the potential move illustrates how the Obama administration is trying to find any way it can to bring down the deficit, which is turning into a political as well as an economic liability.

The White House is in the early stages of considering what bigger moves it might make for next year's budget. The Office of Management and Budget has asked all cabinet agencies, except defense and veterans affairs, to prepare two budget proposals for fiscal 2011, which begins Oct 1, 2010. One would freeze spending at current levels. The other would cut spending by 5%.

OMB is also reviewing a host of tax changes. The President's Economic Recovery Advisory Board will submit tax-policy options by Dec. 5, including simplifying the tax code and revamping the corporate tax code.

White House Chief of Staff Rahm Emanuel is pressing for substantial spending cuts to go with any tax increases to try to avoid the "tax and spend" label that has bedeviled Democrats, according to administration and congressional officials.

The administration is constrained in tackling the mounting deficit, since raising taxes or slashing spending could stunt economic growth. Administration officials say the Obama economic team is especially concerned that rapid deficit reduction could hurt the economy.

On the $700 billion Troubled Asset Relief Program, the administration is considering a change that may appear to improve the fiscal situation. Agreeing not to spend a certain amount of TARP money will enable the White House, in its budget projections, to assume less money out the door and, therefore, less debt issued. The move would also reduce the deficit by an unknown amount since a certain level of spending and borrowing is already factored into estimated future deficits.

The Treasury Department said about $210 billion in TARP funds remains unspent, including about $70 billion returned from financial institutions. A further $50 billion is expected to be repaid in the next 12 to 18 months.

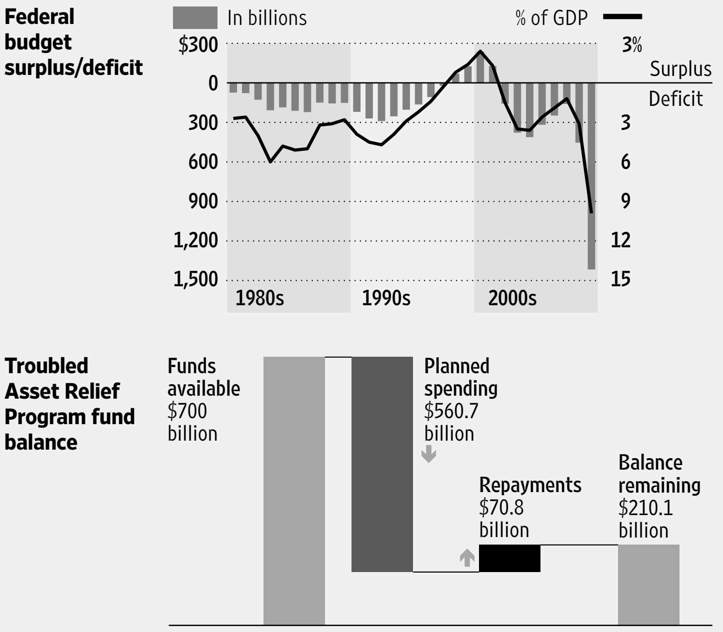
Budget experts said committing some TARP funds toward debt reduction could help calm concerns about the size and intent of the program. "I don't necessarily want them to pull back in a huge way, because there's a lot of uncertainty, but right now what we've got could turn into a $700 billion slush fund" for Congress, said Douglas Elliott, a fellow with the Brookings Institution, a liberal think tank.

The move could buy the Treasury Department time before it hits the so-called debt ceiling, which limits the amount of money the U.S. can borrow. Already, some members of Congress have said they won't approve an increase in the $12.1 trillion debt cap unless efforts to reduce the deficit are included.

Senate Budget Committee Chairman Kent Conrad, the North Dakota Democrat who is proposing a bipartisan commission, along with Sen. Judd Gregg (R., N.H.), to examine taxes, said he won't vote for raising the debt limit unless Congress and the administration start talking about cutting spending and increasing taxes.

Digging out

With a widening deficit, the Obama administration is considering committing unspent financial-rescue funds to debt reduction.



Sources: Office of Management and Budget (deficit); Treasury Department (TARP)

Serbia's EU drive clears a hurdle

BY MARC CHAMPION

BRUSSELS—The Netherlands gave its foreign minister a green light to begin unblocking Serbia's path to European Union membership, if a coming report finds Belgrade is cooperating fully with the war-crimes tribunal for the former Yugoslavia, a Dutch foreign-ministry spokeswoman said Thursday.

While the EU has pledged that Serbia eventually can join the 27-nation bloc, the Netherlands has been preventing a key Stabilization and Association Agreement with Belgrade. Such agreements are considered a necessary first step before membership talks can begin.

Late Wednesday, the main parties in the Dutch parliament gave foreign minister Maxime Verhagen approval to "act accordingly" if a report due Dec. 3 from Serge Brammertz, chief prosecutor of the International Criminal Tribunal for the former Yugoslavia, shows that Serbia is cooperating fully with the tribunal, the spokeswoman said. The decision was the clearest signal to date that the Netherlands may be ready to approve the agreement.

Dutch governments have taken a particularly hard line in pressuring Serbia to come to terms with its role in the 1992-1995 war in Bosnia, in part because of the humiliation of Dutch peacekeepers protecting the so-called United Nations safe haven of Srebrenica in 1995.

Bosnian Serb troops led by Gen. Ratko Mladic overran the territory, as the Dutch peacekeepers looked on helplessly. About 8,000 Bosnian Muslim men and boys are believed to have been executed in the aftermath.

The Dutch hard line on Serbia has given rise to tensions within the EU.

Last year, a newly elected pro-Western government in Belgrade captured wartime Bosnian Serb leader Radovan Karadzic and delivered him to the tribunal in The Hague. But with Gen. Mladic and another Serb indictee still in hiding, the Netherlands has continued to block Serbia's stabilization agreement.

The Dutch government hasn't seen a draft of Mr. Brammertz's report, but Mr. Verhagen told parliament Wednesday that "the first signals are positive," according to the foreign-ministry spokeswoman.

The Netherlands' hard line on Serbia has created tensions within the EU. Many governments say the bloc needs to keep Serbia on track for membership to maintain stability in the region. The EU supported Kosovo's secession from Serbia last year and is trying to manage the fallout from that, as well as an increasingly unstable situation in Bosnia.

The EU is also expected later this month to begin consideration of a request from Serbia's regional rival Albania to start membership talks.

The Netherlands has already begun to soften its position against Belgrade, saying it won't stand in the way of granting Serbs visa-free travel to the EU—a development expected next year.

Last week, Serbia's government said that it, too, plans to apply for EU membership talks by the end of the year, a move that Italy has since backed publically. The Netherlands would oppose such an early move, however, the foreign-ministry spokeswoman said, arguing that Serbia shouldn't skip the association agreement.

Separately, Thursday, an appeals bench at the war-crimes tribunal cut the sentence of a Bosnian Serb general found guilty of crimes to 29 years from 33. The court upheld Dragomir Milosevic's convictions on five counts of murder, terrorizing civilians and inhumane treatment while leading troops who besieged Sarajevo.