Leading the News: The weakening British pound batters Irish economy

THE WALL STREET JOURNAL.

VOL. XXVII NO. 179 | EUROPE | THURSDAY, OCTOBER 15, 2009

DOWJONES A News Corporation Company | europe.WSJ.com

What's News

The DJIA closed above 10000 for the first time in more than a year, and European stocks closed at their highest level since October 2008 on positive earnings reports. Crude futures rose, while the dollar remained under pressure Pages 17, 18, 24

■ Opposition parties walked out of Russia's parliament to protest alleged vote-rigging in recent elections, in a rare act of disobedience. Page 5

■ As Hillary Clinton played down differences with Moscow over tougher moves against Iran, Putin highlighted the contrasts. Page 5

■ Fed officials last month discussed expanding a program to buy mortgage-backed securities, minutes showed. Page 4

■ Industrial output in the euro zone increased for the fourth consecutive month, led by the bloc's three largest economies. Page 4

■ The number claiming British unemployment benefits rose in September, but the increase was the smallest in 16 months. Page 2

■ Eleven foreign banks that operate in the U.K. agreed to reform their pay in line with their British peers. Page 21

■ The jet-leasing unit of AIG will repay $2 billion in short-term debt that comes due Thursday, easing liquidity concerns. Page 17

■ GE plans to hold on to U.K. subprime mortgages in hopes of capitalizing on a projected housing shortage. Page 7

■ A Polish central banker said the country won't be able to adopt the euro until 2014 or 2015. Page 10

■ A mayor from a small political party was nominated to be Romania's new prime minister following the collapse of the government.

■ Crédit Agricole will use funds from bond issues to help it reimburse $4.45 billion in French aid. Page 19

■ Burberry reported better-than-expected sales for the second quarter on demand for the British luxury brand's fall-winter collection. Page 6

■ Drinks company Diageo surprised the market with a 6% decline in its fiscal first-quarter sales. Page 6

■ Died: Bruce Wasserstein, 61, chief executive of investment bank Lazard. Page 2

EDITORIAL&OPINION

Mobile meltdown
Rationing is coming to the wireless Internet.
Page 12

Breaking news at europe.WSJ.com

A missing da Vinci painting ... from a print

Associated Press

FINGER PAINTING: A new work by Leonardo da Vinci may have been revealed by a centuries-old fingerprint. Collector Peter Silverman bought "Profile of the Bella Principessa" in New York on behalf of an anonymous Swiss collector in 2007 for about $19,000. Forensic-art expert Peter Paul Biro said a fingerprint on what was presumed to be a 19th-century drawing matched a fingerprint from Leonardo's "St. Jerome" in the Vatican. One London art dealer now says it could be worth more than $150 million. —Associated Press

J.P. Morgan profit leaps to $3.59 billion

By Robin Sidel

J.P. Morgan Chase & Co. said third-quarter earnings rose sevenfold to $3.59 billion, boosted by strong fixed-income trading in its investment bank, but warned that consumer woes likely will prevent the financial-services behemoth from reaching its full earnings potential until 2011 or 2012.

The New York bank, which was the first major financial institution to report third-quarter results, poured another $2 billion into reserves for soured loans in its consumer businesses.

The results exceeded analysts' expectations, sending shares of J.P. Morgan up 3.2% in late trading, and helping spur a rally that pushed the Dow Jones Industrial Average above 10000.

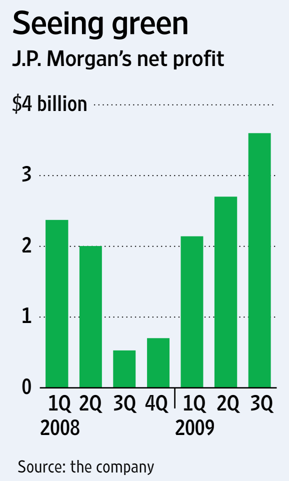
The results bode well for other Wall Street firms like **Goldman Sachs Group** Inc., which reports earnings Thursday. It paints a bleaker picture, however, for banks that have large consumer-lending portfolios, including the large regional banks and **Bank of America** Corp., which reports results on Friday.

In a conference call with analysts, Chief Executive James Dimon said he is encouraged by signs that small businesses, midsized firms and large corporations are planning for the future.

"They are poised and waiting to see if [an economic] recovery is taking hold because they do have plans," he said.

Still, Mr. Dimon expressed caution about continued signs that the pace of consumer delinquencies may be slowing, saying that the trends so far haven't yet convinced the bank to stop building loan-loss reserves. The latest addition brings total reserves to $31.5 billion, or 5.3% of total loans.

Please turn to page 31



Market movers

Calpers reviews fees paid to advisory firm

By Craig Karmin

The **California Public Employees' Retirement System**, the U.S.'s largest public pension fund, is launching a "special review" of fees paid by some of its money managers to an investment advisory firm run by a former Calpers board member, the pension fund said.

"The review was sparked by the recent receipt of information provided to Calpers by investment funds that reported their payment of more than $50 million in fees over a five-year period to **Arvco Financial Ventures** LLC, a placement agent firm headed by former Calpers board member Al Villalobos," the $200 billion California fund said in a press release. It didn't disclose the five-year period.

Mr. Villalobos served on the Calpers board from 1993 to 1995. A call to Arvco wasn't immediately returned.

Placement agents are middlemen who help money managers secure pension and other investment business.

Calpers had its worst returns ever last year, losing nearly a quarter of its value and more than $50 billion.

The review will be conducted by the law firm Steptoe & Johnson LLP, Calpers said.

Calpers's investigation into its own investment process marks a new turn amid a focus this year on so-called pay-to-play concerns in pub-

Please turn to page 31

Inside

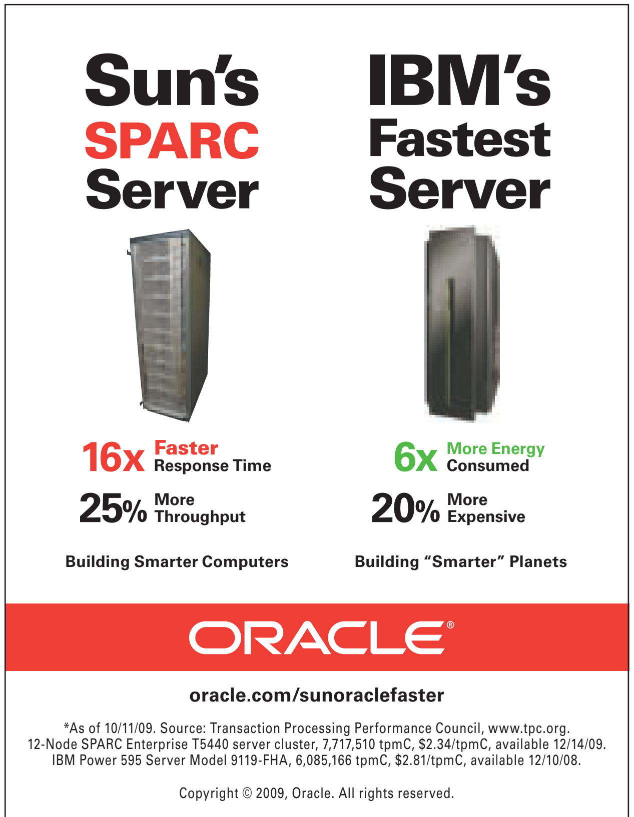
Mind the gap

The U.S. is looking up from a much bigger deficit hole
Leading the News, page 4

Markets

4 p.m. ET

	CLOSE	PCT CHG
DJIA	10015.86	+1.47
Nasdaq	2172.23	+1.51
DJ Stoxx 600	246.98	+2.08
FTSE 100	5256.10	+1.98
DAX	5854.14	+2.45
CAC 40	3882.67	+2.14
Euro	$1.4901	+0.51
Nymex crude	$75.18	+1.39



For information or to subscribe, visit www.services.wsje.com or call +44 (0) 207 309 7799 — Austria €3 · Belgium €3 · Croatia HRK 22 · Czech Republic Kc 110 · Denmark Dkr 25 · Finland €3.20 · France €3 · Germany €3
Greece €3 · Hungary Ft 650 · Ireland (Rep) €3 · Italy €3 · Lebanon L£ 6000 · Luxembourg €3 · Netherlands €3 · Norway Nkr 29 · Poland Zl 12 · Portugal €3 · Slovakia €3.32/Sk 100 · Spain €3 · Sweden kr 29
Switzerland SF 5 · Syria S£ 210 · Turkey TL 4.5 · U.S. Military (Eur) $2.20 · United Kingdom £1.50

THE WALL STREET JOURNAL.

9 772191 986948 42

LEADING THE NEWS

U.K. jobless claims rise

Rate of deterioration in the labor market may be tapering off

BY NICHOLAS WINNING AND PAUL HANNON

LONDON—The number of people claiming British unemployment benefits hit its highest level in more than 12 years in September, but the monthly rise was the smallest for 16 months, indicating that the deterioration in the labor market may be starting to ease, the Office for National Statistics said.

The overall number totaled 1.63 million, the highest level since April 1997. But the claimant count rose by 20,800 in September, compared with a revised 23,000 gain in August—the smallest monthly increase since May 2008.

The claimant count rate rose 0.1 of a percentage point from August to 5.0% in September, the data showed.

"There is some evidence of an easing in the rate of deterioration in the labor market," an ONS statistician said.

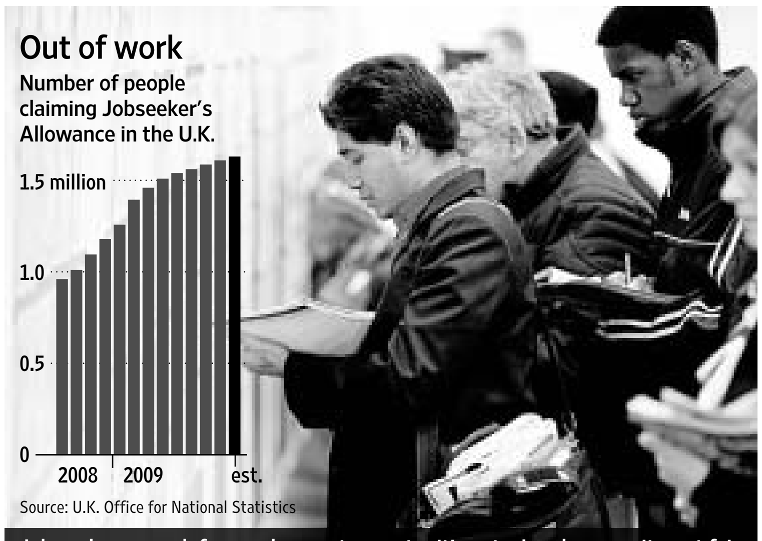
The pound strengthened against the dollar and euro immediately after the release of the data, while gilt futures prices fell slightly.

The broader International Labor Organization rate of unemployment was 7.9% for the three months to August, up 0.3 percentage point from the previous three months. Those data take more time to compile, and are older than the claimant-count figures.

ILO unemployment totaled 2.47 million, up 88,000 from the figure for the three months to May.

However, compared with the three months to July, ILO unemployment dropped 1,000, the first drop since the three months to May 2008, the ONS said.

The ILO measure "is certainly expected to rise further, but at the beginning of the year most people's core expectation for unemployment was a peak of at least three million. This no longer looks likely," Karen Ward, an economist at HSBC, said in a note. She added that unemployment was likely to peak at 2.7 million around the middle of 2010.



Source: U.K. Office for National Statistics

Job seekers search for employment opportunities at a London recruitment fair.

The data also showed the increase in average earnings continues to ease, a sign that unemployment and the general weakness of the economy are still eroding employees' ability to command higher salaries.

Average earnings excluding bonuses increased 1.9% in the three months to August compared with the previous year, the smallest rise since comparable records began in 2001, the ONS said. Including bonuses, average earnings increased 1.6% in the three months to August, down 0.2 percentage point from the previous period.

Lazard Chief Executive Bruce Wasserstein dies at 61

BY DENNIS K. BERMAN AND JEFFREY MCCRACKEN

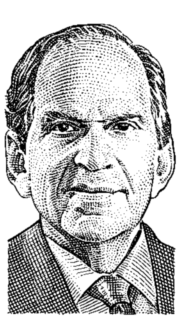
Lazard Ltd. Chief Executive Bruce Wasserstein has died, according to two people familiar with the matter.

Exact details of his passing couldn't be learned. A Lazard spokeswoman wasn't immediately available for comment. He had been hospitalized over the weekend with an irregular heartbeat, the bank said.

The death of Mr. Wasserstein, 61 years old, is a blow to Lazard, the investment bank he has run for several years.

A descendant of Eastern European immigrants, Mr. Wasserstein attended college at 16 and earned law and business degrees from Harvard University. After a stint as a corporate lawyer, he decamped to investment bank First Boston Corp. There, he and another deal maker, Joseph Perella, helped unleash the mergers-and-acquisitions boom that defined the 1980s.

During that decade Mr. Wasserstein forged the persona of the modern investment banker. For Mr. Wasserstein and a cadre of other sharp-witted young guns, banking was no longer the gentlemanly art practiced at places like Lazard. It was more akin to brawling in expensive suits, with tortuous financial tactics, platoons of lawyers and public relations deployed as M&A weapons.



Bruce Wasserstein

After feuding with the management of First Boston, Messrs. Wasserstein and Perella left to start their own bank in 1988. Mr. Wasserstein revealed a fascination with the Lazard mystique. In an interview with The Wall Street Journal in 1988, he said of his new bank, Wasserstein Perella & Co.: "We want to be the Lazard of the '90s."

He was supposed to be enjoying his time as power broker at Lazard. But the trans-Atlantic battle for **Cadbury** PLC lured the veteran Wall Street deal maker directly into the fray.

Mr. Wasserstein emerged as the surprise lead adviser to **Kraft Foods** Inc. on its takeover offer. He spent the Labor Day weekend in London as the Kraft offer was disclosed, said a person familiar with the matter.

It was a flashback to a quarter-century ago, when Mr. Wasserstein was a young banker at the center of the 1980s merger boom. Back then he earned the nickname "Bid 'em Bruce," which he later shunned, famously daring clients to "be great" and pay up for acquisition targets.

At Lazard, Mr. Wasserstein oversaw an investment bank with 2,000 employees and $1.36 billion in annual revenue. Such roles typically require a CEO to make strategic decisions but not to get personally involved in day-to-day projects.

Yet, the big deal—Mr. Wasserstein once wrote a 927-page book with that title—proved to be an irresistible lure. And Mr. Wasserstein was well-prepared for his unexpected role.

As a student at Britain's Cambridge University in the early 1970s, he studied and wrote extensively about British merger and takeover law. He later worked on several U.S.-British deals, including the 1999 acquisition of British supermarket chain Asda by Wal-Mart Stores Inc. In 2000, Mr. Wasserstein worked with Kraft's then-owner Philip Morris Cos. on a deal to acquire food maker Nabisco Holdings Corp.

His background, combined with a large Lazard presence in London, thrust Mr. Wasserstein into the forefront of Kraft's $16.73 billion Cadbury offer, said people working on the deal.

Boutique investment bank Centerview Partners had been advising Kraft on the bid, said two people familiar with the matter. But Centerview didn't have an office in London until recent months, giving Lazard an opening.

Both banks potentially could earn tens of millions of dollars in fees, given Cadbury's size and the fact that the offer is an unsolicited one. Bankers are typically paid hefty "success fees" on unsolicited deals, which make them more risky—and more lucrative if completed.

Another Lazard banker, managing director Peter Kiernan in London, was recently named director general of the Takeover Panel, a regulatory board that could eventually be charged with pushing Kraft to make its offer official, though Mr. Kiernan wouldn't have a role in the matter.

Other bankers working on the deal for Kraft also had ties to Mr. Wasserstein. Centerview's lead banker on the deal, Robert Pruzan, was formerly president of Wasserstein Perella & Co.

Leon Kalvaria, a vice chairman of Citigroup, worked with Mr. Wasserstein in the mid-1980s as a banker at First Boston Corp., where Mr. Wasserstein was co-head of investment banking. Citigroup is listed by Kraft, along with Deutsche Bank, as a corporate broker and an adviser on the offer.

—Dana Cimilluca contributed to this article.

CORRECTIONS & AMPLIFICATIONS

Millennium Management LLC runs a multistrategy hedge fund that is performing above its high-water mark, or the point at which it earns performance fees. It doesn't run a separate high-yield bond fund. A Money & Investing article on Tuesday incorrectly said Millennium runs a high-yield bond fund that is below its high-water mark.

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.
Trademarks appearing herein are used under license from Dow Jones & Co. © 2009 Dow Jones & Company All rights reserved.
Editeur responsable: Patience Wheatcroft M-17936-2003

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

LEADING THE NEWS

Ireland suffers as pound continues its big retreat

Food, drink exports, retail and tourism hit; no wish to ditch euro

By Quentin Fottrell

DUBLIN—The ever-weakening British pound is taking a toll on Ireland's already battered economy, hurting food and drink exports, retailers, and tourism.

But despite the growing costs of having no control over its exchange rate, there is hardly any appetite in Ireland for ditching the euro. The common currency is seen as having contributed to the country's earlier prosperity and helping shelter the country from the global financial crisis.

Ireland's gross domestic product is expected to shrink 7.8% this year, according to the Central Bank of Ireland, a further deterioration from last year's 2.3% contraction and a stunning reversal from 6% growth in 2007. This retreat is due to the collapse in the construction sector, which has led once-booming home prices to fall 24% from their peak in February, 2007, and the near-meltdown of its financial sector.

But now other sectors are suffering, too. Exporters of traditional goods like beef and dairy products to the U.K. face an increasingly punitive foreign-exchange rate. And price wars have intensified between Irish retailers and British grocery stores like **Tesco** PLC and **Marks & Spencer's Group** PLC, which sell cheaper imported goods from the U.K.

On Tuesday, Central Bank of Ireland Governor Patrick Honohan said the current exchange rate for sterling against the euro translates to about £1.18 for one old Irish pound—"a high level never approached during the 20-year independent life of the Irish pound."

Ireland joined the European Monetary System in 1978, breaking the Irish pound's previous link with sterling. It was one of the "first wave" countries to adopt the euro on Jan. 1, 1999.

Although Ireland isn't as dependent on exports to its closest neighbor as it was in 1979, some 18% of its merchandise exports get sent to the U.K., and about 22% of its services exports. The U.S. is a close second, accounting for 18% of merchandise exports and 9% of services exports.

Irish exports to the U.K. fell 23% in the third quarter from a year earlier, according to the Irish Exporters Association, which says 27,400 jobs now are vulnerable to the fall in sterling. The association's chief executive, John Whelan, called weak sterling "catastrophic" for Irish exporters to the U.K.

Economists say the British pound is expected to remain under severe pressure in the short term, with investors using any negative economic news to sell the currency. The euro rose to 94 pence for the first time in six months Tuesday after a weak reading of U.K. inflation. Late Wednesday in U.S. time, the euro was trading at 93.38 pence.

Some analysts also see the euro as over-valued against the dollar, but that is seen as less of a problem for Irish exporters, because most exports to the U.S. are priced in dollars because the exporters are global companies.

"The strong euro will squeeze profit margins because of an increase in labor and energy costs for companies here exporting to the U.S., but a lot of the goods exported to the U.S. from multinationals are priced in dollars," said NCB Stockbrokers chief economist Brian Devine. "Sterling is a bigger issue here than the dollar."

Sterling's weakness is due in part to low U.K. interest rates, the U.K.'s faltering economy and dependence on the financial sector, plus uncertainty about new economic policies after the U.K.'s coming general election, expected to be called by the spring.

The food and drink industry, which accounts for two-thirds of exports other than those by multinational companies based in Ireland, is particularly vulnerable to this weakness in sterling. Approximately 43% of food and drink exports go to the U.K.

"The increasing weakness of sterling is having a crippling effect on our exports," said Paul Kelly, director of lobby group Food and Drink Industry Ireland. "It's time for the government to take action."

He wants the government to start by cutting industrial electricity costs, currently the fourth-highest in Europe and 35% above the eurozone average. He also urges a state-backed export-credit program—a form of insurance covering an exporter against nonpayment by the importer—similar to programs that exist in France and the Netherlands.

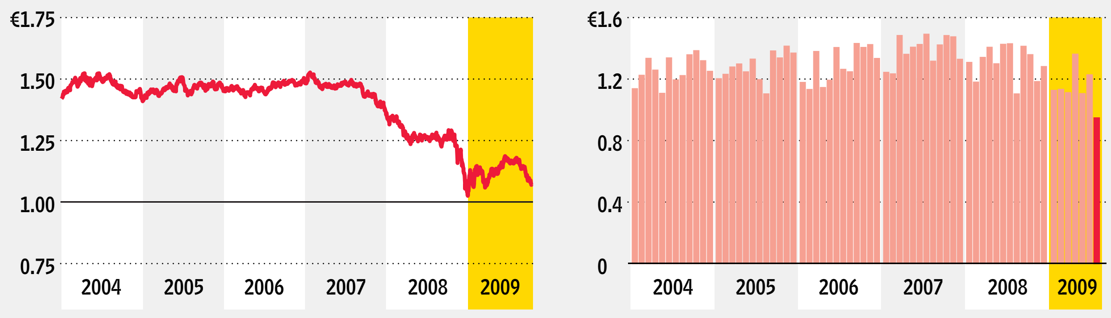
A weaker pound will also hurt Irish retailers during the crucial holiday season. "It will mean more shops here offering even bigger discounts and more people going to Northern Ireland for Christmas," Bloxham's Stockbrokers chief economist Alan McQuaid said.

According to a report from the tax authorities and the government's Central Statistics Office, the Irish economy lost as much as €550 million ($815.6 million) in shopping in 2008 due to shoppers going north and as much as €90 million in lost tax revenue. In 2009, the report says, retailers could lose as much as €700 million if the euro stays as weak as it is against the pound.

An unfinished commercial-building site in Dublin. Ireland's exporters are now sharing the pain of the construction sector.

Bloomberg News

Tough sell | The pound's fall has made Irish products pricier in a key market



Sources: WSJ Market Data Group (exchange rate); Eurostat (exports)

U.S. retail sales fall, hurt by autos

By Luca Di Leo
And Jeff Bater

WASHINGTON—U.S. retail sales fell in September after the federal government's subsidy to buy cars ended, adding to evidence that the economy's recovery will be slow.

Sales fell 1.5% in September as motor-vehicles sales dropped 10.4%, the Commerce Department said Wednesday. For about five weeks in July and August, the government's "cash for clunkers" program provided as much as $4,500 toward a new car to buyers who traded in an older gas-guzzler.

The decline in retail sales was smaller than the 2.1% fall forecast by Wall Street. After a downward revision to the August numbers was factored in, though, the cumulative decline was in line with expectations.

Sales excluding autos rose 0.5%, leading some economists to revise upward their growth projections for the third quarter.

LEADING THE NEWS

U.S. deficit dilemma: this time it's worse

Gap of $1.4 trillion will likely get bigger, even if economy revives

BY DAVID WESSEL

Conveying the enormity of the U.S. budget deficit is tough. As humor columnist Dave Barry once observed, millions, billions and trillions sound too much alike. Think golf balls, watermelons and hot-air balloons, and you get a better idea. If today's tax rates prevail, federal benefits are paid as promised and other spending grows at the same pace as the economy, the deficit will be bigger in 2019 than at any time in Barack Obama's lifetime—and that's even if the economy revives.

For the fiscal year that ended Sept. 30, the final deficit tally will be about $1.4 trillion. Measured against the size of the economy, that's 9.9% of gross domestic product, bigger than any year since 1945. As a share of GDP, tax and other revenues are lower (15%) and spending higher (25%) than anytime in the past 50 years.

CAPITAL

President Obama says this isn't his fault. Of the $9 trillion in deficits projected over the next decade, the White House blames $5 trillion on the past—the Bush tax cuts, the wars in Iraq and Afghanistan and the Medicare prescription-drug bill that a Republican Congress passed and George W. Bush signed without any visible means of support.

The White House pins the other $4 trillion on the consequences of the recession and financial crisis. That assumes that everything labeled stimulus is, in fact, stimulus, but grant that for a moment. The real problem isn't how we got here, it's where we are: Another day older, and deeper in debt.

The U.S. has confronted big deficits before. "Numbers like this will eventually prompt corrective measures, just as a stark but less worrisome budget outlook did in 1990," Goldman Sachs economists assured clients last week.

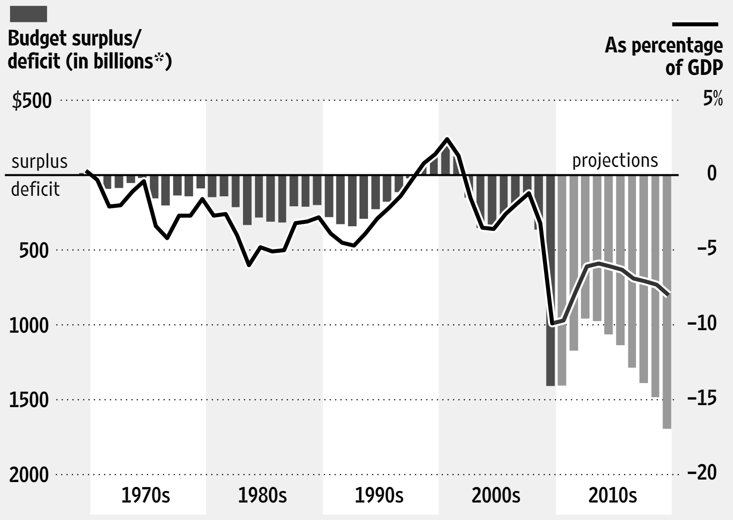
This time will be tougher.

We are starting from a much deeper hole. When the economy began climbing out of the deep recession of the early 1980s, federal debt—the sum of every annual budget deficit—amounted to less than 30% of the U.S.'s GDP, the value of all the goods and services produced in a year. At the beginning of the 1990s, it was less than 40%. Today, it exceeds 50% of GDP and is rising toward 80%, perhaps 100% of GDP over the next 10 years. Even at today's low interest rates, the federal government spent about $195 billion on interest in fiscal 2009, more than 10 times the entire NASA budget. A rising debt-to-GDP ratio means interest takes an ever-greater slice of the budget, much of that going to the foreigners.

The president vows that his health-care plan won't make the deficit bigger. The problem is that the likely congressional compromise, if there is one, won't make the deficit smaller over the next decade either. Maybe it will, as Mr. Obama intends, "bend the cost curve" and reduce the growth rate of health spending. But history suggests increases in spending (subsidizing insurance for those who lack it) will be more likely to stick than projected savings. Congress, for instance, almost certainly will undo cuts in Medicare doctor fees that were counted as "deficit reduction" when they were enacted earlier. (The House health bill does; the Senate doesn't—yet.)

Sinking deeper in debt

Federal budget deficit past and future, if current policies prevail.



*in constant dollars
Note: Projection assumes Bush tax cuts don't expire, appropriated spending grows with economy
Sources: OMB (historical); Committee for a Responsible Federal Budget, CBO (projections)

But the president has yet to offer a business plan to demonstrate how he will prevent the U.S. from becoming the world's largest subprime borrower. The White House says: Wait till health care is done. "We will be showing more about what we intend to do about the deficit when the president's budget comes out in February," promised Peter Orszag, the president's budget director.

Inside the administration, the policy wonks are divided. Those most pessimistic about the economy talk of more deficit-widening stimulus, arguing that reviving economic growth is the imperative. Deal with deficits later. Those who see an improving, if sluggish, economy say the deficit must be addressed before it causes a crisis of confidence among U.S. creditors and provokes a dollar crash or a sharp increase in bond-market interest rates.

The president's political advisers are hardly deficit phobes by nature, but see rising public angst about the deficit and Republicans scoring points by talking about it. The latest Wall Street Journal/NBC News poll posed a choice: Should Washington "worry more about keeping the budget deficit down even though it may mean it will take longer for the economy to recover" or should it "worry more about boosting the economy even though it may mean larger budget deficits now and in the future?" Some 62% chose deficit-fighting; only 30% picked economic revival.

The rub is that the deficit-fearing public doesn't want tax increases or spending cuts. "Everyone dislikes the deficit, and everyone dislikes the specific steps you have to take to get out of it," Mr. Orszag says. Even more troublesome, some of the less politically painful ways to shrink the deficit probably will be used to finance an expansion of health-insurance coverage, such as squeezing doctors and hospitals or boosting taxes on upper-income Americans. Any realistic attack on deficits will both restrain spending on benefits and raise taxes (whether they're called that or not) on Americans earning less than $250,000 a year, despite the president's vow not to do that.

The if-I-were-king answer is to give the economy a little more carefully crafted stimulus now and to enact spending restraints and tax increases that take effect in three or four years when the economy is healthier. But even if Mr. Obama could talk Congress into that, the fiscal credibility of the U.S. political system is so weak that few would believe that the promised belt-tightening actually would take effect.

Write to me at capital@wsj.com. Discuss at wsj.com/capital.

Fed minutes reveal concern over strength of U.S. recovery

BY SUDEEP REDDY

U.S. Federal Reserve officials last month discussed expanding a program to buy mortgage-backed securities, a sign of continued concern within the central bank about the strength of the economic recovery, minutes of the Fed's latest policy meeting showed.

Some members of the Federal Open Market Committee thought increasing the size of the program "could help to reduce economic slack more quickly," the minutes said. At least one member of the committee believed the improving economic outlook "could warrant" a reduction in the purchase target.

The Fed ultimately voted to commit to buying the full $1.25 trillion in mortgage-backed securities it had announced as the upper limit for the program, extending the purchases into March. It also kept its interest-rate target near zero.

The discussion of enlarging the mortgage-securities program underscored the unease among Fed officials about the durability about the economic recovery. Some investors—along with some Fed policy makers—worry about an outbreak of higher inflation from the vast expansion of the U.S. central bank's balance sheet to boost the economy.

But most Fed officials, while stressing they have the tools and willingness to scale back their support at the right time, continue to express concerns about whether growth will be strong enough over an extended period for the economy to heal from its deep downturn.

Fed policy makers at the meeting expressed "considerable uncertainty" about the strength of the economy's upturn once special government programs to support credit and housing markets were withdrawn, the minutes said. FOMC members "discussed the importance of maintaining flexibility to expand the asset purchase programs should the economic outlook deteriorate or to scale back the programs should economic and financial conditions improve more than anticipated."

After the Sept. 22-23 meeting, the Fed's policy committee said it expects inflation "will remain subdued for some time." But with weak economic activity and slack throughout the economy, the minutes said, the FOMC "judged that the costs of growth turning out to be weaker than anticipated could be relatively high."

Still, central-bank policy makers appeared across the spectrum in their inflation concerns. Many officials viewed the risk of higher or lower inflation in the next few quarters as "roughly balanced," the Fed said. But a few saw "some risk" of a substantial drop in the inflation rate. A few officials "felt the risks were tilted to the upside" over a longer horizon, the minutes said.

Many Fed officials at the meeting said they had revised upward their projections for economic growth for the rest of the year due to a leveling out in consumer spending, improving financial conditions and even a brightening outlook for growth abroad to support U.S. exports.

But they still said the economic recovery "was likely to be quite restrained" as consumers and businesses remained cautious and bank lending remained tight. The economy overall was expected to expand through 2010 "but at a pace that was unlikely to reduce the unemployment rate appreciably."

One area that remained a particular concern was real estate. Commercial real-estate activity "continued to fall markedly" in most of the U.S. due to declining occupancy and rental rates and tight credit conditions.

In the residential sector, home sales and prices offered early signs of stabilization. But some Fed officials "viewed the improvement as quite tentative" given the end of the tax credit for first-time home buyers next month and the winding down of the Fed's program to buy mortgage-backed securities.

Euro-zone factory-output gains ease worries about growth

BY BRIAN BLACKSTONE

A fourth straight monthly rise in industrial output in the euro zone, led by its three largest economies, provided further confirmation that the region's severe recession ended around the middle of the year.

Industrial output in the 16 countries that have adopted the euro currency swelled 0.9% in August from July, the European Union's statistics agency said Wednesday. Though below economist expectations, significant upward revisions to June and July output signal that the factory sector has performed better than economists had expected.

The production data also eased worries that the euro zone might slide back into contraction later this year or next, though some economists warned that growth would likely slow once government stimulus programs run their course.

Output growth was concentrated in the euro zone's biggest economies, with Germany up 1.5% from July, France growing 1.9% and Italy's factory output swelling 7%. Ireland posted a steep drop, though that followed large back-to-back monthly increases.

Klaus Baader, chief European economist at Société Générale, said that while the euro zone experienced "a clear 'V' at the beginning of the recovery," it is doubtful that the momentum will continue.

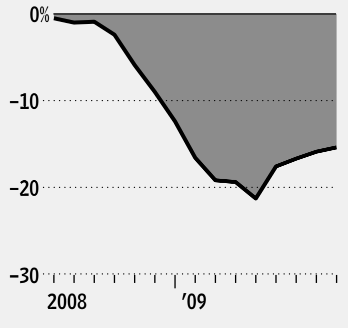
Mr. Baader estimates that euro-zone gross domestic product grew 0.5% last quarter, on a quarterly basis. GDP shrank 0.2% in the second quarter and declined a record 2.5% in the first quarter.

Société Générale's forecast for the third quarter, though at the high end of the range of economist expectations, is by no means robust when compared with expected growth rates in emerging markets and other major economies such as the U.S.

The steady recovery in production suggests there is probably enough momentum in both investment and consumer spending to keep GDP from sliding back into negative territory, said Enam Ahmed, senior economist at Moody's Economy.com.

Grinding forward

Euro-zone industrial production, change from a year earlier



Source: Eurostat

LEADING THE NEWS

Russians protest election

Opposition parties leave parliament, alleging vote-rigging

By Gregory L. White

RIA Novosti

Members of four opposition parties walked out of the State Duma, Russia's lower house of parliament, to protest what they say was vote-rigging in regional elections.

MOSCOW—Russian opposition parties staged a rare act of disobedience in Russia's tightly controlled political system, walking out of parliament Wednesday to protest what they said were rigged regional elections last weekend.

Though there was no sign the action would have major consequences, it cast a spotlight on vote manipulation, a phenomenon the opposition and independent poll monitors say has been widespread for years in Russia but that the Kremlin and electoral officials dismiss.

The walkout also posed a problem for President Dmitry Medvedev, who Monday praised the vote and congratulated the ruling United Russia Party for its strong victory.

Mr. Medvedev has called for a more open, competitive political system, with greater representation for parties other than United Russia, which now controls commanding majorities in national and regional legislatures, as well as among governors and mayors. Critics charge the Kremlin hasn't backed up the promises with actions.

U.S. Secretary of State Hillary Clinton hailed Mr. Medvedev's rhetoric in a speech to students Wednesday at Moscow State University, underlining the importance of "cultivating core freedoms—free speech, freedom of the press and freedom to participate in the political process."

She didn't mention the recent elections. The Obama administration has generally avoided direct criticism of Russia's domestic policies, something that had been a major irritant to the Kremlin. Mrs. Clinton's speech was shown only briefly on Russian national TV news, which focused on her comments on Russian literature.

State media gave more attention to the walkout in parliament. The tone was generally critical of the parties that walked out and favorable to United Russia. The legislature has been known for theatrical tactics, including hunger strikes and fistfights, but Wednesday's walkout was the broadest in years.

The opposition parties—the ultranationalist Liberal Democratic Party of Russia, the Communist Party and Just Russia, a socialist bloc formed with Kremlin support—are typically moderate in their criticism of the government.

But, apparently encouraged in part by Mr. Medvedev's talk of greater political diversity, they had expected better results in Sunday's voting, mainly for seats in regional and local legislatures. United Russia won nearly 80% of the seats, however, including all but three of the 35 seats on the city council in Moscow, where opposition support is traditionally strong.

"We don't recognize the results of these elections," LDPR leader Vladimir Zhirinovsky said before leading his party out of the lower house of parliament, the State Duma. "United Russia acquired the votes through fraud and we can't sit in the same hall with fraudsters."

Legislators accused United Russia of ballot-stuffing and rigging of the vote counting. Golos, an independent vote-monitoring group, said earlier this week that the poll wasn't fair or free. The group said authorities kept opposition candidates off the ballots and independent monitors were denied access to the vote-counting process.

Central Election Commission head Vladimir Churov denounced the walkout as "politics" and dismissed the allegations of widespread violations. United Russia leaders called the opposition sore losers.

A spokeswoman for Mr. Medvedev said the president had no plans to satisfy the opposition parties' main demand—an immediate meeting with the president to discuss the vote results.

Sergei Mitrokhin, leader of the liberal Yabloko party, welcomed the protest but saw little lasting impact. "These are parties that have built themselves into the Kremlin system. Of course, it's a mutiny on the ship, but she's still firmly guided by the hand of Putin and Medvedev."

Clinton, Putin on different pages

By Gregory L. White

MOSCOW—As U.S. Secretary of State Hillary Clinton played down differences with Moscow over tougher moves against Iran, Russia's Prime Minister Vladimir Putin highlighted the contrasts, saying Wednesday it is "premature" to threaten sanctions against Tehran.

At the end of a two-day visit to Russia where Iran policy was a top agenda item, Mrs. Clinton said the Kremlin agrees with the U.S. that tougher sanctions could become inevitable if Iran doesn't do enough to allay international concerns that it is seeking nuclear weapons. She said she was encouraged after a meeting Tuesday with President Dmitry Medvedev, who first suggested last month that Russia might abandon its traditional opposition to sanctions if Iran doesn't cooperate.

But Russian officials have sent mixed signals on the subject since then, leading some analysts to speculate that there could be differences within the leadership. Mr. Putin is widely viewed as the more powerful of the pair and more skeptical about U.S. intentions.

Vladimir Putin

Asked by reporters about possible differences on Iran, Mr. Putin said late Wednesday, "Our president determines foreign policy. If Dmitry Anatolievich [Medvedev] said [sanctions are] inevitable, they're inevitable. But if you look closely at all his statements and the context he made them in, you'll be convinced that there's no steel-and-concrete determination toward sanctions."

Mr. Putin was speaking in Beijing, at the end of a summit of the Shanghai Cooperation Organization, a group including Russia and China that has sought to counter Western domination of the international system. His comments were reported by the Interfax news agency.

Wednesday, Mrs. Clinton, who didn't meet Mr. Putin on her Russian visit, said, "I'm very pleased about how supportive the Russians have been in what has become a united international effort."

French investigators look at several charities

By David Gauthier-Villars

PARIS—French investigative magistrates launched a preliminary probe into several French-based charities, many of which have ties to U.S. marketing and mailing organizations, people familiar with the investigation said Wednesday.

Investigators are trying to determine whether funds raised by more than a dozen charities, whose missions range from supplying food to children in Africa to providing medical relief in Asia, were diverted for other purposes, the people familiar with the investigation said.

Several individuals have been questioned by police but no individual or firm has been put under formal investigation as part of the preliminary probe, the people familiar with the investigation said.

Under French law, preliminary probes are often used by prosecutors to gather information before starting formal probes or putting people or organizations under formal investigation. People or organizations can be the targets of preliminary probes without being notified.

The investigating magistrates' preliminary probe stems in part from a 2008 report by France's health-inspection authorities, the people familiar with the investigation said.

In that report, the health authorities said that French-registered charity Airma had spent only 8.4% of the €5 million ($7.4 million) it had collected from 2004 to 2006 on its declared mission of Alzheimer's research, according to the report, which was reviewed by The Wall Street Journal.

In the report, Airma defended itself by saying it had incurred high legal costs over that period. The French health authorities also described in the report how Airma relied on U.S. marketing company Market Development Group Inc., of Washington, and on the French branch of U.S. company Saturn Corp., which is based in Maryland, to reach out to potential donors via post and email.

In their preliminary probe, investigating magistrates are looking at Airma and several other charities that relied on Market Development Group and Saturn for their marketing and mailing services, the people familiar with the investigation said.

Calls placed to Airma's listed headquarters in Mérignac, near Bordeaux, were answered by an individual who said he knew nothing of the charity. An official at Drive Affaires, which rented the offices to Airma, said the charity left the city a year ago.

Raouf Gueroui, general manager of Saturn Corp. France, said in an interview that he had been questioned in 2007 by the health authorities regarding Saturn's business with Airma. Mr. Gueroui said Saturn's job is limited to handling mail and depositing checks on behalf of the charities, and therefore couldn't have been involved in any wrongdoing related to any magistrates' recent probe. Market Development Group didn't return messages seeking comment.

An official at the Association for Research and Diabetes, a Paris-based charity, said that she had been questioned by police as part of the investigating magistrates' preliminary probe. "They told me that they were satisfied with my answers and I haven't heard from them since then," said Bénédicte Saxe Sers, the charity's chief executive. Ms. Saxe Sers said that her charity was founded by the vice president of Market Development Group. The Association for Research and Diabetes raised €1.9 million last year.

Premier Cercle

In association with THE WALL STREET JOURNAL. EUROPE

EXECUTIVE BRIEFINGS

Energy efficiency

Feasibility, implementation, return on investment

THURSDAY OCTOBER 15th, 2009
RUEIL-MALMAISON

Programme and registration:
www.premiercercle.com/ee2009

solucom management & IT consulting

Schneider Electric

The Wall Street Journal Europe is a registered trademark of Dow Jones Company

CORPORATE NEWS

Burberry's sales increase 4.6%

Shoppers' warm reception of fall-winter clothing line, accessories lifts results

By Kathy Sandler

LONDON—**Burberry Group** PLC reported better-than-expected sales for its fiscal second quarter, boosted by strong in-store demand for the British luxury brand's fall-winter collection of clothes and accessories.

Sales rose 4.6% to £343 million ($545 million) in the quarter ended Sept. 30 from £328 million a year earlier. Sales from Burberry's own retail stores open at least a year increased 5%.

Burberry shares rose on the news, gaining 5.3% to 565.50 pence.

Chief Financial Officer Stacey Cartwright said the group's solid results reflected reduced inventory; better sales of fully priced merchandise, which improves gross margins; and an improved net-cash position. She didn't elaborate on Burberry's current cash position.

But she said she expects Wednesday's update to nudge analysts' full-year forecasts toward the top end of market expectations. Analysts currently forecast full-year pretax profit between £160 million and £190 million.

Burberry attributed the sales increase at its retail stores to consumers' warm reception of its fall-winter collection. Ms. Cartwright singled out handbags, small leather goods and the snood—a pull-on scarf that can be worn around the neck as well as on the head—as particularly popular sellers.

Agence France Presse

Burberry's snood, which can be worn around the neck or on the head, was displayed on the Milan catwalk in February.

The snood, which sells for around £175, falls into the group's growing nonapparel category, which includes handbags, small leather goods, scarves and accessories. Ms. Cartwright said sales in this division in the first half matched clothing sales in its retail stores for the first time.

She didn't provide specific figures for sales growth for accessories. But Burberry had said nonapparel sales for the year ended March 31 had grown to 33% of total sales, including wholesale and retail, up from 29% a year earlier.

The brand's growing share of sales from accessories is part of the strategy enacted by Chief Executive Angela Ahrendts in 2006 to boost results for underdeveloped product. The company has refined its product lines and put the global adverting spotlight on the boots, handbags and scarves that compliment Burberry's clothes. The division is the now fastest-growing product category in the company's stable.

While Burberry has managed to burnish its brand with a strong return of its iconic plaid pattern to the London catwalk last month and is increasing its own-store sales at a pace that belies the global economic downturn, the retail climate for department stores and other retails to which Burberry sells signals the full impact of the difficult economy.

Wholesale results are a lagging indicator, reflecting the fulfillment of orders made six months earlier to stock department-store shelves. And most department stores have been destocking their inventory in an effort to keep costs down.

Wholesale revenue fell 12% in the second quarter to £153 million. The figure tumbled 21% after adjusting for exchange-rate fluctuations.

Burberry said it expects that trend to ease somewhat in the second half, forecasting a 15% decline in wholesale revenue excluding currency effects.

The recent, expected declines in wholesale results are due in part to Burberry's own actions. The company's decision to close some brands and specialty accounts left around 7% of the decline in the hands of department stores.

That is still better than the department stores' plans for double-digit cuts in inventory buying, Ms. Cartwright said.

She added that in the U.S., in influential department stores such as Nordstroms, Saks Fifth Avenue and Bloomingdale's, Burberry is gaining market share.

Burberry, which has 102 retail stores around the world and 250 concessions, earlier this year slashed costs and cut its work force around 15% to save £50 million annually. It is slated to report its interim results Nov. 17.

Diageo posts lower sales, keeps outlook

By Michael Carolan

LONDON—**Diageo** PLC, the world's largest spirits company, surprised the market Wednesday with a drop in fiscal first-quarter sales.

The London-based maker of Johnnie Walker scotch, Guinness stout and Smirnoff vodka said its organic sales in the three months ended Sept. 30 declined 6% from a year earlier. That compared with flat sales in the year ended June 30. Organic sales strip out the effect of acquisitions, disposals and currency fluctuations.

While Diageo, the world's biggest alcoholic-drinks producer by volume, said the first-quarter sales drop was expected, most analysts had forecast a decline of less than 4%. Diageo shares closed down 2.1% in a higher London market.

"The year has started as we thought it would and we reiterate our guidance for low single-digit organic growth in operating profit in fiscal 2010," Chief Executive Paul Walsh said in a statement.

Evolution Securities analyst Simon Hales said the update was clearly negative. He added that the sales figure represents shipments to wholesalers and therefore didn't necessarily reflect the state of consumer demand.

Diageo's customers stocked up ahead of Christmas in the first quarter of the company's previous fiscal year. Since then, distributors have trimmed back their inventories as a result of the credit crunch—so the same level of inventory stocking was unlikely to occur this year.

Chief Financial Officer Nick Rose said he is confident the company's 6% first-quarter sales decline doesn't reflect consumer demand for its products.

"It isn't about underlying demand," he said on the sidelines of the company's annual shareholder meeting. "It's better to judge us at the half-year stage."

Mr. Rose said the lower-than-expected sales level reflected the lower inventory at the company's U.S. distributors compared with a year earlier.

"Once we've been through Christmas, this will all wash out," he added.

Last year, Diageo's sales in the first quarter were strong, rising 6%, only to drop sharply in the second and third quarters as the recession and credit crunch hit demand. Diageo warned in August that its first-quarter figures this year in particular would be weak.

The company is targeting low-single-digit organic operating profit growth in the current year—a sharp slowdown from Diageo's historic trends. As recently as January, it was targeting annual profit growth of between 7% and 9%.

In August, Diageo reported full-year profit growth at the bottom end of the company's target range and predicted even slower earnings growth in the year ahead, amid sluggish demand for premium drinks globally.

The company Wednesday said its restructuring program is on track to deliver £120 million ($190 million) in annual cost savings.

The benefits from less-expensive media rates were continuing, Diageo added.

BAE Systems Warns of Impairments

By Jonathan Buck

LONDON -- BAE Systems PLC warned Wednesday it may make significant impairments to goodwill and intangible assets due to the loss of a key U.S. contract, but said it continues to anticipate good growth in 2009.

The U.K. defense giant offered no new information on its dispute with the Serious Fraud Office, which is seeking consent from the attorney general to prosecute over allegations of bribery in contract awards in Africa and Eastern Europe.

BAE Systems said it continued to expend considerable effort seeking to resolve the matters, and maintained that it had at all times acted responsibly in its dealings with the SFO, which investigates complex crimes.

The company warned it might book significant impairments on goodwill and other intangible assets on its balance sheet after it learned in August that it had lost a U.S. Department of Defense contract for follow-on production of vehicles under the Family of Medium Tactical Vehicles program.

The program was part of the Armor Holdings Inc. business that BAE Systems acquired in 2007. As of June 30, the goodwill and other intangible assets carried in the company's balance sheet relating to the Armor acquisition amounted to £2.4 billion, or $3.81 billion.

BAE Systems in early September protested the loss of the contract. "The implications for the group cannot be fully assessed until the outcome of this protest has been determined," the company said Wednesday. The cash cost of the contract loss wasn't expected to be material.

Meanwhile, sales between July 1 and Oct. 13 were in line with expectations and results were seen benefiting from the pound's weakness, the company said.

During the period, BAE Systems said, it paid £100 million into its U.K. pension plan and $250 million into its U.S. plan as part of the incremental contributions announced earlier this year. The company expects to book a one-time gain of about $410 million in the second half as a result of further pension-benefit restructuring in the U.S.

The recent fall in the value of the pound against the dollar is likely to boost earnings translated from the U.S. currency into pounds. BAE Systems, one of the largest contractors to the U.S. Department of Defense, generates roughly 60% of its revenue in dollars.

Rio Tinto iron-ore production climbs 12% to a record

By Alex Wilson and Stephen Bell

MELBOURNE, Australia—**Rio Tinto** increased its forecast for iron-ore production after strong demand from steelmakers pushed third-quarter output to a record.

The miner said it expects to produce 210 million to 215 million metric tons this year, up from a previous projection of 200 million tons.

Third-quarter iron-ore output reached 47.5 million tons, up 12% from a year earlier and 5% from the second quarter. Production from the Pilbara region in Western Australia operated above its stated capacity.

The company saw "very strong demand from all markets" in the latest quarter, Sam Walsh, Rio's chief executive for iron ore, said in an interview. "Certainly Chinese demand has been very strong but we have also had a pick up across each of the other markets: Japan, Korea, Taiwan, Europe and North America."

Production of iron ore, a key steelmaking ingredient, is central to the Anglo-Australian miner's profit, contributing 76% of underlying earnings in the first half as sagging prices for base metals weighed on results in other divisions.

Mr. Walsh criticized the China Iron and Steel Association's call for a China-specific price for iron ore.

"It won't work in a benchmark system because, basically, steel producers are relying on the fact that there is one price across the world," he said.

Declining ommodity prices have hit Rio's aluminum division particularly hard, forcing it to cut back production. The company said 42% of smelting capacity for its most costly aluminum has been sold or shut down.

Third-quarter aluminum output fell 4% from a year earlier to 956,000 tons. Rio maintained its forecast for full-year output at about 3.8 million tons.

Production of refined copper production increased 46% to 100,600 tons.

CORPORATE NEWS

Soured mortgages weigh on GE

Bad loans in U.K. threaten to hurt giant's earnings

By Paul Glader

One of the biggest hits to **General Electric** Co.'s earnings on Friday will likely be its ongoing losses on subprime U.K. mortgages. But unlike its quick exit from U.S. mortgages, GE plans to hold steady in the U.K. in the hope of capitalizing on a projected housing shortage.

The looming losses on British mortgages highlight ongoing weakness in GE's finance unit, known as GE Capital, which investors will be watching Friday when GE reports third-quarter financial results.

Losses and writedowns at GE Capital have hobbled the conglomerate in the past two years. Analyst Scott Davis of Morgan Stanley expects quarterly profit at GE Capital to fall 94% from a year ago, contributing to a projected 57% decline in GE earnings.

Bloomberg News

GE expects to lose up to $2 billion from 2008 to 2010 on subprime U.K. mortgages. London property signs this summer.

GE said it expects to lose as much as $2 billion between 2008 and 2010 on subprime U.K. mortgages. As of July 28, 15.8% of its $23 billion U.K. mortgage portfolio value was 90 days behind payment, the company said.

That's more than six times the 2.4% delinquency rate on all U.K. mortgages, according to the Council of Mortgage Lenders.

But it is lower than other British subprime lenders.

GE's industrial businesses, meanwhile, which make such things gas turbines, wind turbines and aircraft engines, have kept the company earning money despite major losses at GE Capital, which in addition to the mortgage losses has taken hits on its private- label credit cards and its $80 billion commercial real estate portfolio.

GE's stock price, dragged down by the finance unit, has rebounded from a low of $6 in March to trade at $16.80 Wednesday afternoon, near the price it started the year.

The company is also expected to be one of the biggest recipients of money from the U.S. government's stimulus plan, aiming for as much as $100 billion from stimulus spending in the next three years from big-ticket items such as building a "smart" power grid, health-care technology and renewable energy.

GE Capital's consumer-finance unit, known as GE Money, acquired a series of British lenders beginning in 2001. The U.K. became GE's largest market for mortgage lending, accounting for roughly half its $60 billion global portfolio by 2008.

The U.K. operation dwarfed GE's move into U.S. mortgages, where it bought subprime lender WMC Mortgage in 2004, before selling it in 2007 after about $1 billion in losses. GE says it has a more conservative model in the U.K., where regulation is stricter on brokers and lenders.

The U.K.'s property boom matched that of the U.S. Mortgage debt as a percent of gross domestic product in the U.K. topped 80% in 2007, similar to the U.S., and was up from 40% in 1987. In 2007, 45% of U.K. mortgage borrowers didn't have to verify their income, according to the Financial Services Authority.

The subsequent 25% plunge in U.K. home prices effectively wiped out lenders such as **Northern Rock** PLC, now controlled by the U.K. government; HBOS PLC, now part of **Lloyds Banking Group** PLC; and Abbey National PLC, now part of **Santander** Group.

The companies GE Money acquired were aggressive lenders, specializing in loans to borrowers with patchy credit histories, loans where borrowers didn't have to verify income and mortgages for rental property, according to several mortgage experts in the U.K. GE says it improved the companies' lending practices.

"We compare very favorably" to other subprime lenders, says GE spokesman Russell Wilkerson. Fitch Ratings says 25% of mortgages to U.K. borrowers with impaired credit histories were more than 90 days delinquent in June, up from 13% in December.

GE says it employs sophisticated risk-management practices and was among the first U.K. lenders to consider borrowers' previous debts, as well as income, in making loans. Mr. Wilkerson says GE limited its self-certification loans to self-employed borrowers, and subjected those to some reviews.

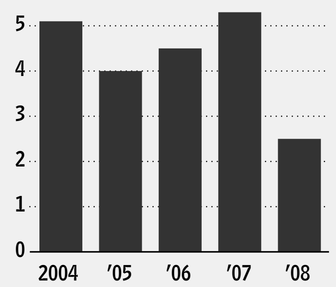
Earlier this year, GE ramped up foreclosures to get delinquent mortgages off its books.

Nonetheless, Mr. Wilkerson says GE is "committed to maintaining a presence in the U.K." even as competitors such as Citigroup Inc. and several British lenders have scaled back new business. "We believe the specialist mortgage market will recover, and this will be helped by the housing shortage in the U.K.," he says.

Analysts are mixed on the outlook for the U.K. market. "Home prices appear to have stabilized…and [U.K.] repossessions are already close to peaking," wrote JP Morgan analyst Bruce Kasman in a recent report.

A fixer-upper

GE Money's gross mortgage lending in the U.K.



Source: CML Research

But analysts at Fitch Ratings say "rising unemployment in Europe has not yet worked through" to delinquencies and foreclosures, particularly for subprime and nonconforming portfolios.

GE issued $26 million in U.K. mortgages in the first half of this year, compared with $5 billion in all of 2008. World-wide, GE said it plans to originate $1 billion or less in mortgages this year, down from $13.8 billion in 2008 and $25.4 billion in 2007.

BASF reports earnings drop, stays cautious

By Allison Connolly

FRANKFURT—**BASF** SE surprised investors by releasing third-quarter results early, saying that although sales and earnings fell from a year earlier, the figures were better than expected and showed an improvement from the second quarter.

BASF, the world's biggest chemicals company by revenue, tempered Wednesday's positive tone by noting that the recovery is "slow and remains fragile" and cautioning that markets have stabilized only at a low level.

Investors nonetheless reacted positively, sending shares in BASF and other European chemicals companies sharply higher amid hopes the worst is over for the sector.

BASF shares rose 7.4% in Germany to €40.61 ($60.22). Shares in Germany's Lanxess AG were 6.3% higher at €25.41, while Switzerland-based Clariant AG was up 7.3% to 11.03 Swiss francs ($10.78), and Belgium-based Solvay SA was up 3% to €73.50 in Brussels.

In its preliminary earnings statement, BASF said sales for the quarter ended Sept. 30 totaled €12.8 billion. That was down 19% from a year earlier but up 2.4% from the second quarter of 2009. Earnings before interest and taxes before special items totaled €1.25 billion—down 20% from a year earlier but 9.5% higher than the second quarter. The company didn't publish net-profit figures. It is to report final third-quarter results Oct. 29.

"The results are even higher than our already ambitious estimates," said UniCredit analyst Andreas Heine. "Whether recovery is sustainable is still a bit uncertain."

Some analysts said the resulting share-price rally seemed overdone given the third-quarter results are still well below year-earlier levels.

"Actually the figures don't come as a big surprise, as there have been signs that demand improved sequentially in the third quarter [from the second quarter] from depressed levels," said Helvea's Martin Flueckiger, adding that "currently there's a tendency in the market to interpret any news positively."

NordLB pointed out that BASF likely won't attain the earnings level of 2008, before the downturn took its toll, until 2012. The brokerage is sticking to its "sell" rating on BASF.

BASF said restructuring measures had a positive impact on its results. It also experienced growth in Asia, especially China.

Mr. Heine said chemicals demand in Europe also increased.

—Julia Mengewein in Zurich contributed to this article.

Redstone will pare his stakes in CBS and Viacom

By Nat Worden

Media mogul Sumner Redstone's privately held company, **National Amusements** Inc., said it will sell more shares in **Viacom** Inc. and **CBS** Corp. and reduce its voting control in both U.S. media conglomerates in order to pay off its $1.46 billion debt and hold on to the bulk of its movie-theater chain.

Facing a $500 million debt payment later this month, the company said Wednesday that it plans to sell about $600 million worth of Viacom shares and $345 million of CBS shares, along with some noncore assets, to pay off its creditors. A person familiar with the situation said Mr. Redstone is in the process of selling 35 U.S. movie theaters outside of National Amusements' core business in the Northeast.

National Amusements said it will sell all its nonvoting shares in both Viacom and CBS, and it will convert a portion of its voting shares into nonvoting shares and sell those as well. It intends to maintain at least three-quarters of the voting power at both companies, and said it has no intention of further reducing its ownership.

National Amusements' total equity holdings in Viacom will be reduced to between 6% and 8% from 10.6%, while its 10.5% interest in CBS will be cut to between 5% and 7%.

"As a result of our actions, National Amusements will be out of debt with its creditors and will still control its most important assets," Mr. Redstone said in a statement.

The stock sale is expected to pressure shares of both Viacom and CBS, which have risen strongly in recent months. In late-afternoon trading Wednesday on the New York Stock Exchange, Viacom shares were up 0.4% at $28.80, and CBS shares were up 2.1% at $12.41 in a broadly stronger market.

Last autumn, during the stock market's historic selloff, National Amusements was forced by lenders to sell $230 million worth of nonvoting shares in both companies. After that, Mr. Redstone said he didn't expect to be required to sell any more shares in either company. Then, when his company reached an agreement with creditors to restructure its debt last spring, National Amusements' Viacom and CBS holdings were included in a list of assets that the company could sell to meet its obligations.

National Amusements began negotiating a sale of part or all of its movie-theater business last spring to raise cash, but a person familiar with the process said Mr. Redstone was dissatisfied with the offers for the theaters.

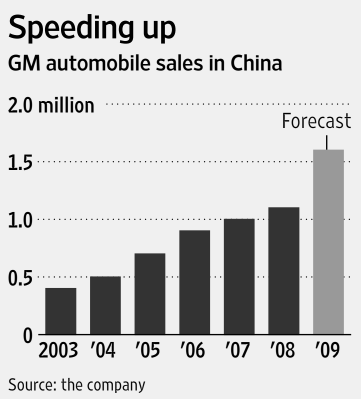
Meanwhile, Mr. Redstone has had a public spat with his daughter, Shari Redstone, who runs the theater business, further complicating the situation.

UBS analyst Michael Morris said Wednesday's announcement will "remove an overhang from the stocks and likely provide a buying opportunity for the most attractively priced stocks in major media."

—Nathan Becker and George Stahl contributed to this article.

THE WALL STREET JOURNAL.
EUROPE
Executive Travel Program
Guests and clients of 320 leading hotels receive The Wall Street Journal Europe daily, courtesy of
THINK MEDIA OUTDOOR
www.thinkmediaoutdoor.be

Associated Press



◀ General Motors CEO Fritz Henderson at a Chinese dealership in Shanghai

GM sees big China growth

Sales should rise 47% from a year ago, car maker says

By Patricia Jiayi Ho

BEIJING— **General Motors** Co.'s sales in China this year will likely exceed 1.6 million vehicles, said Kevin Wale, president and managing director of GM China Group.

The forecast represents an increase of about 47% from last year, when GM's total vehicle sales in China rose 6.1% to 1.09 million. GM in September forecast its China sales growth would exceed 40% this year.

GM sold 1.29 million vehicles in China in the January-September period this year, up 56% from the same period last year. GM counts sales of Wuling commercial vans, produced by a joint venture of which GM owns a third, as part of its overall sales.

By comparison, **Toyota Motor** Corp.'s sales in China have suffered this year after a failure to anticipate the demand for smaller cars. The Japanese auto maker's China sales from January through August rose 9% from a year earlier to 415,000 vehicles.

Toyota has said it seeks to raise its 2009 sales in China slightly from 2008 levels, when its sales rose 17% to 585,000.

Car makers in China have benefited from Beijing's policies to boost sales, including tax incentives for purchases of vehicles with engines of 1.6 liters or smaller, and subsidies to encourage sales of some autos in rural areas. Both policies are set to expire at the end of the year.

GM's sales performance in China could prove especially vulnerable to changes in government policy, as all of the vehicles sold by its Wuling joint venture with **SAIC Motor** Corp. and Wuling Automobile Co. qualify for the small-engine tax cut. Sales by the venture accounted for more than 60% of GM's volume in China in the January-September period.

Mr. Wale said he is confident the Chinese government will take appropriate actions next year to maintain stability in the country's auto market, which is on track to overtake the U.S. as the world's largest car market this year. Mr. Wale also said demand from smaller cities "should ensure some growth momentum."

GM aims to increase its Chinese sales volume next year at a slightly faster rate than that of the overall auto industry, he said.

Tuesday, GM Chief Executive Frederick "Fritz" Henderson, on his first trip to China since GM emerged from bankruptcy in July, said China plays an increasingly important role in GM's global operations.

Mr. Wale echoed those remarks Wednesday. "China is a key part of GM's future strategy. It is currently the largest and fastest growing market in the world," he said. "We will continue to put priority on our success here in China."

GM executives have repeatedly extolled China's significance but haven't quantified how much revenue comes from the country.

The China Association of Automobile Manufacturers said Tuesday that China's passenger-vehicle sales in September rose 84% from a year earlier to 1.02 million.Tota vehicle sales from January through September rose 34% from a year earlier to 9.66 million. The association expects overall auto sales for the whole year to exceed 12 million.

Mr. Henderson said Tuesday that GM plans to launch a new Chevrolet Sail by the Lunar New Year in mid-February, designed and developed primarily by the Pan-Asia Technical Automotive Center Co., or Patac, an automotive design and development joint venture between GM and SAIC Motor in Shanghai.

Mr. Henderson said the compact Sail "has been developed for customers in China and has great potential for other customers in emerging markets." GM said in August that its Wuling joint venture will expand exports of two microminivans produced in China,.

Other auto makers also have come up with small, no-frills cars targeted at emerging markets. **Ford Motor** Co.'s recently unveiled Figo, to be made in India, will be exported, as will be **Renault** SA's low-cost Dacia models.

Separately, GM's Thai subsidiary said it has reached an agreement with striking assembly workers that will allow production to resume Thursday at its factory in Rayong province, the Associated Press reported. Production had halted Oct. 5.

P&G takes on taboo with Web campaign

By Jonathan Cheng

To promote its line of feminine sanitary products in Singapore, **Procter & Gamble** Co. is taking on a cultural taboo.

P&G has gone online in an effort to instill a positive attitude in young Singaporean women about their menstrual periods, seeking to dispel some of the squeamishness toward the subject that persists in much of Asia. In doing so, it hopes to win the loyalty of a new generation of customers for Whisper, its Asian brand of sanitary napkins.

Whisper currently has a 22% market share in Singapore, just behind **Kimberly-Clark**'s Kotex brand, which has a 23% share, according to market researcher Euromonitor International.

Whisper's new campaign, called "Happy It's Here!," began in early September and involves an interactive Web site on which users can post real-time comments among smiling clouds that say, "It's here!" It also includes a group on social-networking site Facebook.

"I love my life, and I'm proud to be me," one poster wrote on the Web site www.happyitshere.com. Another wrote, "I have a reason to pamper myself with chocs!"

P&G says the comments are unedited, but it reserves the right to remove expletives.

In recent years, P&G has adopted a more direct approach to marketing its global female hygiene brands, Always and Tampax, seeking a bigger piece of a world-wide market Euromonitor estimated at $3 billion last year; Singapore accounted for about $32.2 million of that total.

In the U.S., P&G has relied in part on cheeky TV commercials that exhort women to "Outsmart Mother Nature" or "Have a Happy Period." But in Singapore, where much of the TV audience might be shocked by such slogans, P&G is trying a different tack, using the Internet to prod younger women to talk openly about their menstrual cycles, while also providing health tips and debunking menstrual myths.

"We see our role as being over and beyond just selling the products," says Sujay Wasan, associate marketing director for P&G's feminine-care division in Asia. "Periods are not a necessary evil, or a curse, or a problem to be solved. It's an absolutely natural part of being a woman, and it needs to be appreciated and celebrated," he said.

The main feature of the "Happy It's Here!" Web site, which is heavy on pastel colors, is a calendar on which a young woman can enter the date her last cycle began. That generates day-by-day advice on when such symptoms as insomnia or sensitive skin might be a problem, and tips on how to cope. (When mood swings are a problem, it says, "Offer to take the neighborhood dogs out for a walk. You'll get a fun workout at the same time!")

The site carries a small Whisper logo in the bottom corner, with little smiling clouds that can be downloaded as emoticons or wallpaper desktops.

The Facebook page comes with an application that allows users to send uplifting mesages to one another and a "Happy It's Here!" badge to pin on one's personal Facebook page. On the group page, young women ask for advice, like whether exercising should be avoided during "that time of month." (The consensus: light exercise is great.)

The Singapore campaign, which like P&G's global campaign, is overseen by **Publicis Groupe**'s Leo Burnett Co., stemmed from a survey of 500 young women in the city-state. It found that they had many misconceptions about their periods—for instance, that they increased thirst and caused poor eyesight. Only 5% of respondents said they felt happy at the onset of their cycles.

Nick Handel, regional director of digital for Leo Burnett, says the initial response has been encouraging. Last month, the agency began buying "unobtrusive" ads on Facebook and instant-messaging program MSN Messenger that promise to reveal "secrets of the cycle." Clicking on the ad leads to the Web site. The agency also has recruited several female bloggers to document their cycles, day by day. "A key pillar of our campaign is for women to appreciate their period by defining how the cycle is a part of their life," Mr. Handel says.

Abbott's net rises as Humira rebounds

By Peter Loftus

Abbott Laboratories' third-quarter profit rose 36%, helped by higher sales of nutritional products and heart devices and accelerating sales growth for the company's top drug, arthritis treatment Humira.

The earnings exceeded Abbott's forecast, and the company boosted its outlook for the year.

The Abbott Park, Ill., company has enjoyed solid sales and profit growth in recent years, avoiding some of the pitfalls affecting its rivals in the pharmaceutical industry. But Abbott pins much of its growth on certain products, including Humira, sales growth of which slowed earlier this year. Abbott shares are down about 7% year-to-date, though they have been on the rise in recent weeks. Abbott shares were up 3.4% in Wednesday afternoon trading on the New York Stock Exchange.

To diversify, Abbott has made a series of acquisitions, including agreeing in September to purchase Solvay SA's pharmaceutical unit for $6.6 billion.

Abbott on Wednesday reported earnings of $1.48 billion, or 95 cents a share, compared with $1.09 billion, or 69 cents a share, a year earlier. Excluding items, earnings rose 17% to 92 cents. Abbott in July forecast earning 88 cents–90 cents a share on that basis.

Net sales increased 3.5% to $7.76 billion. Unfavorable currency-exchange rates sliced 4.9 percentage points from growth.

Sales in Abbott's biggest division, pharmaceuticals, declined 1.6% to $4.06 billion. U.S. sales fell 6.6%, and non-U.S. sales rose 3.8%. But sales of Humira rose 24% to $1.49 billion, accelerating from earlier in the year when sales growth for the arthritis drug slowed because of currency fluctuations and rising co-payments for some patients.

Abbott forecast that Humira's sales would increase 18%–20% this year, compared with the 15%–20% forecast previously. Abbott began the year forecasting that Humira's sales would rise 25%.

Sales of HIV drug Kaletra fell 8.7%, combined sales of cholesterol drugs TriCor and Trilipix fell 1%. Sales rose 11% for cholesterol drug Niaspan. Sales of epilepsy treatment Depakote plunged 71% because of competition from generic drugs.

Sales of nutritional products, including Similac baby formula, rose 9.8% to $1.39 billion.

Sales of Abbott's diagnostics products declined 0.3% to $909 million.

Sales for Abbott's vascular products—which include the Xience V artery-opening stent—rose 4.7%, a marked slowdown from recent quarters. Xience was introduced in the U.S. in the summer of last year, so the most-recent quarter was the first with meaningful year-earlier comparisons for Xience.

Abbott raised its forecast for full-year earnings to $3.70–$3.72 a share excluding items from $3.65–$3.70.

Anheuser-Pepsi purchase pact

By Aniali Cordeiro
And Kathy Shwiff

Anheuser-Busch Inbev NV and **PepsiCo** Inc. agreed to jointly purchase goods and services for their U.S. operations to get more competitive prices.

The purchases may include computer hardware, office supplies, travel services, transportation, maintenance, repair and operating supplies.

While it is unusual for large independent companies to make joint purchases, Anheuser-Busch InBev and PepsiCo go back a long way. AmBev, which is part of the Belgian brewer, is a PepsiCo bottler in Brazil and several other Latin American countries.

Still, the pact raises questions about how the companies could collaborate even further, possibly taking advantage of their distribution capabilities. Industry watchers have often speculated about the possibility of a wider collaboration between the two beverage companies, although there are no signs that latest pact will translate into anything bigger in the near future.

In an e-mail statement, Anheuser-Busch InBev said the agreement "is nothing more than joint purchasing in the United States for goods and services for use primarily in U.S. operations."

No further joint activities are being contemplated at this time, the brewer said.

PepsiCo spokesman Dick Detwiler said the two companies were focused purely on jointly purchasing indirect goods and services. The deal won't involve commodities, he said.

Procurement experts for each company will focus on common areas of spending and negotiate purchases on behalf of both.

ECONOMY & POLITICS

Palestinian support for troops wanes

Morale of American-trained security forces is eroding along with popular sentiment for them and President Abbas

By Charles Levinson

Jaafar Ashtiyeh/AFP for The Wall Street Journal

Palestinian security forces take part in exercises in the West Bank city of Nablus in August.

QALQILYA, West Bank—Commanders of the U.S.-trained Palestinian security forces who have been locking up criminals and battling Hamas militants here for nearly two years have maintained morale in the ranks with a single promise: They will one day be the anchor of security for an independent Palestinian state.

The lack of progress toward that goal is starting to sap Palestinian public support for the forces and erode morale among troops, even as they win praise and fresh funding from Washington for their accomplishments.

Meanwhile, the more the Palestinian Authority Security Forces cooperate with the U.S. and Israel to suppress Hamas, the more they threaten to undermine popular support for Palestinian President Mahmoud Abbas—who is key to Washington's Mideast peace effort.

Popular anger at Mr. Abbas has already boiled over because of a series of concessions he made to Israel, under U.S. pressure, including his decision to withdraw support for a United Nations report that alleged Israeli war crimes in Gaza. Mr. Abbas later reversed the decision, and supported the report. Israel has denied its forces acted improperly.

Many Palestinians applaud the PASF's success in boosting security in the once-lawless West Bank, which is dominated by Mr. Abbas's Fatah party.

Dov Schwartz, an aide to U.S. Lt. Gen. Keith Dayton, who is overseeing the PASF training program, says "the Palestinians have undertaken a serious and sustained effort to return the rule of law to the West Bank. People now feel safe."

Gen. Dayton has graduated about 2,100 paramilitaries in the nearly two years his training program has been under way. Recruits are trained in Jordan by Jordanian police, under the supervision of American, Canadian and British officers. The trainees stand out from the West Bank's often poorly equipped and disheveled security services. They sport crisp olive uniforms and carry well-maintained AK-47s supplied by other countries, including Jordan and Egypt.

Gen. Dayton said he hopes to eventually train over 5,000 men, out of a total West Bank security force of roughly 25,000.

The forces won exceptional praise from Israeli officers for their effectiveness keeping a check on protests in the West Bank during the December-January Gaza War. Since then, day-to-day cooperation between Palestinian and Israeli security officials has improved dramatically, Israeli military officials say.

"They won the battle for public order, but I am concerned they may not have won the battle of public opinion, and were seen as protecting the Israeli army," says Paul Kernaghan, who leads the European Union team training Palestinian police officers.

In an incident last fall, Palestinian forces swept into a West Bank town on the heels of the Israeli army—only to be chased out by angry residents. An internal memo distributed among the Gen. Dayton's training team after the incident warned: "There are growing signs that the local population are increasingly losing respect for the PASF."

In Qalqilyah, on May 31, the PASF engaged in an all-night shootout with Hamas, leaving two Hamas militants, three PASF members and a bystander dead. After the shootout, hundreds of angry Palestinians took to the streets. "Dayton's Army serves the Jews," Subea Abu Yussuf, a 24-year-old law student, shouted at a PASF officer.

The confrontation put the PASF on the defensive. As dusk settled, a Palestinian major tried to buck up his troops. "We didn't join the Palestinian security forces to fight Hamas or train with the Americans," he said. "We came here to serve our homeland and build our state." His subordinates quietly nodded.

Today's Palestinian security forces were born out of the Palestine Liberation Organization's guerrilla army, founded 45 years ago to fight Israel. After the Oslo Peace Accords in 1994, thousands of exiled fighters returned to the Palestinian territories and formed the nucleus of a nascent, often-unwieldy security apparatus.

Under Palestinian leader Yasser Arafat, founder of the Fatah party, the forces included at least 13 independent branches. In the years after Oslo, the Arafat-commanded forces launched crackdowns on Hamas and other militant groups that opposed the peace process.

"At first, everyone was highly motivated," says Col. Said Najjar, a PASF commander who in the 1990s was a lieutenant. "I slept in my shoes and worked constantly to make Palestine safe, because we had been promised an independent state within five years in return."

Throughout the latter half of the 1990s, as an Israeli-Palestinian peace deal looked increasingly remote, Col. Najjar says his soldiers grew disillusioned. Operations against Hamas and other anti-Israel groups appeared at odds with a Palestinian public that increasingly viewed him and his men as doing Israel's bidding and getting little in return.

After the failure of the Camp David peace talks in 2000, the second Intifada, or Palestinian uprising, erupted. Many members of the security services turned their guns on Israel.

One of Col. Najjar's soldiers, Sgt. Jihad Qabaha, went to Israeli prison in 1999 for throwing a Molotov cocktail at an Israeli jeep. He says he gave up fighting Israel after he was released from prison in 2002, and joined the PASF.

In January, Sgt. Qabaha, who is now 31 years old, graduated from Gen. Dayton's training camp beaming with pride. His trainers told trainees they were at the vanguard of efforts to build a Palestinian state.

Since then, family members and friends have asked dispiriting questions about his loyalties. While he was on leave recently, his 21-year-old sister criticized the PASF for arresting Palestinians. "People say the security forces are working for the Israelis," she said disapprovingly.

"I know that Palestinian statehood will only come by serving this way, not with force, but it's hard when the people you love question what you're doing," says Sgt. Qabaha.

Solidarity faced a Herculean task in cleaning up Poland

As we approach the 20th anniversary on Nov. 9, we will chronicle the events that precipitated the fall of the Berlin Wall as they played out in the pages of The Wall Street Journal.

On Oct. 13, 1989, Poland plotted a rush toward capitalism after 45 years of communism. The new Solidarity-led government unveiled an economic program aimed at introducing free-market mechanisms and capitalist institutions "in the swiftest possible way."

East and West
As the Berlin Wall Fell

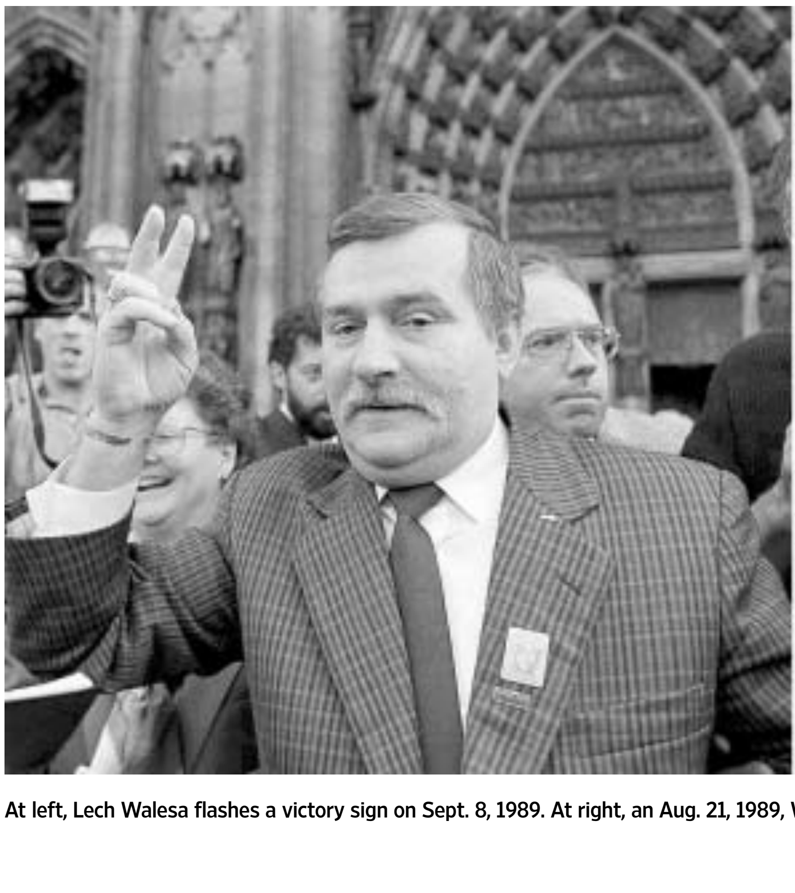
The program, which included restoring private property and other forms of nonstate ownership, was the first step in what was clearly going to be a tough economic restructuring.

During the summer of 1989, the independent trade union Solidarity had given rise to a broad anticommunist movement. Now, having achieved the highly unlikely task of being asked to form the East bloc's first non-Communist government in more than four decades, the party attempted the impossible.

"The nine-year-old labor union, outlawed until just four months ago, has to quickly clean up an economic basket case of a country without being able to control the police, the army or the huge bureaucracy, all of which remain with the politically discredited but still powerful Communist Party," the Journal wrote on Aug. 21, 1989. "The entire East bloc, and in particular the Soviet Union, is watching anxiously to see if Poland can make the painful shift to a market-dominated economy without setting off massive unrest."

The government knew that the program would be difficult, with industrial recession and unemployment a given. They predicted it would be a year before Poland's hard-pressed people saw any signs of improvement. But Solidarity asked the public, parliament and major political and labor groups to give the plan a chance.

In one example, Solidarity leader Lech Walesa encountered a gang of young hecklers who shouted, "We want bread, not a prime minister." Mr. Walesa replied: "If you know how to make bread, come forward. Poland must be built. Bread must be baked. Change requires effort."



Associated Press

Taking Charge

No Longer an Outsider, Solidarity Must Face Poland's Economic Ills

Food Shortages, Debt Burden Call for Painful Reforms That Could Stir Unrest

The Communists' New Role

By Philip Revzin And Barry Newman
Staff Reporters of The Wall Street Journal

GDANSK, Poland—Leaders of Solidarity, the trade union that suddenly finds itself the Polish government, came home to Gdansk from Warsaw yesterday to do what they have always done during nine years of struggle.

They prayed.

In Solidarity's home church, St. Brygida, a packed Sunday Mass applauded through tears as parish priest Henryk Jankowski introduced Solidarity leader Lech Walesa and Poland's prime minister-designate, Tadeusz Mazowiecki.

"Gdansk will pray for you. Poland will pray for you," intoned Father Jankowski

At left, Lech Walesa flashes a victory sign on Sept. 8, 1989. At right, an Aug. 21, 1989, Wall Street Journal article.

Poland expects delay in adopting the euro

Central banker says target date likely will be 2014 or 2015

BY MALGORZATA HALABA AND MARCIN SOBCZYK

WARSAW—Poland won't be able to adopt the euro until 2014 or 2015, said a Polish central banker, in comments that reminded markets that the country is failing to meet all but one euro-adoption criteria and it can't start formal talks on abandoning the zloty anytime soon.

"Poland will not have the euro probably before 2014 or 2015," said Halina Wasilewska-Trenkner, according to Polish daily Dziennik Gazeta Prawna. Ms. Wasilewska-Trenkner is a member of the National Bank of Poland's Monetary Policy Council.

Representatives for the finance ministry and the central bank declined to comment on her statement, but the central bank spokesman pointed to its latest report on Poland's progress toward the euro zone.

In that report, the central bank declined to offer a possible euro-adoption date. Instead, it said adopting the euro could boost Poland's gross-domestic-product growth by 7.5 percentage points over the long term, although most of the risks—including higher inflation and economic slowdown—would materialize shortly after the switch to the common currency.

When Prime Minister Donald Tusk last year set 2012 as a euro-adoption target, Poland was widely expected to become the euro zone's next entrant, following Slovenia and Slovakia. Poland is the largest country from the 10 mostly post-communist states that joined the European Union in 2004.

But the government in July dropped the 2012 target after a period of volatility against the euro and decided against setting a new date amid the global financial crisis. Mr. Tusk said at the time that the government remains upbeat about the euro but that setting a new date then would be risky.

To join the euro zone, Poland needs to meet criteria set out in the EU's Maastricht Treaty, after which it would have to stay for two years in the European Exchange Rate Mechanism, an ante-room to adopting the currency.

Currently, Poland complies only with the criterion that applies to interest rates, the finance ministry said in its monthly report for October.

Poland doesn't meet the Maastricht Treaty's requirement that a country's budget deficit must not exceed 3% of GDP. The budget shortfall was at 3.9% of GDP in 2008 and is expected to widen in coming years. According to the finance ministry, the government's deficit will rise to 6.6% of GDP in 2009 and to 7.3% in 2010. EU rules require Poland to reduce the deficit by 2012.

In addition to budgetary compliance, Poland needs a stable currency, low inflation and political consensus to join the euro. None of these criteria has been met.

Separately, the European Commission warned Britain and four other EU nations that their economies are at high risk because soaring public debt may hurt their ability to meet future needs, such as paying pensions.

It told all EU nations that they couldn't rely on fast economic growth to reduce debt because Europe faces a problem that will "dwarf the effect of the crisis many times over"—an aging population where fewer workers will pay higher pension and health care costs for more retirees.

This means that governments have little choice but to make budget cuts and labor-market changes that could raise potential growth, it said.

It highlighted Britain, Spain, Greece, Ireland and Latvia, saying the impact of the downturn on their public finances and growth in the next few years was a "serious concern." British government debt is swelling at the fastest rate of the Group of Seven industrialized nations, and borrowing is forecast to reach a record £175 billion ($277 billion), or 82% of GDP next year.

—The Associated Press contributed to this article.

SUBSCRIBE AND SAVE UP TO 60%

The Wall Street Journal Europe Print and Online for just €2.94 a week

Subscribe today and receive up to **60% off the cover price.**

Your subscription includes:

- The Wall Street Journal Europe **print edition** delivered directly to your home or office every business day
- **Full access to WSJ.com** on your desktop or mobile. Our new Europe edition offers a global perspective with laser-sharp European focus
- **WSJ.** our quarterly lifestyle magazine
- **Special Reports** and supplements

To subscribe visit www.services.wsje.com/AW09 or complete the form below

THE WALL STREET JOURNAL EUROPE.

business | europe | asia | world | analysis | tech | markets | comment

know more

☐ **YES!** Please start my subscription to The Wall Street Journal Europe with 12 months at the special low rate of **€153 a year - that's up to 60% OFF the standard rate and just €2.94 a week!** **OFFER CODE: APAH000AL**

Title ________ Full name ______________________

Address ______________________

Country ______________ Zip ______________

Email ______________________

Telephone ______________________

☐ **Charge my Credit Card:**

Visa ☐ Amex ☐ Eurocard ☐ MasterCard ☐

Card Number: ☐☐☐☐ ☐☐☐☐ ☐☐☐☐ ☐☐☐☐ Expiry ____

Signature ____________ Date ____________

☐ **Invoice Me/My company**

POST THIS COUPON TODAY The Wall Street Journal Europe, Stapleton House, 29-33 Scrutton Street, London, EC2A 4HU.
OR CALL +44 (0) 207 309 7799 OR VISIT www.services.wsje.com/AW09

We may provide your information to third parties, including companies outside of the EU, in order to fulfill your subscription request, process data and provide you with promotional information from WSJE, its affiliates and other carefully selected companies. ☐ I do not wish to receive promotional materials from other carefully selected companies. ☐ I do not wish to receive promotional materials from WSJE or its affiliates. Hand delivery subject to confirmation by local distributor. Offer only open to new subscribers. Please allow up to 2 weeks for delivery to commence.

DOWJONES A NEWS CORPORATION COMPANY

© 2009 Dow Jones & Company Inc. All rights reserved

Palestinians, Israelis clash over U.N. report

BY JOE LAURIA

UNITED NATIONS—Israel and the Palestinian Authority clashed during a debate in the Security Council on Wednesday over a U.N. report that accuses both Israel and Hamas of committing war crimes in last winter's conflict in Gaza.

The United Nations investigation, conducted by a commission headed by South African jurist Richard Goldstone, concluded that "Israeli operations were carefully planned in all their phases as a disproportionate attack designed to punish, humiliate and terrorize" Gazan civilians, more than 1,400 of whom were killed.

In its findings, the Goldstone commission accused Gazan authorities of the war crime of firing 8,000 rockets since 2001 indiscriminately at Israeli civilians. Israel says it launched an effort, called Operation Cast Lead, to stop the rocket fire, which killed three Israeli civilians.

The report recommends that the Security Council give Israel and Hamas six months to conduct internal investigations into the report's war-crimes charges or have their cases sent to the International Criminal Court in The Hague.

Gabriela Shalev, Israel's ambassador to the U.N., said the peace process would remain on hold as long as the international community considered the Goldstone comission report.

"This Goldstone report is an obstacle to the peace process," she told reporters after addressing the Security Council. Ms. Shalev said the report "puts us and Hamas on the same level and this is something we are not going to accept."

Earlier, Riad al-Malki, the Palestinian Authority's foreign minister, said peace couldn't be achieved without implementation of the report.

Aked how the two views could be reconciled, Mr. al-Malki said that Israel was using the Goldstone report as an excuse not to resume talks. "If there were no such report, the Israelis would have looked for something else," he said.