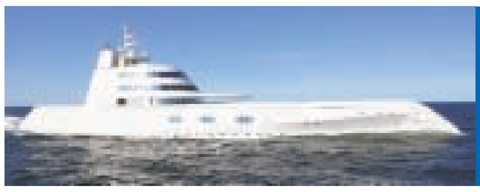

Taking an exclusive tour aboard oligarch's $350 million yacht
WEEKEND JOURNAL

The airline that knows way round volcanic ash clouds
C-SUITE 27

THE WALL STREET JOURNAL.

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DOWJONES A News Corporation Company | europe.WSJ.com

A broadcast of President Barack Obama's speech on the financial industry Thursday catches the attention of a trader at the Goldman Sachs Group Inc. booth at the New York Stock Exchange.

Bloomberg News

EU questions Greek figures, bailout looms

By Charles Forelle

BRUSSELS—New figures revealed that Greece's debt crisis is even worse than investors believed, leading to a fresh shock throughout European markets and all but ensuring that the International Monetary Fund and euro-zone countries will have to step in within weeks to bail out the country.

In Athens, where IMF and European officials are meeting with the Greek government, attention focused on preparing for a bailout. Time is short: Greece must repay €8.5 billion ($11.4 billion) in borrowings on May 19, a sum it doesn't now have.

"It is probably only a matter of days" before Greece asks for such help, Commerzbank analysts said.

The European Union's statistical authority said Thursday that Greece's 2009 budget deficit—already yawning—was wider than Athens had estimated. Also Thursday, Moody's Investors Service downgraded Greece's debt rating.

Those twin developments sent Greek bond prices into a tailspin, all but dashing any remaining hope that Athens could continue funding its operation by borrowing afresh from international markets. These prices, an indication of investors' sentiment toward the borrower, showed a marked shift toward the belief that Greek bondholders won't get all of their money back. Markets, in other words, are pricing in the probability that even after a bailout goes ahead, Greece will also default on debts and seek to renegotiate with creditors.

"The market has concluded that a restructuring is much more likely than it previously was," says Ken Wattret, an economist at BNP Paribas in London.

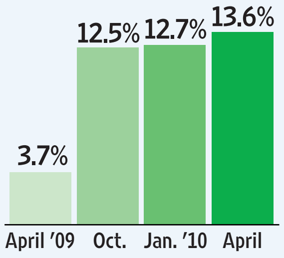
Officials have been trying to squelch those thoughts; International Monetary Fund chief Dominique Strauss-Kahn said Thursday that the fund, which would join any EU bailout, isn't considering restructuring.

Greece's original problems were born of faulty statistics, and the warning from the Eurostat agency left investors worried that the figure-fudging—which Greece promised was behind it—isn't entirely straightened out.

Please turn to page 3

Greek mathematics

Changing estimates of Greece's 2009 budget deficit as a percentage of GDP



Source: Eurostat

Obama reprimands Wall Street

By Jonathan Weisman and Damian Paletta

President Barack Obama returned to Manhattan's Cooper Union college on Thursday, two years after a campaign speech that laid out his vision for Wall Street, to castigate a financial industry that he said has too often forgotten the ordinary Americans who have suffered from its reckless irresponsibility.

The speech comes at a pivotal moment in Senate negotiations over a sweeping measure to re-regulate the financial industry. After trading barbed accusations, senators from both parties now say they are near a deal that would preserve the framework of Mr. Obama's plan. By appearing just two miles from Wall Street, Mr. Obama hopes to raise the political pressure and seal the deal.

"A free market was never meant to be a free license to take whatever you can get, however you can get it," Mr. Obama said. "That's what happened too often in the years leading up to this crisis. Some—and let me be clear, not all—but some on Wall Street forgot that behind every dollar traded or leveraged there's family looking to buy a house, or pay for an education, open a business, save for retirement. What happens on Wall Street has real consequences across the country, across our economy."

As he has done several times in the year-long debate, the president implored industry executives to call back the lobbyists engaged in "furious efforts" to thwart or water down his legislation.

"I'm sure that some of these lobbyists work for you and they're doing what they are being paid to do," he said. "But I'm here today specifically—when I speak to the titans of industry here—because I want to urge you to join us, instead of fighting us in this effort. I'm here because I believe that these reforms are, in the end, not only in the best interest of our country, but in the best interest of the financial sector."

For the first time recently, Mr. Obama didn't threaten to veto the bill if it didn't come up to his standards, a marked change in tone. He made that threat during his State of the Union address and again as recently as a few days ago. That suggests the White House feels the long process of securing the overhaul is close to completion.

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The Quirk

From the North Pole down to Morocco, stamp collecting is hot competition. Page 29

World Watch

A comprehensive rundown of news from around the world. Pages 30-31

Editorial & Opinion

Will Germany's FDP shake its past and get tough with Iran? Page 13

U.K. debate focuses on foreign policy

LONDON—Leaders of the Britain's three main political parties faced off on foreign-policy Thursday in the second of three televised debates, as they sought to win over wavering voters in the country's tightest political race in almost 20 years.

Before an audience of about 150 people in Bristol, southwest England, Liberal Democrat Nick Clegg sought to portray himself as an alternative to the two parties that have traded power for most of the 20th century.

Mr. Clegg, who saw his party's poll ratings surge after a strong performance in last week's debate, which was watched by 9.4 million viewers, faced fire from Prime Minister Gordon Brown of the Labour Party and Conservative leader David Cameron, who began the campaign in a strong position to regain power for his party after 13 years in opposition.

The debate's focus on foreign affairs was a departure for a very close political campaign so far dominated by the economy and a parliamentary expenses scandal.

Full article on page 5

U.K. Election 2010
WSJ.com/UKElection

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It's not about the economy, stupid, it's the voters' urge to kick politicians

[Agenda]

By Martin Vander Weyer

The economy was supposed to be the big issue in the U.K. election. "Tory cuts mean double-dip recession" and "We made the right calls during the banking crisis" were, and forlornly still are, the twin pillars of Labour's campaign. Conservatives thought they had a winner when they put Gordon Brown on their posters saying "I doubled the National Debt. Vote for me." The Liberal Democrats best shot was "Our economics spokesman Vince Cable is the wisest owl in Westminster."

But that's not the way it looks now. Lib Dem leader Nick Clegg, barely a contender at all before last week's leaders' debate, has become the nation's pin-up—and it seems to matter little what he says about the economy, because it is not his party's incoherent ragbag of left-of-center policies that are attracting attention, except perhaps his promise to tax "greedy bankers" to the hilt.

Instead, voters seem to have decided—at least on current poll showings—to treat the election as an exceptionally shallow TV talent contest, and in doing so, to cast a nihilistic vote against parliament itself, as punishment for the expenses scandal. Just as Labour backbenchers decided out of mischief to elect the widely disliked John Bercow as Speaker of the House of Commons, so the electorate at large now says it will throw votes at a man of whom they know next to nothing but who isn't David Cameron or Gordon Brown. It's a turn of events no pundit or pollster foresaw: It has set the election alight and raised the prospect of a chaotic hung-parliament outcome.

But let's not forget the received wisdom of past elections everywhere, summed up in that famous Clintonian phrase: "It's the economy, stupid." Whatever voters may say beforehand, the theory goes, most make their choice in the privacy of the polling booth on the basis of their own economic interests.

Reuters

Stranded at airports, but Britons show signs of more discretionary spending.

So we must surely expect to see some tailing off of the febrile Lib Dem surge, and an uptick in the suddenly shrunken Conservatives share.

> **Voters seem to have decided to treat the election as an exceptionally shallow TV talent contest**

Or will we? Alongside the public mood of "a plague on both your houses" that has wrong-footed Tories and Labour alike, there seems to be a second message coming through. The state of the economy, and in particular the fear of double-dip recession and an extended period of austerity, does not loom nearly as large as an issue on the doorsteps of marginal provincial constituencies as it does in Westminster.

On a day when the headline figure for public borrowing in the financial year just ended was revealed as £163 billion—a catastrophic sum, even if slightly lower than the chancellor's budget forecast—that must mystify those watching this U.K. election from elsewhere. This confirmation of an unprecedentedly deep hole in public finances comes on top of a 15-year peak in unemployment, at 2½ million in February, and weaker than expected retail sales in March. How can such a dismal picture not matter to voters more than the issue of whether Mr. Clegg looks more relaxed than Mr. Cameron, or which of them has the foxier wife? Has the electorate taken leave of its senses as well as its democratic responsibilities?

Well, underlying this phenomenon I believe there is a disconnect between statistics and ordinary people's experience. We have just come through "the worst recession in living memory"—in a peak-to-trough GDP-numbers sense, but not in terms of personal pain or (except in the darkest moments of the 2008 banking crisis) fear. This has not been like the mid-1970s, when the lights went out, inflation soared and life was halted by a succession of industrial disputes.

It has not been like the early '90s, when interest rates were cripplingly high, hundreds of thousands of homeowners faced negative equity or repossession, and unemployment hit three million. In this recession, many people have had to adjust to short-time working or lower pay, but rock-bottom interest rates have helped keep money in their pockets—and whatever the retail stats may say, shops, theaters, cinemas, pubs and restaurants are mostly doing satisfactory trade. Perhaps the most revealing fact from this week's airline crisis has been that 150,000 Britons were stranded abroad, the great majority of them on holiday: That suggests ample cash for discretionary spending. It just hasn't been that bad.

Meanwhile, the National Debt is no more than a big abstract number in the public psyche. We all know that whoever wins the election will sooner or later have to make severe spending cuts, which must mean public-sector job losses, to bring the public finances back towards balance. But none of the three parties (least of all the Lib Dems) has been frank or specific about where the cuts will fall. David Cameron and George Osborne in particular have failed to make a persuasive case that they hold any magic formula for future prosperity and fiscal rectitude. Not seeing any clear difference between Labour and the Tories on the issue of economic competence, not feeling the pinch as much as they had been told they would, voters have decided to use this election for an unexpected purpose: to give the two mainstream parties a good kicking.

Martin Vander Weyer is editor of Spectator Business.

What's News

■ **Belgian Premier Leterme** tendered his resignation, but was rebuffed by King Albert II, throwing the fractious nation into another round of political chaos and delaying a historic vote to ban the full-face veils worn by some conservative Muslim women. 7

■ **A British watchdog** alleged that Cathay Pacific and Virgin Atlantic colluded to set fares on flights between London and Hong Kong. 6

■ **BP was close** to announcing an oil discovery in the Gulf of Mexico where a drilling rig caught fire and sank. Rescuers continued to search for 11 people missing since the fire began Tuesday. 18

■ **US Airways said** it discontinued merger talks with United after "several months" of discussions. 20

■ **Credit Suisse said** first-quarter net profit rose 2.4%, but it failed to match recent healthy quarterly showings from U.S. rivals. 19

Inside

The busted homes behind that big mortgage bet. **14-15**

Struggling snooker wants to jazz up its image. **28**

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"When the passengers stopped crying, they got their groove back. They wanted retribution."

Quentin Fottrell on Ryanair's decision to compensate stranded passengers

Continuing coverage

Follow developments in the U.K. general election, including debate analysis, at **wsj.com/ukelection**

Question of the day

Vote and discuss: Who won the second debate among U.K. party leaders?

Vote online and discuss with other readers at **wsj.com/dailyquestion**

Previous results

Q: Should European governments suspend Goldman Sachs as a financial-policy adviser during the SEC probe?

Yes	54%
No	46%

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NEWS

Long-lost paintings to be auctioned

Sotheby's in June will sell works that disappeared during World War II by Cézanne, Picasso and other artists

By Dalya Alberge

Masterpieces by Cézanne, Picasso and other major artists of the 19th and 20th centuries are going on sale in June, after disappearing during World War II and later being discovered in a Société Générale vault. The collection, valued at about £17 million (about $26 million), is set be sold by Sotheby's at auctions in London and Paris.

According to Sotheby's, the collection had been hastily deposited at Société Générale in 1940 by Erich Slomovic, a Yugoslavian, before he fled Paris to escape the Nazis. Slomovic, who was Jewish, was killed by the Nazis in 1942, leaving the collection at the bank.

Sotheby's said the works were in Mr. Slomovic's hands on consignment from Ambroise Vollard, the prominent Parisian dealer who gave Picasso his first exhibition in 1901. Vollard, who helped shape Impressionist and modern art as we know it today, had taken Slomovic under his wing as his protégé. He was killed in a car crash in 1939.

The art works remained forgotten and untouched for 40 years until 1979 when Société Générale realized it was owed decades of unpaid storage fees.

Under French law, it was permitted to open the vault and sell any contents to recoup the debt. Inside, the bank found paintings, prints, books and drawings by some of art history's foremost artists.

Since the collection's discovery, it has remained hidden from public view because of legal challenges by the distant heirs of both Slomovic and Vollard. Following the resolution of the legal dispute in 2006, the proceeds of the sale will go to the heirs of Vollard.

Helena Newman, vice chairman of Impressionist & Modern Art Worldwide at Sotheby's, described it as an "extraordinary collection" giving a glimpse into the world of a legendary dealer.

She said: "This is like walking back into Vollard's Paris gallery."

The works includes more than 140 paintings, prints, books and drawings by key artists of the late 19th and early 20th centuries. The collection will be displayed at Sotheby's in London (June 16-22) and in Paris (June 24-29).

Sotheby's (2)

André Derain's 'Arbres à Collioure,' above, and Paul Cézanne's ''ortrait d'Émile Zola' are set to be sold by Sotheby's in June.

Among the jewels are André Derain's "Arbres à Collioure," which is estimated to break the artist's record and sell for £14 million. Painted in 1905, in the coastal town of Collioure in the South of France where Derain and Matisse spent the summer working together, it is the Fauve artist's most important work ever to come to auction and reflects the influence of the intensely bright Mediterranean light.

Ms. Newman said it marks the pinnacle of Derain's Fauve style and a milestone in the development of 20th-century art: "It's as fresh as the day it was painted."

Other important works include Paul Cézanne's "Portrait d'Émile Zola," an oil on canvas, estimated at £725,000.

It is one of three surviving portraits of Zola by Cézanne. Painted around 1862-64, it is the earliest of them. The friendship between the two dated from childhood.

"This painting is therefore a wonderful symbol of the two great minds and their friendship dating from the time before they both became famous," Ms. Newman said. She added that it is a particularly intimate portrait, focusing on Zola's face.

A range of prints by artists such as Cézanne, Degas, Gauguin, Renoir and Picasso—with whom Vollard worked—reflect his passionate interest in graphic arts and print publishing.

There is Picasso's 1904 etching, Le Repas Frugal, estimated at £360,000 and a striking monotype of a brothel scene by Degas, "La Fête de la Patronne," circa 1878-79, which has been estimated at £275,000.

Data show wider Greek gap

Continued from first page

Eurostat, in its semiannual report on EU debt and deficit released Thursday, said Greece's 2009 budget deficit was €32.3 billion, or 13.6% of its gross domestic product. Greece had estimated the deficit at 12.7%. But Eurostat, noting that it still didn't have confidence in the new figure, said it could actually be above 14%.

In thin trading Thursday, the yield on a Greek 10-year bond rose to 8.69%, on par with some emerging markets and 5.66 percentage points more than Germany pays.

That spread was a record since Greece joined the euro-zone, sharply higher than levels of even a month ago. The price for insuring Greek debt against default zoomed up as well. The euro slid below $1.33.

Meanwhile, in Greece, public-sector unions angry with the government's cost-cutting measures staged a 24-hour strike. They say the burden of adjustment is falling unfairly on them.

Two things are primarily rattling investors and driving up yields, says Mr. Wattret, the BNP Paribas economist. One is fear that a hesitant Germany—which is deeply reluctant to help Greece—may slow down aid. The other worry is that given the huge budget cuts Athens will need to effect to set Greece on course to pay down its debt pile, the country will not quickly grow out of its debt.

Usually in IMF-led programs, governments cut spending. But they are able to generate growth by devaluing their currencies. Greece, however, is locked into the euro, closing the currency depreciation route.

Moody's cut Greece's debt rating one notch, from A2 to A3, still investment grade, and said further downgrades are likely.

Europe upturn grows

Private-sector output hits 32-month high, heralding rise in GDP

By Nicholas Winning

LONDON—The euro zone's economic recovery gathered pace in April, with private-sector output surging to a 32-month high, a survey by financial-information firm Markit showed Thursday.

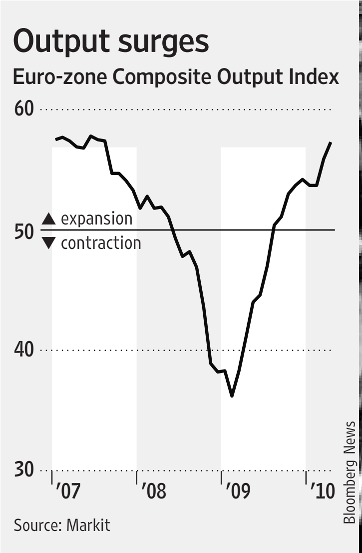
"Manufacturers are showing the best performance for 10 years, with the PMI [purchasing managers index] signaling near double-digit annual growth," said Chris Williamson, chief economist at Markit. "The recovery is also gaining momentum in services."

Markit's euro-zone preliminary composite output index—a measure of private-sector business activity based on about 85% of replies from a monthly survey of companies—rose to 57.3 in April from 55.9 in March. A reading above 50 indicates output is growing, while a reading below shows it is contracting.

Economists were expecting the composite reading to increase to 56.0, according to a survey of economists last week by Dow Jones Newswires.

"After what looks likely to be another depressingly weak quarter's growth in Q1, activity does now look set to bounce back strongly in Q2," said James Nixon, an economist at Société Générale. He added that second-quarter growth in gross domestic product could be as strong as 0.6%.

Euro-zone GDP growth stalled in the fourth quarter of 2009, fueling concerns that the recovery from recession was running out of steam. The first reading of first-quarter GDP is due May 12.



Renault factory in Valladolid, Spain

The breakdown of the Markit survey showed the services-activity index rose to a 30-month high of 55.5 in April from 54.1 the previous month. Expectations for the year ahead in the service sector also showed the strongest optimism since the start of 2006.

The purchasing managers' index for the manufacturing sector climbed to a 46-month high of 57.5 from 56.6 in March. Manufacturing also recorded the fastest growth of production since June 2000.

New orders grew at the fastest pace since August 2007, Markit said. Exports played a key role in boosting manufacturers' order books, rising at a rate that was similar to the 10-year peak seen in March, with support from the weaker euro. Measured against a basket of currencies from the euro zone's main trading partners, the euro has lost more than 6% of its value since early December.

In an another positive sign for the outlook for domestic demand, long the Achilles heel of euro-zone economy, other figures released Thursday showed euro-zone consumer confidence is growing.

The European Commission said its preliminary measure of consumer confidence in the euro zone rose to minus 15.2 in April from minus 17.3 in March. The measure for the European Union as a whole also rose to minus 12.5 from minus 13.9.

—Paul Hannon contributed to this article.

U.K. borrowing hits high

By Natasha Brereton and Ilona Billington

LONDON—British public-sector borrowing was larger than expected in March, taking the sum for the latest financial year to its highest level since records began 63 years ago.

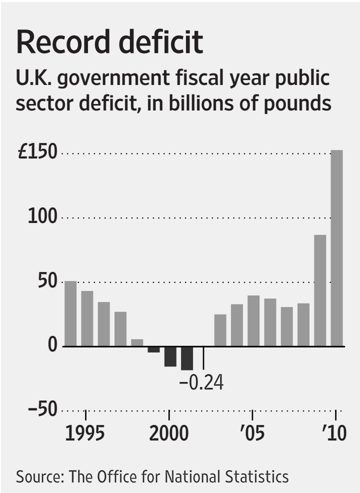
Also Thursday, the Office for National Statistics said retail sales rose in March, but by less than expected. Economists warned that high inflation and concerns over further jobs cuts could mute consumer spending in coming months.

Economic data could have a big influence on the outcome of the coming British election, which will take place May 6. Currently, British Prime Minister and Labour Party leader Gordon Brown trails Conservative Party chief David Cameron. Nick Clegg, head of the Liberal Democratic Party, is also in the race.

The deepest recession in more than 50 years has depressed U.K. government tax receipts and pushed public spending higher over the past 18 months. Ratings agencies have highlighted the public sector's large debts and have threatened to cut the U.K.'s triple-A credit rating if aggressive action isn't taken after the election to slash it.

The ONS said net public-sector borrowing was £23.5 billion ($36.2 billion) in March—the largest amount since the monthly series started in January 1993.

In the year that ended March 30, net borrowing by the public sector soared to £152.8 billion—the highest since records began in 1946-47 and up £65.9 billion from 2008-09, but slightly below a government forecast of £156 billion.



"This is still the biggest budget deficit since the Second World War and on a rough par with that of Greece," said Jonathan Loynes, U.K. economist at Capital Economics. "With all parties' fiscal plans based on extremely optimistic economic assumptions and unspecified spending cuts, a further sizable fiscal squeeze will still be needed after the election, whoever is in charge."

Figures from the European Commission Thursday showed the U.K. deficit stood at 12.3% in the latest fiscal year, up from 6.8% the year before.

Excluding the effect of actions to support the banking sector during the crisis, public-sector net borrowing for the fiscal year was £4 billion lower than forecast by Chancellor of the Exchequer Alistair Darling in the March budget, leaving it at £163 billion.

British retail sales, meanwhile, rose 0.4% from February and 2.2% from a year earlier in March.

"The figures suggest that consumer demand is recovering from January's snow and the 2.5% [value-added tax] increase at the start of the year," said Investec Securities economist Philip Shaw. "However we note that the level of sales has yet to recover fully from the weakness at the start of the year and volumes are now broadly down where they were last August," he said.

The smaller-than-expected increase in sales came despite the Easter holiday falling in March, and also suggests that consumers continue to exercise caution over their spending.

Economists also warn that still rising prices of goods as well as concerns over job cuts when the next government introduces reduced spending plans will likely weigh on spending in coming months.

"With the nasty combination of very weak wages growth and at least temporarily high inflation squeezing real income growth, and households still under pressure to repair their balance sheets, the outlook for consumer spending remains fragile," said Capital Economist economists.

Debt crises' new victims: rich developed economies

[Brussels Beat]

By Stephen Fidler

With financial markets hyperventilating about the prospect of a debt default by the Greek government, the International Monetary Fund fretted aloud this week about the prospects for a sovereign-debt crisis—centered on Europe.

Since Mexico announced it couldn't pay its bank debts in 1982, poor emerging economies have been the origin and main victims of most big financial crises. This time, it's the governments of developed economies and their bloated debt burdens that are the focus of concern.

Greek bond yields have now risen to levels that suggest investors believe even a joint IMF-euro-zone bailout won't be enough to avoid a debt restructuring for Greece. In a report this week, the IMF said Portugal, and to a lesser extent Spain and Italy, would be the most likely to suffer from contagion if Greece goes over the edge.

Surges of government debt follow financial crises—not because of the direct costs of bank bailouts but mainly because tax revenues fall and government spending rises in the resulting economic slowdown. Following an exhaustive historical study, economists Carmen Reinhart and Kenneth Rogoff have calculated that central-government debt increases in real terms by 86% on average during the three years following a crisis.

That increase is well under way in major economies, which is why sovereign-debt worries are growing. By 2014, according to a private forecast commissioned from Oxford Economics by the accountancy firm Ernst & Young and published last week, euro-zone governments' debt will exceed 88% of annual gross domestic product.

Under fairly benign economic assumptions, including no Greek default, the forecast sees Italy's debt-to-GDP ratio growing to 126% of GDP, the highest in the euro zone, followed by Greece, 116%, Belgium, 109%, Portugal 102%, France, 100%, Ireland, 89% and Spain, 81%.

Germany's would be 74% of GDP. Other projections suggest the debt of the UK. and the U.S. will touch 100%, though a quarter of the U.S. debt is held by other government bodies, such as the Social Security Trust Fund, not the public.

Yet debt restructuring is far from a foregone conclusion. For one thing, debt-to-GDP isn't the only relevant yardstick.

Claudio Loser, a former senior IMF official now with the InterAmerican Dialogue, a Washington-based think tank, says the IMF will pore over a raft of variables to analyze whether Greece will be able to sustain its debt burden. On Thursday, Dominique Strauss-Kahn, the IMF's managing director, said that a Greek debt restructuring isn't under consideration, suggesting that he either had the result of that analysis or decided to preempt it.

Mr. Loser said the IMF-World Bank model, used mainly for poorer countries, suggests a country with strong economic policies should be able to sustain a debt of half its GDP, twice its exports and three times government revenues.

Debt-servicing costs—interest payments plus debt maturities—should be no more than 25% to 35% of revenues.

By some measures, Greece's debt looks high, at 124% of GDP at the end of 2010. (For comparison, the U.K. had debt at the end of World War II of close to 240%, remained above 100% until 1961, and it didn't default.) But its debt-servicing bill is about 32% of government revenues, and its interest bill just 13%, half of that of Turkey.

Some other traditional measures of debt vulnerability may not be very relevant.

Greece is borrowing in its own currency, so it doesn't have to worry about currency risks unless it leaves the euro.

Since Mexico's default in 1982, poor emerging economies have been the origin and main victims of most big financial crises.

About 86% of Greek government debt is held by foreigners, according to the IMF, and much of that is owed to other members of the euro zone, primarily to banks and insurance companies. A default would therefore be a euro-zone family affair: one important reason why many people think Greece is likely to get a bailout, if it needs one, from other euro-zone governments this year, next year and the year after.

One interesting aspect of the IMF's contagion analysis is that Ireland, in the line of fire a year ago, would escape the worst of a Greek default, despite its big budget deficit. (Eurostat, the European Union statistical authority, said Thursday that because of a technical adjustment the Irish budget deficit was in fact 14.3% of GDP in 2009, rather than 11.7%.) That's because investors appear to believe that Ireland has acted pre-emptively and decisively to get the deficit under control.

To avoid Greece's plight, says Uri Dadush, a former World Bank official now at the Carnegie Endowment in Washington, that is exactly what Italy should do. It needs to move aggressively to cut its budget deficit by a further 4% of GDP over three years, and engineer a real devaluation through 6% in wage cuts and economic reforms. "I think the broad policy recommendations have general applicability in Spain too," he says.

EUROPE NEWS

Press Association

Liberal Democrat leader Nick Clegg, center, visited Bristol, England, as he hit back at allegations surrounding donations paid directly into his bank account.

Candidates face off in debate

As they vie for wavering voters, Brown and Cameron attack rising Liberal Democrat Clegg

By Joe Parkinson
And Paul Hannon

LONDON—The leaders of Britain's three main political parties faced off on foreign policy Thursday evening in the second of three televised election debates, as they sought to win over voters in the tightest race in almost 20 years.

Opinion polls point to no single party winning a majority of parliamentary seats on May 6.

Labour Prime Minister Gordon Brown was judged by voters to have fared worst in the first debate, but he stressed his foreign-policy experience.

"This may have the feel of a TV popularity contest but in truth this is an election about Britain's future," he said. "If it's all about style and public relations, count me out. If it's about judgment, if it's about delivering a better future for this country, I'm your man."

Conservative Party leader David Cameron, in his opening statement repeated his message of change.

"It's clear from last week's debate that the country wants change. ... If you vote Conservative you will get a new team running the country from May 7 and you won't be stuck with what you've got now," he said.

In front of an audience of around 150 people in Bristol, southwest England, Nick Clegg of the Liberal Democrats sought to portray himself as an alternative to the two parties that have traded power for most of the twentieth century.

"I'm proud of the values that made our country so great," Mr. Clegg said. "But the sad truth is that governments under the old parties have let those values down."

Mr. Clegg, who saw his party's poll rating surge after a strong performance in last week's debate, which was watched by 9.4 million viewers, faced fire from Messrs. Brown and Cameron, who began the campaign in a strong position to regain power for the Conservative party after 13 years in opposition.

Mr. Brown, fighting his first election as Labour leader following 10 years as Treasury chief, has appeared more sanguine over Mr. Clegg's gains, signaling that Labour is open to a coalition with the Liberal Democrats if the election results are inconclusive.

The debate's focus on foreign affairs was a departure for a campaign so far dominated by the economy and a parliamentary expenses scandal.

The parties clashed on European policy, with Mr. Cameron seeking to woo voters with pledges to restrict the influence of European Union legislation in the U.K., a pitch that is popular with an electorate that is skeptical of efforts to boost European integration.

Messrs. Brown and Clegg repeated accusations that a Conservative government would isolate Britain, citing Mr. Cameron's decision to pull out of the European Parliament's main center-right bloc—which includes the ruling parties of France, Germany and Italy—to set up an antifederalist grouping that includes far-right parties in central and eastern Europe.

"Let us never again be an empty chair in Europe—my fear is that David's policy would do that again," Mr. Brown said.

Front and center in the debate was the governing Labour Party's record on the increasingly unpopular war in Afghanistan, where 281 British soldiers have been killed since operations began in 2001.

The prime minister defended the U.K.'s role in the conflict, but Messrs. Clegg and Cameron questioned whether the British troops were adequately equipped.

"If we ever take that decision again let's make sure we've got the right equipment, the right strategy," Mr. Clegg said.

"I still worry we're not doing enough to get the political situation right in Afghanistan," Mr. Cameron said.

Mr. Brown twice accused Mr. Clegg of being anti-American.

The Liberal Democrat leader denied that he was anti-American, and said the relationship between the two countries was "very special." However, he said he had reservations about the way the relationship was managed by British governments. "It shouldn't be a one way street, we shouldn't always do what our American friends tell us to do," he said.

Pollsters have said allegations over the adequacy of military equipment would resonate with the public and further erode the prime minister's support.

In a YouGov poll released before the debate Thursday, the opposition U.K. Conservative party held a five point lead over the governing Labour party and the Liberal Democrats were back in third place.

That contrasted with polls late Tuesday showing continued strong support for the Liberal Democrats, with one survey putting them in the lead and another showing them running narrowly second to the Conservatives.

The debate took place as the Liberal Democrats hit back at allegations surrounding donations to party leader Mr. Clegg, labeling it a political smear and saying there was no evidence of wrong-doing.

The allegations against Mr. Clegg surfaced in a story in U.K. newspaper the Daily Telegraph, which said three businessmen paid money directly into Mr. Clegg's bank account that was used to pay for a member of his staff.

Mr. Clegg said any suggestions he had done anything wrong were "totally, totally out of order" and said he would publish figures to back up his claims.

"I received money from three friends which was properly given, properly received, properly declared and properly used to pay for the salary for a member of my staff. Any suggestion that I did something wrong is out of order and I'm going to publish the figures to prove it," Mr. Clegg told Sky News.

The Liberal Democrats said a raft of other stories in U.K. newspapers Thursday, which criticized Mr. Clegg's stance on immigration, Afghanistan and Europe, amounted to a political smear.

"I think I must be the first politician who has gone from being Churchill to being a Nazi in under a week," Mr. Clegg in reference to headlines last week saying his popularity was in par with the U.K.'s World War II Prime Minister Winston Churchill. "But I hope people won't be frightened in trusting their instincts, in doing something different this time."

—Ainsley Thomson contributed to this article.

Armenia scraps its border deal with Turkey

By Marc Champion

Armenia said on Thursday that it is abandoning a U.S.-backed agreement with Turkey to reopen the border between the two countries, until Ankara drops preconditions and ratifies the deal.

In a televised statement to the nation, Armenian President Serzh Sargsyan accused Ankara of stalling ratification of the agreement, which was signed in October. He said Turkey was treating the process as "an end in itself," whose main goal was to prevent the U.S. from acknowledging the 1915 massacre of Armenians by the Ottoman Empire as genocide.

The Armenian decision came just days before U.S. President Barack Obama is due to make the White House's annual statement on the April 24 anniversary of the massacres, in which up to 1.5 million people were killed. The U.S. administration has repeatedly argued against a genocide declaration, on grounds that it would torpedo efforts to secure the border deal between Turkey and Armenia.

"For a whole year, Turkey has done everything to protract time and fail the process," said Mr. Sargsyan. "Reasonable time frames have, in our opinion, elapsed. The Turkish practice of passing the 24th of April at any cost is simply unacceptable."

The agreement signed in October was designed to cut through the range of disputes between Turkey and Armenia. In the 1990s, relations suffered further, when Armenia fought a bloody war over the enclave of Nagorn Karabakh in Azerbaijan, a close Turkish ally, leaving Armenia in control of a swathe of Azeri territory. Turkey closed the border in protest, in 1993.

Armenia and Turkey began secret negotiations some two years ago to secure a deal that would reopen the border, establish diplomatic relations, and set up a joint commission to discuss problems of history, such as the 1915 killings.

A year ago Thursday, the two sides set out a road map for the deal, and in October, they signed it. Neither side, however, has ratified the agreement. Armenia has waited for Ankara to move first, while Ankara—under heavy pressure from Azerbaijan—insisted there should first be progress on resolving Nagorno Karabakh dispute, an issue not mentioned in the agreement.

Turkey strongly denies that genocide took place in 1915, describing the deaths as the tragic result of a civil war in which all sides suffered. Most historians say the Ottoman state was guilty of genocide.

Armenia's parliament this year passed legislation that would allow Mr. Sargsyan to withdraw his country's signature from treaties, but the president said Thursday he would leave October's agreement intact, out of respect for the U.S., Russia and France, which back the deal.

Thursday's decision left the door open to diplomacy, but some critics say the Mr. Sargsyan has been duped by Turkey into providing Mr. Obama with an excuse not to call the 1915 massacres genocide, as he pledged to do in his election campaign. Since a U.S. House Foreign Affairs Committee voted last month to recognize the genocide, the White House has lobbied against a full vote on the House floor, saying it would kill the border agreement.

Ryanair drops bills battle

Carrier to compensate passengers for costs of being stranded but vows to fight payout rules

By Steve McGrath
And Quentin Fottrell

Agence France-Presse/Getty Images

A man sits on his luggage beside a poster for Irish low-cost Ryanair in Stansted airport in Essex, England, on Thursday.

LONDON—**Ryanair Holdings** PLC on Thursday backed down and said it will compensate passengers for the costs of being stranded by the ash cloud that closed airspace over most of northern and central Europe for six days, but the battle over rules governing who will pay the costs of the current crisis is set to go on.

Ryanair had said Wednesday it would compensate its passengers only up to the cost of their air tickets, and was prepared to go to court to challenge current European Union rules. These rules state that airlines have a "duty of care" to passengers and must refund receipted expenses for costs incurred due to flight delays, if passengers choose to be re-routed rather than taking ticket refunds. Thursday, Europe's largest low-cost carrier said it will comply with the EU rules, although it will continue fighting to change them.

"[Ryanair Chief Executive] Michael O'Leary realizes that he got it wrong [Wednesday]," a Ryanair spokesman said.

The airline has said the crisis will hit its net profit by €42 million ($56 million) in fiscal 2011, provided it can resume a normal schedule by Friday. But this doesn't include likely receipts from stranded passengers for items such as hotel and food, which could total hundreds of euros per passenger.

Ryanair, which charges low prices for flights but makes money from items such as charging for baggage-handling and food, said it should be compared with train, coach and ferry operators, which don't fall under duty-of-care rules.

It is at odds with travel operators like **TUI Travel** PLC and **Thomas Cook Group** PLC, which Wednesday accused low-cost airlines of putting duty of care second to getting their flight operations back to normal. The low-cost airlines argue that they can't be compared with travel operators, which offer higher-price packages that include hotels and meals, and have a bigger duty of care.

"The events of the last seven days, under which Europe's airlines were prevented from flying by the closure of European airspace, highlight how absurd and discriminatory the regulations are towards Europe's airlines," Mr. O'Leary said.

Ryanair's U-turn comes after the European Commission, the EU's executive branch, said Wednesday that it will enforce its duty-of-care rule in the wake of the shutdown.

Airlines across Europe are urging national governments and the EU to help pay for the cost of the crisis and to consider changing the duty-of-care rules for events that are outside an airline's control. They say they are prepared to pay for stranded passengers if they are at fault, but couldn't do anything about the ash cloud because national authorities had made the decision to close airspace.

The regulation "was intended to apply when airlines had individual delays or cancelled flights. It was never intended to apply to wholesale shutdown of the airways system imposed by governmental rulings and without any limitation of time," the Board of Airline Representatives in the U.K., which represents over 90 airlines, has said.

Airlines around the world are estimated to have lost $1.7 billion in revenue due to the crisis, which resulted in more than 100,000 canceled flights and more than eight million passengers stranded. European airlines are estimated to have lost close to €1 billion in revenue.

"It is an extraordinary situation exaggerated with a poor decision-making process by national governments," Giovanni Bisignani, director general of the International Air Transport Association, said Wednesday. "The airlines could not do business normally. Governments should help carriers recover the cost of this disruption."

IATA represents some 230 airlines world-wide with 93% of scheduled international air traffic.

The EU and some national governments have indicated they will look at claims for compensation due to the ash crisis, but only once the situation has normalized and carriers have covered the initial costs.

It has said aid to airlines and passenger rights, however, are two separate issues.

"Ryanair has long campaigned for these reimbursements under passenger-rights legislation to be limited to the ticket price paid in the same way they are for train, coach and ferry operators," CEO O'Leary said. "We will continue to work through the European Low Fares Airlines Association and other industry bodies to persuade the European Commission and the European Parliament to alter this regulation to put this reasonable limit on these reimbursement claims."

On Thursday, airlines across Europe were still using extra aircraft to repatriate passengers stranded for the week. Most of Europe's airports were open and returning to normal, although some airports in Norway, Sweden and Scotland were closed in the morning.

U.S. Air Force warns that ash still poses risks

Associated Press

RAF LAKENHEATH, England—U.S. Air Force officials warned Thursday that their biggest fighter wing in Europe could suffer long-term damage if Iceland's volcano keeps belching ash into the skies.

The Air Force sent two F-15 fighters on test flights Wednesday and eight more on Thursday but said not enough data have been gathered to resume normal operations, despite the lifting of the civilian flight ban and the return to the skies of commercial airliners.

Col. John Quintas, an F-15 pilot who commands the 48th Operations Group, said the test flights all returned safely after about 75 minutes in the air. The fighters didn't encounter any major problems, though some pilots reported haze in areas that were deemed the highest risk.

"They certainly didn't come down clean, but they did come down safe for flight," he said.

Mechanics were analyzing the fighter engines to determine the extent of the ash's impact, he said, adding that determining safety would be a complex task because the risks might not be immediate.

"What we are concerned about is the long-term effects of low-level exposure," he said at RAF Lakenheath, an Air Force base about 100 kilometers northeast of London. Lakenheath's 82 F-15s make it the largest U.S. fighter base in Europe.

Normally, about 50 to 60 fighters take off on missions from the base each day. On Thursday, only the eight test flights were allowed.

"We are in uncharted territory," Col. Quintas said. "We could be in this situation for months."

The safety of the military fighters has been watched as an indicator of whether commercial airliners should be allowed to fly and the first forays weren't good—test flights by a Belgian F-16 and two Finnish F-18s over the weekend, before the civilian ban was lifted, resulted in minor engine damage.

But fighters are potentially more susceptible to the ash than commercial airliners.

Cathay, Virgin face U.K. probe over pricing

By Jonathan Buck

LONDON—The U.K.'s Office of Fair Trading issued a statement of objections alleging that **Cathay Pacific Airways** Ltd. and **Virgin Atlantic Airways** Ltd. colluded to set airfares on flights between London and Hong Kong in breach of competition law.

The office on Thursday said the airlines coordinated strategies on passenger fares through the exchange among employees of sensitive information about pricing and other commercial matters over several years.

The course between the U.K. and Hong Kong is one of the busiest long-distance routes in the world.

The office said the matter was brought to its attention by Cathay Pacific under the watchdog's leniency policy, in which a company that is the first to report its participation in cartel conduct can qualify for immunity from penalties. Provided it continues to cooperate, the Hong Kong carrier would be immune from any penalty imposed in this case, the office said.

"For a market economy to work effectively it is vital that competing companies determine their pricing strategies independently of each other and do not seek to avoid the rigors of competition through unlawful coordination," said Ali Nikpay, the Office of Fair Trading's senior director of cartels and criminal enforcement. "The parties will now have an opportunity to respond to our proposed findings before we decide whether competition law has in fact been infringed."

Agence France-Presse/Getty Images

Passengers checked in at Hong Kong's international airport in March.

"Virgin Atlantic intends to robustly defend itself against these allegations," which cover the years 2002 to 2006, the U.K. airline said. "The airline does not believe that it has acted in any way contrary to the interests of consumers."

The airline noted that no definitive findings have been made against Virgin Atlantic by the office. No decision on any potential infringement will be made by the office until Virgin Atlantic has an opportunity to formally respond, the airline said.

Cathay Pacific said it "has a policy of full compliance on competition-law issues and will fully cooperate with any authorities if required to."

Virgin Atlantic has been a whistleblower in alleged cartel activity in the past. In 2007, it escaped a fine from regulators after acknowledging that it colluded with competitors to fix prices on certain flights between the U.S. and the U.K. In that case, British Airways PLC was fined £269 million ($414 million).

U.S. NEWS

Reuters

Belgian Prime Minister Yves Leterme leaves the Royal Palace in Brussels after a meeting with King Albert II on Thursday.

New turmoil for Belgium

Premier tenders resignation, but king says no; burqa-ban vote on hold

By John W. Miller

BRUSSELS—Belgian Prime Minister Yves Leterme tendered his resignation Thursday but was rebuffed by King Albert II, throwing this fractious nation into another round of political chaos and delaying a historic vote to ban the full-face veils worn by some conservative Muslim women.

Belgium was set to become the first European country to forbid the practice of wearing the burqa in public. The proposed law, which has already been approved in committee, has broad support in Parliament and is expected to pass when the dust settles from the current crisis.

Mr. Leterme's hand was forced Thursday morning when the Dutch-language Conservatives withdrew from his five-party coalition, leaving it without a workable majority. "We've lost confidence in the government," said Alexander De Croo, president of the Conservatives.

The crisis comes at a poor time for Belgium, just 10 weeks before the country is scheduled to take over the European Union's rotating presidency. The presidency is a chance to showcase Herman Van Rompuy, a former Belgian prime minister and now the EU's first-ever president. Mr. Leterme, 49 years old, had been busy organizing a promotional tennis match between national stars Justine Henin and Kim Clijsters.

Belgium is also grappling with managing its economic recovery, cutting its budget deficit and dealing with the flight ban following the volcanic eruption in Iceland.

Mr. De Croo and other members of Belgium's Dutch-speaking majority charge that Mr. Leterme has offered too many concessions to Belgium's French-language minority in a technical dispute over administration of the suburbs of Brussels.

The crisis left the prime minister no choice but to submit his resignation to King Albert II. But after an afternoon meeting, the king refused. "A political crisis would be inopportune and would do serious damage to the economic and social well-being of the citizenry and to Belgium's role at the European level," Mr. Leterme and the 75-year-old monarch said in a joint statement.

The parties will hold meetings on Monday to try to find a way out of the impasse. Possibilities include Mr. Leterme finding a compromise to rebuild his coalition, the emergence of a new prime minister, or national elections. Parliament will also reconvene on Monday, but a vote on the burqa ban isn't likely until the political dust has settled.

At the heart of the dispute that forced Mr. Leterme to offer his resignation is a fight over the suburbs surrounding Brussels. A gaggle of small towns and villages numbering several hundred thousand people, these multilingual neighborhoods are in Flanders but are still tied to francophone-controlled Brussels via a common court and electoral system, thanks to a 1960s-era treaty.

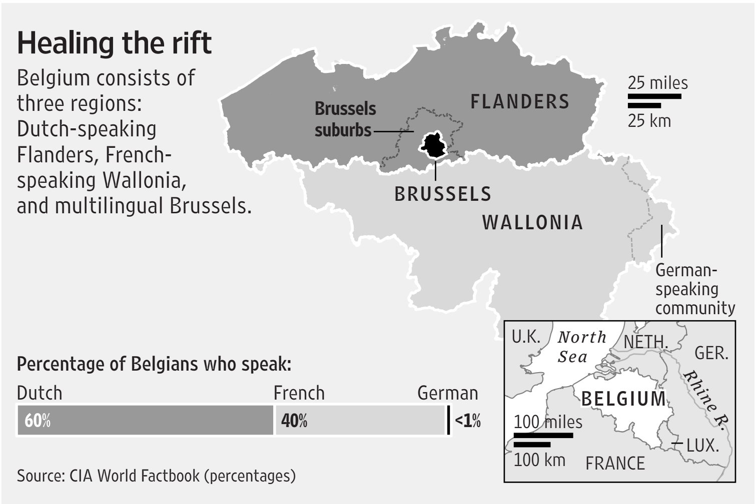
Belgium's Dutch-language majority is seeking to split this area from the core of Brussels. In practice, that would force the residents of those suburbs to use Dutch-language courts, and they could vote only for politicians running for office in Flanders. Most importantly, it would be a major symbolic victory for Flemish politicians who advocate ever more autonomy for Flanders. The two language groups also fight regularly over everything from taxes and school districts to football and what to write in history books.

It is an issue that has haunted Mr. Leterme ever since his party won power in elections in 2007. It took nine months for him to forge a coalition. He has now offered his resignation five times, although he has exited power only once, over his role in a state bailout of Fortis Bank.

Mr. De Croo had been threatening for weeks to quit the government unless French-language parties gave up the Brussels suburbs. "The Flemish parties are playing Russian roulette," said Olivier Maingain, a member of the Francophone Democratic Front.

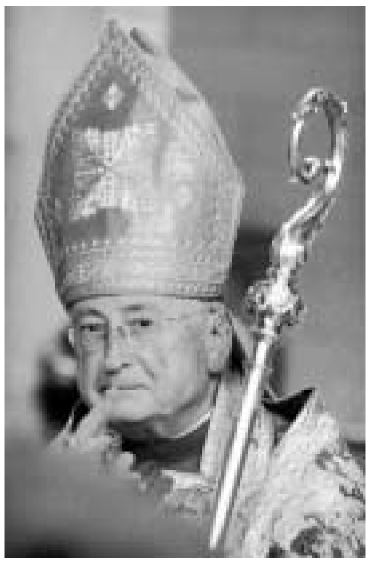
Despite the divisions, no major Belgian political party is advocating a breakup. The French-language group can't afford to lose the financial support of Flanders, one of the wealthiest regions in the world. Flemish politicians oppose a divorce because they would lose political control of Brussels, because it would cost them geopolitical capital and because it would simply be too expensive. Belgium's 97% ratio of debt to gross domestic product is the third-highest in the euro zone, behind Italy and Greece.

"Belgium is not dead, but there are increasing problems of understanding between the two sides," said Pascal Delwit, a political scientist at the Free University of Brussels.



German bishop says he will step down

By Vanessa Fuhrmans



Reuters

Bishop Walter Mixa earlier this month

One of Germany's most prominent conservative bishops tendered his resignation amid allegations that he routinely flogged children decades ago as a priest, becoming the most senior Catholic official to offer up his post in the country's widening clerical abuse scandal.

Walter Mixa, who was appointed in 2005 by Pope Benedict XVI to head the German diocese of Augsburg, submitted a letter to the pontiff late Wednesday, offering to resign and pledging to cooperate fully in clearing up the allegations of physical abuse against him, diocese officials said Thursday. Bishop Mixa requested to step down both as bishop of Augsburg and from his post as Germany's highest-ranking Catholic military chaplain.

Vatican spokesman Rev. Federico Lombardi said the Vatican would review Bishop Mixa's offer to resign. A spokeswoman for the Augsburg diocese said the Vatican hadn't asked for Bishop Mixa's resignation. Father Lombardi declined to comment.

Bishop Mixa offered an apology on Thursday, though he didn't specifically address or admit to the allegations of physical abuse. "I am and always have been aware of my weaknesses," the bishop said in a statement. "I ask today again for forgiveness from all those to whom I may have been unjust and from all those I have caused sorrow."

The offer of resignation marks the first from a German bishop since hundreds of people have come forward since January with stories of being physically or sexually abused as children by clergy in Germany.

Bishop Mixa, the highest-level German church official directly implicated in physical abuse claims, has come under pressure to resign amid a string of public accusations in recent weeks from at least half a dozen former residents of a Catholic children's home in the Bavarian town of Schrobenhausen.

Bishop Mixa's accusers have submitted sworn statements to German newspaper Süddeutsche Zeitung that while he was a parish priest in the 1970s and 1980s, he often punished them and others with slaps in the face, punches to the arms and beatings with a cane or carpet beater. They haven't accused him of sexual abuse. The bishop is also facing a church-initiated investigation into whether some of the orphanage's funds were misused, such as for a tanning bed, while the bishop was in charge.

Bishop Mixa has rejected the claims of being violent with children as untrue, though he acknowledged in a German newspaper interview last week that he had occasionally disciplined students with a slap, which he called a "completely normal" practice in schools and other Catholic institutions then. The bishop has found himself increasingly isolated in recent days, in particular by other German church leaders.

On Wednesday, Freiburg Archbishop Robert Zollitsch, head of the German Bishops' Conference that oversees Germany's Catholic Church, took the unusual step of publicly suggesting that Bishop Mixa take an extended leave of absence. He told reporters that he had discussed with Bishop Mixa whether "a period of spiritual retreat and distance" wouldn't be best while the allegations are investigated.

Bishop Mixa, 68 years old, is among the most conservative and outspoken of Germany's 27 bishops, and has sparked controversy before with some of his views. He drew fire in February after saying the "so-called sexual revolution" was partly to blame for the unfolding clerical sexual abuse scandal. He was criticized last year after attacking a German government move to provide more preschool care to enable mothers to return to work as an effort to turn women into "birth machines."

A bishop can't step down until the pope accepts his resignation. It could be weeks, or even months, before the pope formally accepts Bishop Mixa's.

Under Roman Catholic canon law, a bishop can't step down until the pope accepts his resignation. It could be weeks, if not months, before Pope Benedict formally accepts Bishop Mixa's.

The pope, under criticism that the Vatican hasn't done enough to crack down on sexual abuse within the church, reaffirmed on Wednesday before pilgrims massed in St. Peter's Square that he would take action.

On Thursday, Pope Benedict accepted the resignation of Bishop James Moriarty of the diocese of Kildare in Ireland. He is the third Irish bishop to relinquish his post since two Irish government reports last year revealed decades of sexual abuse of thousands of children by Catholic clergy and a cover-up attempt among church officials. Bishop Moriarty, 73, who offered to step down in December, said Thursday that he was resigning because "renewal must begin with accepting responsibility for the past."

Two other Irish bishops, John Magee of the Cloyne diocese and Donal Murray of Limerick have also resigned in recent months. Two auxiliary Dublin bishops, Eamonn Walsh and Ray Field, are waiting for Benedict to formally accept their resignations.

—Stacy Meichtry contributed to this article.

U.S. tries to buy time for its Iran strategy

[Capital Journal]

By Gerald F. Seib

Iranian forces launched a big military exercise in the Persian Gulf Thursday, thereby underscoring a grim reality: The strategy for stopping Iran's nuclear program is turning into a race against time before options turn from mediocre to bad to worse.

The goal of American policy right now is to slow down the clock—that is, to stretch out the time Iran needs to become nuclear-arms capable. The hope is to buy time to give other kinds of pressure a better chance to work before military options move to the fore.

That's why the current foot-dragging in adopting new economic sanctions at the United Nations Security Council is so troublesome. In an ideal world, and in the Obama administration's original vision, a U.N. resolution imposing new economic penalties would have been passed two months ago.

So now, here's where things are headed: American officials say they hope a U.N. resolution will pass in the next few weeks. That would clear the way for step two, in which the U.S. and its European allies, with some help from Japan, would layer on additional sanctions of their own with more bite, clamping down on Iran's access to the international financial system and squeezing its Revolutionary Guards, the real power behind Iran's nuclear program.

Getting this economic squeeze in place is crucial. The hope is that when Iran's leaders see that economic pressure has moved from possibility to reality, they will return to negotiations over their nuclear program, which they contend is for producing energy, not weapons.

It's worth pausing here to note that having a credible military threat on the table is useful for both prongs of this strategy—getting biting sanctions, as well as getting Iran to take its predicament seriously. Israeli Prime Minister Benjamin Netanyahu, while feuding with the Obama administration on the Israeli-Palestinian peace process, is extremely useful on this front.

Already, informed sources say, the U.S. has essentially said to the recalcitrant Chinese: "Look, you'd better cooperate on sanctions, because if we don't do something, Netanyahu is just crazy enough to attack Iran." And if there's a silver lining to the military exercises Iran just launched, it's that they suggest Tehran is taking the military threat seriously.

If these combined pressures compel Iran's leaders back into negotiations, the goal would be to revive the kind of nuclear-swap deal Iran agreed to, then backed away from, last fall. Under that agreement, Iran was to ship about half of the low-enriched uranium it has accumulated to Russia and France for reprocessing into fuel for a nuclear reactor in Tehran.

The beauty of that deal was that, by taking potential nuclear-weapons material out of Iran's hands and turning it into something else, the world would know with confidence that it had slowed down Iran's march toward nuclear-weapons capability by a year or so. That would, in the words of one senior Obama administration official, "shift the timetable to the right," extending the time available to find a longer-term solution.

That breather would be crucial on several fronts. First, the U.S. would buy more time to build a real regional security arrangement under which it would help strengthen the defenses of friendly Persian Gulf states and work out a plan for a joint response to Iranian provocations. More time also would allow the U.S. to move ahead in building a defense system to knock out Iranian missiles that could carry nuclear warheads.

It's possible that the combination of a regional defense plan and a real American missile-defense shield would signal to Iran that acquiring nuclear arms wouldn't give it the power to intimidate its neighbors that it might envision, and help convince Tehran that developing nuclear weapons isn't worth the economic pain the world can inflict.

And if that doesn't work, slowing down the nuclear program would at least create more time to determine whether opposition forces within Iran have any hope of threatening the regime.

There's at least some reason to hope new pressure might pull Iran back into negotiations. U.S. officials suspect that President Mahmoud Ahmadinejad, for all his bluster, actually wanted to do the nuclear-swap deal last fall, but was stopped by supreme leader Ayatollah Ali Khamenei.

And in recent days, Iranian officials have been floating an alternative to last fall's deal, indicating they want to talk to other nations about it, perhaps at a meeting on nonproliferation in New York next month.

Meanwhile, though, nuclear centrifuges in Iran continue to spin out enriched uranium. Iran's ultimate goal may well be to leave the outside world paralyzed in a state of suspended animation by demonstrating it has developed the ability and material to make nuclear arms, while stopping just short of making the weapons themselves.

Even that nebulous outcome would compel the world to ponder two far less appealing options. One would be that military strike.

The second would be to accept that Iran has become a nuclear-capable state, and adopt a strategy of containing it while using economic pressure—perhaps even an economic blockade—to force a reversal or to bring down the regime. That's essentially what the West did to the Soviet Union during the Cold War. It did, however, take 50 years.

Write to Gerald F. Seib at jerry.seib@wsj.com.

Associated Press

An abandoned warship is used as a target by Iran's military during exercises in the Persian Gulf on Thursday.

First-time buyers fuel gains in home sales

By Meena Thiruvengadam And Luca Di Leo

U.S. home sales climbed in March as first-time home buyers rushed to take advantage of a government tax credit ahead of the program's expiration.

Separately, the number of U.S. workers filing new claims for jobless benefits decreased last week, but the levels still aren't low enough to be consistent with an improving job market.

Meanwhile, U.S. wholesale inflation rose by more than expected last month as food prices moved sharply higher, but the core measure that strips out volatile food and energy items barely increased.

Sales of existing homes were up slightly more than expected, climbing 6.8%, to a 5.35 million annual rate from a downwardly revised 5.01 million annual rate in February, the National Association of Realtors said Thursday. Analysts surveyed by Dow Jones Newswires had expected sales to rise to an annual rate of 5.25 million. Sales were up 16% from March 2009.

Sales of distressed properties, such as foreclosures, accounted for 35% of March sales, the Realtors said.

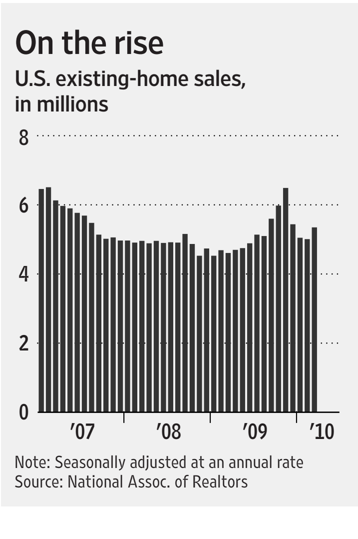
Lawrence Yun, chief economist for the Realtors' group, credited the government's tax-credit program with driving sales higher, but he said it would take months for the full effects of the program to be reflected in the data.

He said the Realtors' group didn't plan to push for another extension of the program, saying the housing-market recovery had reached a point where that wouldn't be necessary. The tax credits were originally set to expire in November but were expanded and extended to apply to contracts signed through the end of April.

First-time home buyers purchased 44% of all homes in March, up from 42% in February, the Realtors said.

Housing inventory in March rose 1.5% to 3.58 million, representing an eight-month supply. That's down from an 8.5 month supply in February, the Realtors' group said.

The group said the median price for existing homes rose 0.4% to $170,700. Prices were up across most of the U.S., except in the West, where median prices slipped 7.9% to $209,400.



Meanwhile, the Labor Department said in its weekly report Thursday that initial claims for jobless benefits fell by 24,000 to 456,000 in the week ended April 17. The drop was right in line with the expectations of economists surveyed by Dow Jones Newswires.

The previous week's level was revised downward to 480,000 from 484,000.

The decline in jobless claims comes after two weeks of unexpected surges in the figures, which the U.S. Labor Department blamed on the Easter holiday and other seasonal factors. The department had said rising layoffs weren't likely to blame for the increases, but nevertheless the elevated numbers raised concern among outside experts.

The four-week moving average, which aims to smooth volatility in the data to help paint a better picture of the underlying trend, rose for the week ended April 17. The Labor Department said the four-week moving average went up by 2,750 to 460,250 from the previous week's revised average of 457,500.

Total claims lasting more than one week, meanwhile, fell.

Jobless claims continue to remain stubbornly high even though the U.S. economy is growing and the Labor Department's March report showed jobs were being created.

That report found nonfarm payrolls rose by 162,000, although some of the gains came from temporary hiring for the 2010 Census. Overall, unemployment still remains at 9.7%.

Economists have generally agreed that it will still take time to see an improved labor market.

In other news Thursday, the producer price index for finished goods rose by a seasonally adjusted 0.7% on the month in March, the Labor Department said, after falling by 0.6% in February.

Core wholesale prices, however, barely moved. Excluding volatile energy and food prices, producer prices rose by just 0.1% last month, the same increase seen in February.

Economists polled by Dow Jones Newswires had expected wholesale prices to rise 0.4% in March. Core producer prices were seen up 0.1%.

To aid an economy that is still recovering from a severe recession, the Federal Reserve has kept short-term interest rates near zero for more than a year, pointing to low inflation and high unemployment as the main factors behind its strategy.

Inflation has been slowing recently, particularly the price readings that strip out volatile food and energy items that are closely watched by the Fed. In March, core consumer prices moderated to an annual 1.1%, the lowest level since 1966.

—Sarah N. Lynch and Darrell Hughes contributed to this article.

SEC V. GOLDMAN SACHS

In Germany, a backlash

Officials, companies speak out against Goldman Sachs's approach

By Marcus Walker

BERLIN—**Goldman Sachs Group** Inc. brought investment banking to Germany 20 years ago. Now, many here say it is giving the business a bad name.

Goldman's approach to winning business is coming under fire from German officials, companies and banks. The firm's latest headache: A dispute with the city of Berlin, which has accused Goldman of trying to intimidate it with legal threats in order to make more profit from a housing sale. Goldman denies the accusation.

The Wall Street bank has built up a powerful franchise in Germany since it opened its Frankfurt office in 1990, cultivating contacts in Germany's boardrooms and ministries that are the envy of its rivals. In 2009, Goldman was the top foreign investment bank in Germany by revenue and finished second overall behind **Deutsche Bank** AG, the country's largest bank, according to data provider Dealogic.

Germany is the world's fourth-biggest economy and home to many of Europe's largest companies, making it a crucial battleground for Goldman's global ambitions. But Goldman's tactics in pursuit of gain have been a source of friction in a country that values consensus and compromise over confrontation.

Now, in the wake of the U.S. Securities and Exchange Commission's civil-fraud charges against Goldman, quiet grumbling is turning into a vocal battering. The SEC has charged that Goldman withheld important information from investors on a derivatives deal whose victims included German bank **IKB Deutsche Industriebank** AG, which needed a state-backed bailout totaling about €10 billion ($13.4 billion) in 2007. Goldman has denied wrongdoing and is fighting the suit.

"I would not deal with this bank again unless I couldn't avoid it," said Ulrich Nussbaum, the city of Berlin's finance chief, after months of negotiations over Goldman's wish to take public a company that owns municipal housing in Berlin.

This week, lawmakers in Chancellor Angela Merkel's governing coalition called on the federal government to put all dealings with Goldman on ice. The bank also lost an advisory mandate with German public-sector lender **BayernLB**, which cited the SEC's civil suit. And the head of **Robert Bosch** GmbH, the world's largest auto-parts supplier by sales, said it should face criminal prosecution if the SEC allegations are true. Bosch wouldn't say whether it had any dealings with Goldman.

A Goldman spokeswoman declined to comment on the criticism. Goldman bankers in Germany said the wave of criticism is unfair.

During Goldman's early years in Germany, the firm succeeded by offering companies U.S.-style investment-banking services that they couldn't get elsewhere. Corporate finance in Germany had been dominated by old-fashioned commercial banks making loans to long-term business clients. In the 1990s, Goldman introduced many companies to bond and stock markets, and pioneered mergers and acquisitions advisory in Germany.

Since then, Goldman has been involved in almost every major corporate deal in Germany.

Under its current head, Alexander Dibelius, Goldman's German unit has diversified its business, becoming a major investor in German businesses as well as a financial adviser.

That has led to accusations of a conflict of interest from German companies, which have complained privately that Goldman is both their adviser and competitor in bidding for assets. "Only those who don't win any business have no potential conflicts," has long been Mr. Dibelius's reply in interviews. The issue is how banks manage such conflicts, he has said.

Mr. Dibelius declined to comment through a spokeswoman.

Mr. Dibelius's pursuit of deals has made him a target for the German media, with one newspaper calling him "Goldfinger" after the James Bond villain. Investment banking is the third career at which the 50-year-old has proved to be a highflier. He became a heart surgeon at the age of 24. Within a decade he had become a partner at consultancy McKinsey & Co., before jumping to Goldman in 1993.

Mr. Dibelius's dealings have sparked controversy. In 2009, retail and travel group **Arcandor** AG went bust in Germany's biggest-ever corporate failure, jeopardizing 70,000 jobs. Goldman, a longtime adviser to Arcandor, had earlier bought the group's department stores, which it then leased back to the company. Analysts have blamed Arcandor's failure partly on the high rents it had to pay Goldman Sachs and allied investors. Goldman declined to comment about Arcandor.

Critics complained Goldman was playing the roles of adviser, investor and landlord. Goldman officials said they had no formal mandate to advise Arcandor at the time the firm bought the stores. In January, Mr. Dibelius drew more fire after he told a group of students that banks "do not have an obligation to promote the public good."

Goldman's dealings with Germany's capital city, Berlin, are proving controversial, too. In 2004, Goldman and private-equity firm **Cerberus Capital Management** LP bought municipal-housing company **GSW**, owner of 66,000 apartments, for €2.1 billion. The contract stipulated that the buyers wouldn't sell a majority stake in GSW through an initial public offering until 2014, unless the city of Berlin consented.

Last year, however, Mr. Dibelius pressed Berlin officials to agree to let Goldman take the housing company public. The city of Berlin, struggling with high debts, said it wanted €30 million in return for the earlier-than-planned IPO.

Imago Stock/Zuma Press

Goldman Sachs is coming under fire in Germany for what critics say is its aggressive tactics. Here, the bank's German headquarters in Frankfurt.

This January, Goldman sent city finance chief Mr. Nussbaum a legal opinion, from a Stuttgart law firm, which argued that such a payment could be prosecuted as criminal bribery.

"It was a transparent attempt to intimidate us," said Mr. Nussbaum, a wealthy former entrepreneur. "I accept that business people negotiate hard, but it's a question of style. It's difficult to deal with someone if they start negotiations by saying your demands would break criminal law," he said.

Mr. Dibelius told Berlin officials that he wasn't trying to pressure them, and only wanted to be sure any deal was legally sound, according to people involved in the deal. Mr. Nussbaum said he didn't believe Mr. Dibelius.

A Goldman Sachs spokeswoman said: "Our approach, from the beginning, has been to ensure that all aspects of the process for the IPO of GSW were both appropriate and acceptable to Berlin."

In February, when Berlin didn't back down, Goldman commissioned a second legal opinion from a university law professor, which said a payment to Berlin's coffers, if done transparently, would be fine. Berlin's chief anticorruption prosecutor concurred. Mr. Dibelius then tried to negotiate a lower price, but eventually agreed to pay the €30 million. Berlin's legislature approved the IPO this week.

Obama scolds Wall Street, asks for cooperation

Continued from first page

Although differences remain about how to regulate Wall Street, the populist rhetoric that infected the debate has cooled. Senate Banking Committee Chairman Christopher Dodd (D., Conn.) has been locked in negotiations with Sen. Richard Shelby (R., Ala.) over a potential compromise, which some believe could come within days.

In his speech, Mr. Obama dodged discussing elements of the bill that may change, including the power of state regulators over national banks and certain provisions designed to beef up the powers of company shareholders that Republicans strongly oppose.

He also acknowledged certain companies could be exempt from legislation that would redraw the market for derivatives. Some firms, such as agricultural concerns and airlines, use derivatives to hedge their exposure to constantly changing prices of commodities like oil.

Investors, however, trade them as pure speculative bets, something the administration wants to restrict. By making that distinction clear, the president could win over support from senators worried about the breadth of the planned restrictions.

"The only people who ought to fear the kind of oversight and transparency that we're proposing are those whose conduct will fail this scrutiny," Mr. Obama said.

The crowd at the Great Hall of Cooper Union, filled with students and supporters, was receptive. Much of the front three rows were reserved for Wall Street executives whose responses were considerably more subdued. Their hands remained in their laps when the president spoke of his bank fee to recover the remaining bailout funds and his plea to call off the industry lobbyists seeking to shape the bills.

J.P. Morgan Chase & Co. CEO Jamie Dimon, a longtime Democratic supporter who has grown frustrated with Washington, wasn't in attendance. The bank's chief risk officer Barry Zubrow was there instead. Goldman Sachs Group Inc.'s two top executives, Lloyd Blankfein and Gary Cohn were present. The firm was charged last week with fraud by the Securities and Exchange Commission for its role in selling mortgage-related investments. Other big financial firms represented included Barclays, Morgan Stanley and Credit Suisse.

The legislation would grant the federal government the power to seize teetering financial giants and dismantle them the same way the Federal Deposit Insurance Corporation now can seize failing banks. It would create a new financial consumer regulator, would boost the strength and budget of the Securities and Exchange Commission and would impose new transparency rules on the trading of derivatives, the complex financial instruments that helped bankrupt Lehman Brothers and nearly wipe out American International Group and Merrill Lynch.

Mr. Obama is treating his return to Cooper Union as something of a triumphal homecoming, with a touch of "I told you so" in the speech. Two years ago, he called on Congress to give the Federal Reserve more supervisory power over the biggest financial institutions and to demand tougher new capital and liquidity requirements.

Pending legislation largely follows that demand. Congress appears ready to meet his request, now two years old, for a new financial consumer regulator. His calls for stronger, international accounting standards and financial stability requirements have been taken up by the Group of 20 nations, although talks are proceeding haltingly.

His 2008 suggestion of streamlining the hodgepodge of "overlapping and competing regulatory agencies" has been abandoned. But he is dwelling more on the warnings he issued in that first Cooper Union address.

"I take no satisfaction in noting that my comments have largely been borne out by the events that followed," he said. "But I repeat what I said then because it is essential that we learn the lessons from this crisis, so we don't doom ourselves to repeat it. And make no mistake: That is exactly what will happen if we allow this moment to pass—and that's an outcome that is unacceptable to me and it's unacceptable to you, the American people."

"One of the most significant contributors to this recession was a financial crisis as dire as any we've known in generations," Mr. Obama said in the highly anticipated speech at Cooper.

He told the crowd that America must learn from the mistakes of the economic crises and enact legislation to help prevent it from happening again.

Mr. Obama's push for financial reform has intensified in recent weeks and he has lashed out at Republicans for meeting with Wall Street lobbyists. In his speech, he said legislative proposals in Congress would help restructure the rules that allowed Wall Street to take risky bets that Americans ended up paying for.

He said he wouldn't accept compromises that would weaken the bill, particularly in the area of derivatives, complex financial instruments that played a role in the economic crisis. He also said that financial reforms must set limits on the size of risks that banks can take, and include provisions that would make it easier for a failing institution to unwind before taxpayers would be affected.

Agence France-Presse/Getty Images

Mohamed ElBaradei leaves the Al-Hussein mosque in Cairo on March 26 after performing Friday noon prayers.

ElBaradei widens effort

Former nuclear watchdog tests possible challenge to lead Egypt

By Ashraf Khalil

CAIRO—Activist Mohamed ElBaradei has moved his campaign for Egyptian political reform to the streets, testing how tolerant President Hosni Mubarak would be of a possible challenge by the former top United Nations nuclear watchdog in next year's presidential polls.

Mr. Mubarak, who has ruled the Arab world's most populous country under de facto martial law for 29 years, hasn't yet said whether he will run for a sixth five-year term. The president, 81 years old, returned to full duty last week after a gall-bladder operation in Germany.

Many analysts had figured 2011 would be the year Mr. Mubarak would step aside for a hand-picked successor. His younger son, Gamal, tops the list of possible heirs.

But Mr. ElBaradei's high-profile entry into Egyptian politics has clouded the calculus. After returning to a hero's welcome in Egypt after 20 years away—much of that as head of the U.N.'s International Atomic Energy Agency—Mr. ElBaradei says he is considering running for president. But he says he would run only if significant reforms were enacted to make the November 2011 contest a fair race.

Mr. Mubarak's government has been rounding up political opponents for years. In recent months, officials have tightened the dragnet—particularly against the banned but powerful Muslim Brotherhood. This month, police also squashed two protests in downtown Cairo, jailing dozens for demanding political reform.

Despite the crackdown, Mr. ElBaradei this month has made public appearances at Friday prayers at Cairo's venerable Al-Azhar mosque and at a rally in the Nile Delta city of Mansoura. His political organization, the National Association for Change, is out collecting signatures in support of a seven-point political reform plan, an effort organizers hope will demonstrate broad appeal for change.

Egyptian authorities so far haven't directly attacked Mr. ElBaradei or key leaders of his movement. But two young activists were arrested in February for spray-painting pro-ElBaradei slogans on public buildings. Earlier this month, a publisher who put out a pro-ElBaradei book had his office raided and his computers confiscated, and spent a night in jail. All three have since been released.

Mr. Mubarak, in a news conference before his surgery last month, said Mr. ElBaradei, or any Egyptian citizen, was free to run for president, as long as they abide by existing rules.

Mr. ElBaradei and his supporters have rejected suggestions that he join an opposition party sanctioned by the government to run a candidate in the vote.

Mr. ElBaradei's public appearances have made headlines, and supporters see his signature drive for reform as key to any real political challenge to Mr. Mubarak.

Sitting behind a desk in his modest downtown office, Abdel Rahman Yusuf waves the latest draft of an instruction manual organizers plan to distribute to several thousand volunteers recruited to spearhead the drive. "This is our No. 1 priority right now," says Mr. Yusuf, a prominent poet and television personality, who is coordinating the petition drive. "How we do on that will, to a large extent, determine what comes next."

Organizers plan to kick off the campaign in earnest at the end of the month. Mr. Yusuf doesn't cite any target for the number of signatures the group hopes to collect. He acknowledges the challenges of mounting a Western-style, grassroots political-action drive under restraints that make open political opposition a risky prospect.

Mr. Yusuf's draft manual emphasizes ways for his volunteers to gather signatures while staying off the government's radar. He recommends volunteers move within trusted circles. "Don't go to the street, go to your community—your friends, family and co-workers," he says he advises workers.

The petition focuses on the National Association for Change's seven-point list of reform demands. Those are ending Egypt's longstanding state of emergency, letting judges supervise polling places, allowing election monitoring by local and international nongovernmental organizations, equal media access and time for candidates, allowing Egyptian expatriates abroad to vote, simplifying voter requirements, and eliminating official obstacles to the sort of independent presidential candidacy that Mr. ElBaradei appears inclined to pursue. Mr. ElBaradei also advocates presidential term limits.

The signature drive—no matter how popular—carries no legal weight. The changes it calls for would require rewriting three articles of the constitution, a measure that could be undertaken only via national referendum.

Mostafa Elwi Saif, chairman of Cairo University's political-science department and a member of Mr. Mubarak's ruling National Democratic Party, dismisses any chance of Mr. ElBaradei rallying enough of a public groundswell before the polls.

"The constitution is not the Quran. It's not a sacred text. But 18 months is not enough time to realistically gather that kind of support," he said.

If Mr. ElBaradei is serious about pursuing the presidency, he should join an opposition party sanctioned to run a candidate in the vote, Mr. Saif added. This is a prospect Mr. ElBaradei and his supporters have rejected. Joining a licensed party "would be the biggest favor [Mr. ElBaradei] could do for the regime," says Mr. Yusuf, the ElBaradei campaigner. "Once you join a party, you're on the stage. Well, who built the stage? Who wrote the script?"

Financial revamp at risk, IMF says

By Bob Davis

WASHINGTON—The International Monetary Fund's managing director said he worried that national rivalries were making it difficult to reach a deal on global financial regulation, as fund members split on whether to adopt an IMF-proposed bank tax.

"The risk—which is not only a risk but already materialized somewhat—is that different parts of the world will have their proposals which all make sense when you are looking at the interests and problems of the countries preparing these reforms but which may be somewhat inconsistent," said Dominique Strauss-Kahn, the managing director, at a press briefing before the IMF's spring meeting this weekend.

"Our main concern is to have everybody trying to work together and to maintain the cooperation and momentum" that countries had last year when the IMF urged nations to increase stimulus spending.

The spring meeting comes at the same time as a gathering of the finance ministers and central bankers from the Group of 20 wealthy and developing nations—essentially the IMF's largest shareholders. The G-20 is pursuing an ambitious agenda of regulatory reform, including increased capital and liquidity requirements, with a Dec. 31 deadline for an agreement.

Mr. Strauss-Kahn said that the Obama administration's efforts to push through Congress a financial regulation package could hinder the development of a global regulatory regime because it may not be consistent with other nations' efforts.

"It comes too soon in terms of having a global answer," he said, though he noted that some of the administration's proposals are similar to IMF proposals, "so I don't think it creates a big problem."

At the same time, the G-20 is looking to revamp the global economy so it depends less on debt-financed spending by U.S. consumers. Trade-surplus countries, especially China and Germany, would be expected to ramp up domestic demand and cut exports, while trade-deficit countries, notably the U.S., would boost saving and export more.

The G-20 session and IMF sessions aren't expected to produce much in the way of concrete results, given that the financial regulation deadline is eight months away, and the G20 has no enforcement mechanism. Rather, Mr. Strauss-Kahn wants to keep pressure on countries to make promised changes.

But Egyptian Finance Minister Youssef Boutros-Ghali, who heads an IMF's policy-making group, said that because G-20 operates by consensus it's hard for the group to tackle politically difficult issues.

"They generally agree on things they can agree on" such as stimulus spending, he said. "If there are more fundamental problems, how do they come to a decision? Majority vote? Two-thirds? The G20 is doomed not to address anything that is controversial." Mr. Boutros-Ghali said that a revamped IMF, which has voting rules, would be a better place to make global changes.

On Tuesday, an IMF bank-tax proposal designed for G-20 nations was leaked and since then has dominated discussion by G-20 officials. The U.S. and Europe have generally embraced the idea, said a G-20 official, but Canada, Australia and Japan are balking.

Officials seek to alter the global economy to rely less on debt-financed spending by U.S. consumers.

The latter countries are arguing that their banks shouldn't be subject to new taxes because they didn't cause the global financial crisis and didn't require government bailouts.

The IMF proposed what it called a Financial Stability Contribution"—a tax on balance sheets, including "possibly" off-balance-sheet items, but excluding capital and insured liabilities—to pay for the costs of winding down troubled financial institutions.

On top of that, the IMF would have nations add a Financial Activities Tax, levied on the sum of profits and compensation of financial institutions. That would be paid to a nation's treasury to help finance the broader costs of a financial crisis.

Hyun Song Shin, a Princeton economist who is advising Korea's president on G-20 issues, said there may be several ways to break an impasse. Different countries could assess different tax rates, he said, or those countries that balk at imposing a tax might instead require tougher capital and liquidity requirements.

Reuters

World Bank President Robert Zoellick speaks in Washington on Thursday.