DJIA 10058.64 ▲ 1.52% | Nasdaq 2150.87 ▲ 1.17% | DJ Stoxx 239.19 ▲ 0.12% | FTSE 100 5111.84 ▲ 0.38% | DAX 5498.26 ▲ 0.24% | CAC 40 3612.76 ▲ 0.15% | Euro 1.3735 ▲ 0.25% | Pound 1.5605 ▼ 0.24%

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THE WALL STREET JOURNAL.

VOL. XXVIII NO. 8 | EUROPE | Wednesday, February 10, 2010

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EU bailout for Greece awaits German decision

BERLIN—Germany is considering a plan with its European Union partners to offer Greece and other troubled euro-zone members loan guarantees in a bid to calm fears of a government default and prevent a widening of the credit woes that have shaken global markets in recent days, people familiar with the matter said.

By David Crawford and Matthew Karnitschnig in Berlin, and Charles Forelle in Brussels

The proposed plan would be undertaken within the EU framework but led by Germany, one of the people said. German Finance Minister Wolfgang Schaeuble has discussed the idea in recent days with European Central Bank President Jean-Claude Trichet, according to the person.

The deliberations underscore concerns in Europe that the market turmoil surrounding high debt levels in Greece and other countries on the periphery of the 16-nation euro zone could undermine the monetary union.

It is unclear how the guarantees might be structured, but any initiative that allows countries in violation of the currency bloc's deficit rules, such as Greece and Spain, avoid the consequences of loose fiscal policies, would likely fuel concerns over the long-term viability of the common currency.

That the EU nonetheless is considering such a step suggests that policymakers view the alternative—a potential default of a euro-zone country—to be an even worse outcome and one that could have grave consequences for both the Europe and the global economy.

EU leaders are expected to discuss the situation at a summit in Brussels on Thurday. A final decision on the plan may not come this week but Germany has concluded that guarantees are likely the most efficient way to contain the debt crisis, a person familiar with the matter said.

A spokesman for Germany's finance ministry said no decisions on aid had been made.

A spokesman for EU President Herman Van Rompuy declined to comment. An ECB spokeswoman declined to comment.

For weeks, investors have fretted that Greece's budget deficits and national debt load put its sovereign bonds at risk of default if the country can't come up with the cash to make payments on its borrowings.

On Tuesday, reports that

Please turn to page 7


Bloomberg News

European Central Bank President Jean-Claude Trichet departs Australia Tuesday for the EU summit.

Toyota faces risk to image, ratings

By William Lyons and Javier Espinoza

Toyota Motor Corp. faced the prospect Tuesday of losing its "Aa1" rating as credit-rating firms threatened a downgrade amid analyst concerns that the auto maker faced uncertainty over its operations and finances.

The move came on the back of Toyota's announcing a recall of 437,000 Prius models world-wide to modify the software that controls the hybrid vehicles' antilock brake system.

The Japanese company already is trying to fix problems in millions of vehicles recalled out of concern they may suddenly accelerate.

On Tuesday, **Moody's Investors Service** confirmed it had placed the Aa1 senior unsecured long-term rating of Toyota under review for a possible downgrade. Separately, Fitch Ratings said late last month it had placed Toyota's "A+" rating on watch for a possible downgrade.

Analysts in Europe say Toyota's reputation has been damaged and that as a result of the global recall the car maker will lose competitive advantage.

Juergen Pieper, an automotive analyst with Metzler Equities in Germany, said Toyota was known for having the best production processes and

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The Quirk

Unknown scrapyard sculptors are outstanding in their fields in Kansas. Page 29

Editorial & Opinion

Saba Farzan: No tyranny, not even Iran's, can last forever. Page 15

European airlines seek to revise state financing rule

By Daniel Michaels

Nine top European airlines, including **Air France-KLM** SA, **British Airways** PLC and Germany's **Deutsche Lufthansa** AG, are lobbying to shake up how airplane sales are financed so they can get access to government export guarantees that most other airlines around the world now use.

The effort is a spillover from the credit crisis of late 2008 that could potentially roil the global aviation market. Last year, some $20 billion of subsidized guarantees helped finance more than 30% of the 979 jetliners delivered by Europe's Airbus and **Boeing** Co. of the U.S.

Airlines in the lobbying push, who instead depend on commercial financing and have seen lending rates rise since the credit crisis, say the government guarantees give their rivals a boost of several million dollars per airplane.

The nine carriers are from France, Germany, Britain and Spain, the home countries of Airbus. They want to rework a longstanding agreement between the U.S. and the European Union that limits which carriers can benefit from government-backed export financing.

The deal, known as the home-market rule, forbids airlines from the home countries of Airbus and Boeing from receiving the support.

"The arrangement is unfair," said British Airways Chief Executive Willie Walsh in an interview. "It clearly gives an advantage to those carriers that can access export credit."

Export credit consists of loans or loan-guarantees extended by a government to foreign buyers of the country's products and services. Britain and the U.S. created the system decades ago to boost overseas sales and help developing economies. Most countries now offer such credits, and airplanes are a major target. The U.S. Export-Import Bank, for example, funded $8.6 billion of Boeing's foreign sales in the bank's recent fiscal year, through Sept. 30.

Airlines in the lobbying push say guarantees mean their rivals have lower costs. Several participants cited the

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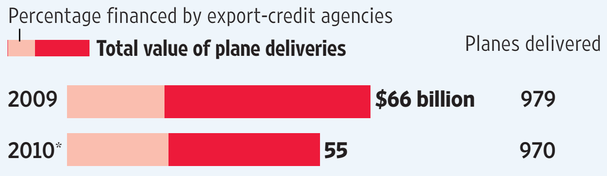
A big lift

Export-credit agencies are supporting a growing portion of Airbus and Boeing deliveries amid the financial crisis.



Sources: DVB Bank; the companies

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£1.50
Bahrain BD 1.50 - Egypt $1.75 (C/V)
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Chance of real reform slipping away

[Agenda]

By Iain Martin

"Wanted: New chief executive for large financial-services agency based in London, reporting to the government. Applicants should be prepared to endure abuse from ministers, the opposition, the press and even some of those in the banking industry. Long-term job prospects are limited and this position is offered only on a short-term basis as a potential incoming government is pledged to close down the organization or at least merge it with a rival. At the end of the successful applicant's tenure even a knighthood is not guaranteed."

As job descriptions go it doesn't sound too appealing, does it? But it is with something like that in mind that the Financial Services Authority must begin the search for its new chief executive following the resignation of Hector Sants Tuesday.

Mr. Sants was there throughout the British end of the financial crisis—from the Northern Rock debacle, through the meltdown of HBOS and the Royal Bank of Scotland, widespread criticism of the FSA being asleep at the wheel and the public backlash against the bankers. Tuesday, he indicated that three years of this was more than enough. He said he had never intended to work any longer than that and promptly served notice to quit.

For the U.K. government this is a headache it could do without. It will find it difficult to engineer the appointment of a strong successor, just as it approaches a difficult stage in the life of any administration.

A day comes, shortly after it becomes widely believed that there may soon be a change of government, when ministers pull the levers of power and find that they don't work in the way they once did. This works with patronage especially. "We'd very much like you to hop over to head X agency" finds plenty of takers when no election is in prospect. Then, quite suddenly when they think the other side might get in, the volunteers vanish.

Reuters

U.S. President Barack Obama (right) with Paul Volcker

Mr. Sants' resignation is also a headache for the opposition Conservatives. They are pledged to abolish the FSA and move its functions inside the Bank of England. This would end of the tripartite system of regulation established by Gordon Brown in 1997. To put it politely, it faced a certain amount of criticism after those involved failed completely to spot how vulnerable some British banks had become thanks to their innovative activities during the boom years.

> **The global coalition of policy makers has fractured beyond any chance of repair any time soon**

But Mr. Sants' departure adds further doubt and instability to the mix ahead of potential Tory reforms. It was already unclear how Shadow Chancellor George Osborne would avoid a new and expanded bank of England incorporating the defunct FSA becoming an unwieldy and over-large tangle of regulators and central bankers jostling for position.

It had been thought that Mr. Sants was set for a role as deputy governor of the Bank, and that this might help smooth the transition. Now the FSA must drift on over the course of an election and toward its break-up with its chief executive stuck in the departure lounge.

The U.K. isn't alone in experiencing such uncertainty. Indeed, it is indicative of wider political confusion when it comes to global financial regulation.

President Obama's attempt last month to set a bold course on reform hasn't produced anything resembling a consensus on what needs doing next. Mr. Obama tried to tap into the spirit of the original progressive trust-busters of the early 20th century, who took on large and monopolistic vested interests. He called for measures to limit the activities and size of the so-called mega-banks. The implication was that greater competition would create consumer choice and more stability. Investment banking should be separated cleanly from retail banking, he said. This was heady stuff.

But if he was hoping that the G-7 finance ministers' meeting in Canada at the weekend might pursue this agenda in any meaningful way he was to be disappointed. The most useful products of their summitry were some amusing pictures of central bankers such as the Bank of England's Mervyn King plonked on sledges being towed by huskies.

Where the G-7 failed, might its bigger brother—the G-20—succeed in agreeing to a program of reform along the lines of that envisaged by Mr. Obama? You shouldn't hold your breath. There is no sense that the Germans or French will oblige. Or that the British government would either—with nationalized banks aplenty they don't want to break up. The Tories say they are broadly in favor of the general direction of Mr. Obama but won't act without every other country in the G-20 doing the same.

And Mr. Obama's timing was off too. That he produced the vague outline of such reforms in the days after his party's shock election defeat in Massachusetts allowed his critics to say he wasn't serious, and that this was mere political opportunism.

It has underlined that the global coalition of policy makers and leaders that came together during the financial crisis has fractured beyond any chance of repair any time soon. In Europe there are now other more urgent priorities: namely dealing with the sovereign debt crisis in Greece and the coming fall-out.

It may be that later this year when Basel III appears, the result of technocratic negotiations aimed at agreeing new global rules governing banking and regulation, then all governments will be forced to act as one next year. Again, it might be unwise to hold your breath.

For now, the opportunity to use the crisis for a great program of reform coordinated by the governments in the G-20 has passed by. And amid the widespread confusion and vacillation which group is happiest of all? It's the largest banks, who go about their business rather more quietly than they once did—but not much more impeded than they were in the boom years.

ONLINE TODAY

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The Source

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"Singling out one company, or shutting down one project, won't solve a thing."

Prasenjit Bhattacharya on Vedanta's brush with environmental activists in "Vedanta, 'Avatar' and Tribal Activists"

Continuing coverage

Follow earnings results from European firms such as Air France and Sanofi at **wsj.com/earnings**

Question of the day

Vote and discuss: Has Hector Sants been an effective leader at FSA?

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

Previous results

Q: If you were in the market to buy a car today, would you consider buying a Toyota?

Yes	50%
Maybe	8%
No	42%

What's News

■ **Hector Sants submitted** his resignation as CEO of the U.K.'s Financial Services Authority, which faces an uncertain future. The opposition Conservatives have vowed to disband it if they win the next election. **9, 32**

■ **UBS reported** its first quarterly profit in more than a year, but its private-banking business continued to hemorrhage wealthy clients spooked by assaults on Swiss bank secrecy. **19, 32**

■ **GM plans to revamp** Opel and Vauxhall in part by boosting sales and market share, a strategy that some analysts question. **21**

■ **Small businesses** in the U.S. grew slightly more optimistic last month, while a report showed wholesale inventories fell in December. **10**

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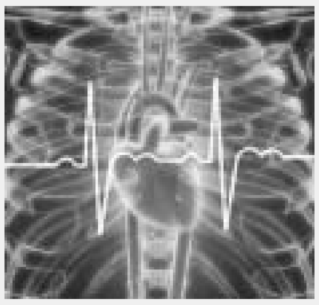

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Some entrepreneurs put in an Olympic effort. **28**

THE WALL STREET JOURNAL EUROPE
(ISSN 0921-99)
Stapleton House, 29 - 33 Scrutton Street,
London, EC2A 4HU

SUBSCRIPTIONS, inquiries and address changes to: Telephone: +44 (0) 207 309 7799. Calling time from 8 a.m. to 5 p.m. GMT. E-mail: subs.wsje@dowjones.com. Website: www.services.wsje.com

ADVERTISING SALES worldwide through Dow Jones International. Frankfurt: 49 69 9714280; London: 44 207 842 9600; Paris: 331 40 17 17 01.

Printed in Belgium by Concentra Media N.V. Printed in Germany by Dogan Media Group / Hürriyet A.S. Branch Germany. Printed in Switzerland by Zehnder Print AG Wil. Printed in the United Kingdom by Newsfax International Ltd., London. Printed in Italy by Telestampa Centro Italia s.r.l. Printed in Spain by Bermont S.A. Printed in Ireland by Midland Web Printing Ltd. Printed in Israel by The Jerusalem Post Group. Printed in Turkey by GLOBUS Dünya Baslnevi.

Registered as a newspaper at the Post Office.

 Editeur responsable: Patience Wheatcroft M-17936-2003.

Registered address: Boulevard Brand Whitlock, 87, 1200 Brussels, Belgium

NEWS

High-end retailers put hope on display

Pricing remains key for luxury-goods sellers

By Elizabeth Holmes
And Rachel Dodes

Optimism is creeping back into style, following three seasons of budget slashing, according to luxury-retail executives who will attend New York Fashion Week.

More than 50 designers will showcase their collections in the tents at Bryant Park in Manhattan this week as part of the twice-a-year fashion extravaganza staged for retail buyers and the press.

Forecasting consumer sentiment six months out—when those styles will land in stores—has become easier in recent months, as wealthy shoppers have exhibited an increased willingness to spend. Even so, there's a focus on luring back "aspirational shoppers."

"We think we've weathered the storm and want to move somewhat from defense to offense—but we're going to do it in a targeted, cautious manner," says Ron Frasch, president and chief merchandising officer of luxury retailer **Saks** Inc.

The environment is breeding what Saks Chief Executive Stephen Sadove calls a bifurcation of the market. Designers are limiting production of some high-end items to foster a sense of scarcity. At the same time, established brands are offering a broader range of entry-level goods.

Chloé, a French label known for its $1,200-and-up handbags, introduced a canvas handbag line this season priced 50% below its comparably sized leather goods. The brand has also been able to stoke demand for higher-priced products, such as a new $1,600 "Marcie" handbag, by keeping supplies low. Chloé Chief Executive Ralph Toledano says that the bag is almost entirely sold out for spring 2010.

Still fresh on the minds of retailers is the disastrous 2008 holiday season, when consumers abruptly stopped spending on anything that seemed optional, and the wealthy found conspicuous consumption quickly went from desirable to distasteful.

This year should be a little better. Retailers remain conservative but will begin to boost orders from designers for the latter half of 2010. The consultants at Bain & Co. are forecasting a "timid" global uptick for luxury in 2010, with 1% growth globally following an estimated 8% decline in 2009.

Core luxury consumers—those with assets of at least $5 million—have re-emerged from the spending slump, and people with at least $1 million in assets are on their way back as well, says Hana Ben-Shabat, partner at management consultancy A.T. Kearney.

Noticeably absent, however, are the "aspirational shoppers" who, before the recession began, drove the luxury boom by stretching to buy higher-priced prestige items. With credit tight and unemployment high, they remain on the sidelines—but are still window shopping and keeping track of trends, says Ms. Ben-Shabat.

Retailers are looking for ways to woo them back, primarily by pushing designers to create lower-priced collections.

High-end footwear brand **Jimmy Choo** has expanded its assortment of value-conscious styles, such as rubber-soled flats that retail for around $365.

Designer Tory Burch, whose collection is already in the lower-end of the luxury pricing spectrum, is adding more small leather goods as well as categories such as eyewear, with sunglasses for less than $200. "We're having great success with that," Ms. Burch said last month.

Saks Inc.

Scarcity and exclusives are being used to rebuild the luxury market. Above, Saks Fifth Ave.'s designer floor.

THE TOYOTA RECALL

Brakes spur Toyota to recall Prius

By Norihiko Shirouzu

TOKYO—A reluctant **Toyota Motor** Corp. on Tuesday announced a global recall of its flagship Prius and other gasoline-electric hybrid vehicles, even as executives suggested they weren't required to do so.

Toyota's quality chief, Shinichi Sasaki, said at a news conference that the brake systems in the recalled cars "meet safety standards," a comment implying the company isn't legally required to recall the vehicles. But Toyota decided to update software that controls the brake system to "be in accordance with the spirit" of those standards, Mr. Sasaki said.

Many at Toyota—from top executives to engineers to sales managers—believe the Japanese auto maker is being forced into the corrective action on its popular hybrids because of heightened government and public scrutiny of recent quality problems at home and in the U.S.

These executives say the Prius problems are much smaller than, and unrelated to, the sudden-acceleration complaints that have triggered criticism of the company.

A top quality executive said in Toyota City recently he believes the recalled hybrid vehicles' brake issue—what Toyota has described as a momentary loss of braking power during the slow and steady application of brakes on bumpy or slick roads—is a matter of "brake feel" that some people find problematic and others consider acceptable.

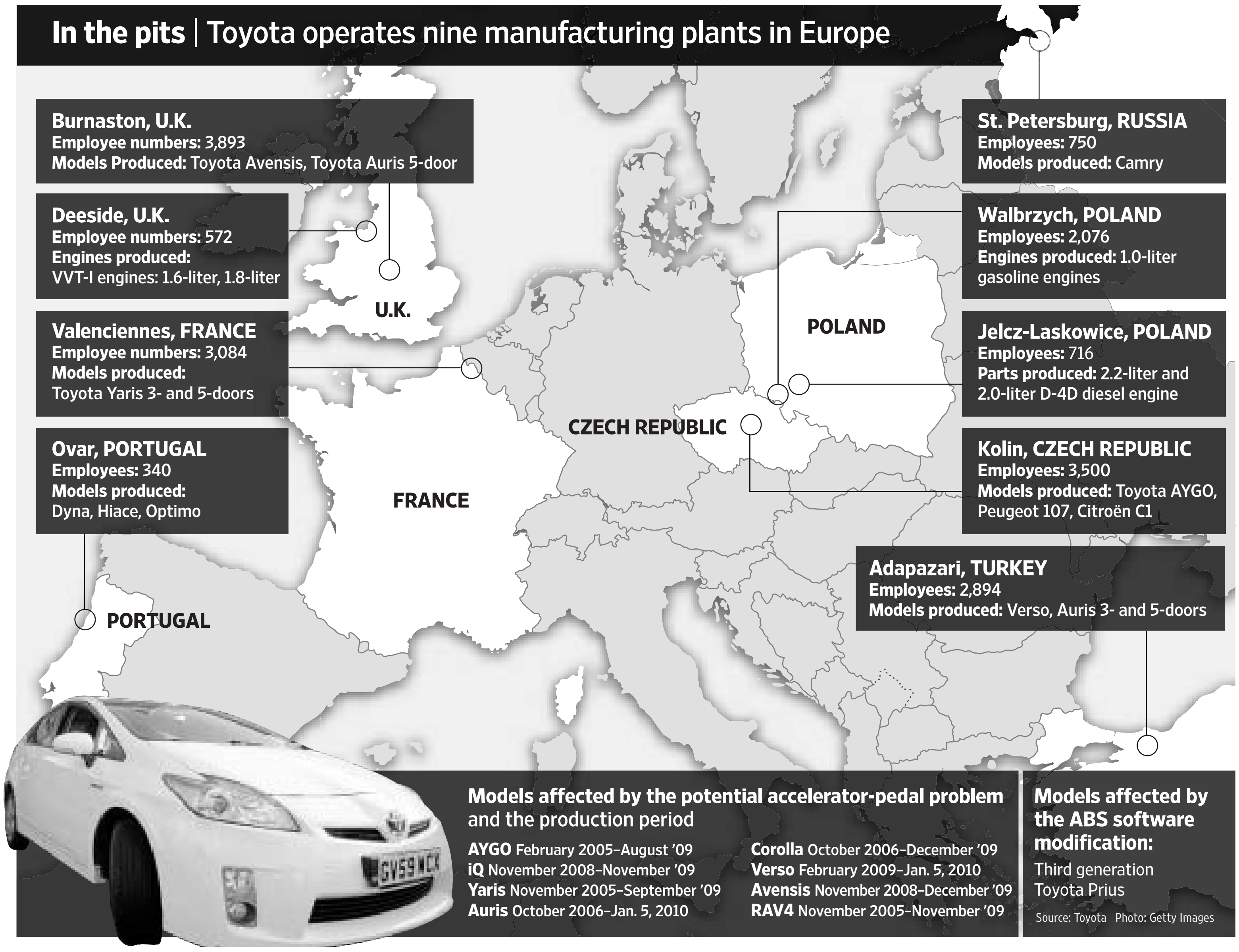
To him, it is "a matter of customer preference"—not something for which there should be a recall, an action tantamount to admitting a defect. Before the latest controversy, many Toyota engineers felt the issue could have been handled quietly, with dealers fixing the problem when customers raised issues.

Critics have said that mind-set is what got Toyota in trouble in the first place. "It might be that [Toyota] considered it a minor problem," Japanese Transport Minister Seiji Maehara said Tuesday in a briefing, referring to the brake problem. Mr. Maehara said Toyota must deal with the problem "quickly based on the viewpoint of customers."

Toyota officials acknowledge the company may have made mistakes in handling customer complaints in recent months and may have angered regulators, but at this point "this is 60% political," one U.S.-based top Japanese Toyota executive said.

Toyota said it will recall 437,000 hybrid cars world-wide, including the Prius, to fix the brake problems. The cars affected, in addition to the Prius, include the Prius Plug-In Hybrid, the Toyota Sai and the Lexus HS250h. In the U.S., Toyota is recalling about 133,000 2010 Prius cars and 14,500 2010 HS250h cars. In Japan, Toyota will recall 223,000 hybrid vehicles, while the number should total 52,900 in Europe.

The Prius recall follows a recall of about eight million cars to correct problems linked to sudden acceleration, which Toyota has blamed on improperly installed floor mats, as well as sticky accelerator pedals. The company said it has received 84 complaints on the brake systems of the recalled hybrid cars, though they haven't been blamed for any injuries or fatalities.



Source: Toyota Photo: Getty Images

Toyota faces hits to ratings, image

Continued from first page

quality control in the world. But the crisis has left it struggling to retain its competitive advantage over European auto makers. "Even before this global recall, other auto makers in Germany were already catching up in terms of quality."

"The current problem will wipe out Toyota's advantage in Europe and they will find it hard to come back to the position they had before," he added.

The number of vehicles recalled globally by Toyota has reached 8.5 million. Tuesday's Prius recall followed a separate recall announced Jan. 29 to reinforce the accelerator pedal assembly on just under 1.7 million vehicles to eliminate the potential risk of excess friction that could, in rare instances, cause the pedal to stick.

A Toyota representative said the first shipment of accelerator-reinforcement parts had arrived in Europe and repairs will start this week.

Announcing plans for a global recall of more than 430,000 of its flagship Prius hybrid cars on Tuesday and a production suspension of a high-end hybrid Lexus model, Toyota's president, Akio Toyoda, struck an apologetic tone.

"I don't see Toyota as an infallible company that never makes mistakes," Mr. Toyoda said at a news conference Tuesday. "We will face up to the facts and correct the problem, putting customers' safety and convenience first."

Mr. Toyoda has been criticized for being largely invisible during the two weeks after the company announced Jan. 21 the gas pedal recall in the U.S., Europe and China.

He apologized at his first public news conference last Friday, but was criticized by Japanese media for failing to outline concrete steps to tackle the safety crisis and reassure customers.

Michael Tyndall, an auto industry analyst at Nomura, said: "The amount of damage to the brand is contingent upon how quickly Toyota remedy the situation. It is only now that the seriousness of the situation is sinking in.

"Akio Toyoda needs to show consumers that Toyota is very, very serious about the inconvenience the value disruption and the concerns they have caused customers," the analyst said.

Tuesday's recall will primarily affect 2010 Priuses sold in Japan and the U.S. since last May. It will also cover three other hybrid models: the Prius plug-in, the SAI and the Lexus HS250h.

In Europe, the recall is being taken in response to reports of inconsistent brake feel during slow and steady braking on bumpy or slick road surfaces when the anti lock brake system is actuated.

The Prius holds a cherished spot in Toyota's vehicle lineup and is symbolic of its leadership in the "green" car market.

Toyota was one of the first companies to mass-market a hybrid, which combines electric motors with a gasoline engine, introducing the Prius in Japan in 1997. Its high gas mileage made it popular among environmentally conscious drivers, especially when gas prices spiked two years ago.

But the complexity of the Prius, a highly computerized car, has led to problems in the past.

In 2005, the company repaired 75,000 of them to fix software glitches that caused the engine to stall. The vehicle has also had trouble with headlights going out.

Corolla owner says he's wary of brand

By Javier Espinoza

LONDON—As authorities in the U.S. were reviewing steering complaints from Toyota Corolla drivers, complaints about the model emerged in Europe.

In the U.K., Bilal Mahmood, a 29-year old public-relations consultant in London, is the owner of a 2006 Toyota Corolla and says he has gradually grown wary of the brand.

"Toyota are known to be a reliable, efficient and most importantly a trustworthy brand," Mr. Mahmood says.

When he bought his second-hand car for £7,500 ($11,699) from a Toyota dealer in Doncaster, U.K., last December, it had only clocked 9,000 miles. "I got several recommendations from friends to buy other cars but I took the advice of my father, who has driven Toyotas all his life, and bought my car," Mr. Mahmood added.

He says he encountered initial acceleration problems before the recent news broke, but his local dealer assured him it was fine.

"I took their word. But now with all the news, I feel betrayed. I am sure Toyota will deal with the problem but it would have been nice to have seen their management on TV addressing the problem at the time rather than hear it from journalists.

Toyota wasn't immediately available to comment.

"When I heard of the recall last week, I called the garage again and they tried to ignore it but I have convinced them to look at it," Mr. Mahmood says. He has an appointment for next week.

Mr. Mahmood's Toyota garage is now looking into the problems with his cars and will likely try to fix the problem in the next couple of days.

His local dealership says, however, that despite the massive recall in Toyota vehicles it has hardly received any complaints at all.

Mark Reed of Key Cars, a dealership in Doncaster that sells second-hand cars, says there has been "no comebacks in relation to the recent recall."

EUROPE NEWS: THE DEBT AND DEFICIT CRISIS

Greece grapples with tax evasion

Country's shadow economy hurts attempts to rein in huge budget shortfall; a €50 receipt for a €40 taxicab ride

By Sebastian Moffett
And Alkman Granitsas

ATHENS—Greece has one apparently simple option for reining in a budget deficit that has roiled financial markets: Clamp down on widespread tax evasion, which costs the country an estimated €15 billion ($20.5 billion) a year, an amount that would pay off a big chunk of the budget deficit.

The trouble is, tax evasion in this Mediterranean country is extremely difficult to eradicate.

Trying to cope with its budget problems, Greece announced new austerity measures Tuesday.

Finance Minister George Papaconstantinou said public-sector salaries would be frozen and supplemental incomes for civil servants cut by an average of 10%. Salaries and bonuses for the prime minister, senior government officials and officials at state-owned enterprises will be frozen, and under some conditions reduced. The measures would save some €850 million this year, said Mr. Papaconstantinou.

The government also announced a higher marginal tax rate of 38% on people earning more than €40,000 a year, up from about 25%.

In addition, dozens of tax loopholes and special rebates will be eliminated, and taxes will be increased on dividends and offshore companies. The tax measures would yield some €1.2 billion in revenue this year, the government said.

The Greek shadow economy, which is made up of unreported income, was 25.1% of gross domestic product in 2007, according to Friedrich Schneider, a professor at Johannes Kepler University in Linz, Austria. The shadow economies of Spain, Portugal and Italy were all around a fifth of GDP. That compared with just 11.8% for France and 7.2% for the U.S., he said.

Trying to explain the rampant tax evasion, Prof. Schneider says countries like Spain, Portugal and Greece have had continuous democracies only since the 1970s, and people aren't used to governments representing the public interest.

"In most of these countries, what matters is your family. ... There is less of a sense of duty towards the state," says Alberto Alesina, a professor of political economy at Harvard. "Evading taxes is something you can freely talk about—and be proud of—at a dinner party in these countries."

Media reports are rife with accounts of corruption among tax officials. Ethnos, a newspaper, reported in mid-December that a 51-year-old Athens tax official had been arrested on suspicion of taking €1,000 from a pet-shop owner in exchange for not imposing a €3,000 penalty on the pet shop.

Meanwhile, in a government survey last year of 150 doctors in Kolonaki, an upmarket Athens neighborhood, half of the doctors said they were paid less than €30,000 a year. Thirty said they made less than €10,000.

"It is not possible for a taxpayer to declare an income of €15,000 while at the same time maintaining a big house, a big car, a recreational boat and sending his kids to private school," Mr. Papaconstantinou said Tuesday.

Repeated requests for comment on the survey of Athens doctors were unanswered by the Athens doctors association.

A taxi driver last week offered a business traveler a €50 receipt for a €40 ride, to enable the traveler to overclaim expenses to his company. The condition was that this receipt be scribbled on a piece of paper and not a printed receipt from his meter, which would result in the payment being registered.

Dimitris Mavrogiannis, who owns an auto-paint shop in the New Kosmos district of Athens, says he usually issues receipts, especially as a lot of his work is for insurance companies, who insist on them. But he says he makes exceptions.

"In the majority of cases, I do issue receipts," says Mr. Mavrogiannis, 58. "But sometimes people ask for a discount on the VAT tax and I say, 'OK.' "

Such tax dodging is a problem now, as Greece's budget deficit was likely around 13% of GDP in 2009. which led to a selloff of Greek government debt and boosted the interest rate the government has to pay.

Economists say there is no overnight fix, and the only way to solve Greece's tax problems is through incremental measures. Greeks say they would like a fairer system.

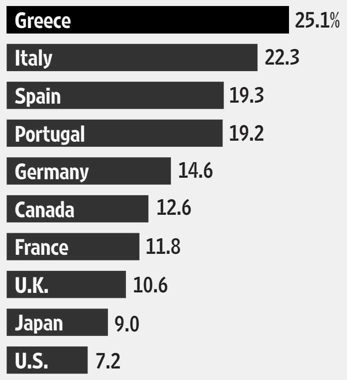
"I work for a large Greek construction company ... but of course, I have also done my own jobs on the side off the books," says Alexandros Foukis, 27, a building contractor. "What the government needs to do is provide incentives to people to issue a receipt."

Reuters

Greek Finance Minister George Papaconstantinou at a news conference in Athens on Tuesday after the country outlined new austerity measures.

Cast of billions

Size of the shadow economy in 2007, as a percentage of GDP



Sources: Lars P. Feld, University of Heidelberg; Friedrich Schneider, Johannes Kepler University Linz

Bank of Spain welcomes deficit measures

By Stephen Fidler
And Jonathan House

MADRID—A senior official at Spain's central bank said measures announced by the government to curb its budget deficit were a shift in the right direction.

José Luis Malo de Molina, chief economist at the Bank of Spain and a member of its policy-setting executive board, said the bank had been urging a response from the government to the challenges faced by the Spanish economy.

"We think it is a significant change in the right direction," he said in an interview.

In order to bring its deficit down to 3% of gross domestic product in 2013, the government said Jan. 29 that it intends to take revenue-raising and spending-reduction measures to slice about €50 billion ($68.3 billion), or 5.7% of GDP, from the budget deficit through 2013. Together with the automatic adjustments expected as the economy recovers, this will help bring down the deficit to under 3% of GDP from 11.4% in 2009.

"In the past we have been warning the government constantly that it was absolutely necessary to assume a program of fiscal discipline as soon as possible, and now clearly we welcome the change," he said.

Though he described the proposals as realistic, he said it might be necessary to make further adjustments, particularly if growth fell below government forecasts.

He welcomed statements from senior government officials in recent days saying that the government would take such steps if necessary. Mr. Malo de Molina said further spending cuts could be made relatively easily from government capital-expenditure programs.

Associated Press

Prime Minister Zapatero appears before the Spanish Senate in Madrid Tuesday.

For over a year the central bank has been urging the government to lay out a plan to rein in its budget deficit and Gov. Miguel Angel Fernandez Ordonez also has provoked the ire of government officials and union leaders by repeatedly calling for overhauls such as a revamp of the country's labor-market regulations.

Mr. Malo de Molina described the government's growth assumptions as slightly optimistic for the later years of its program.

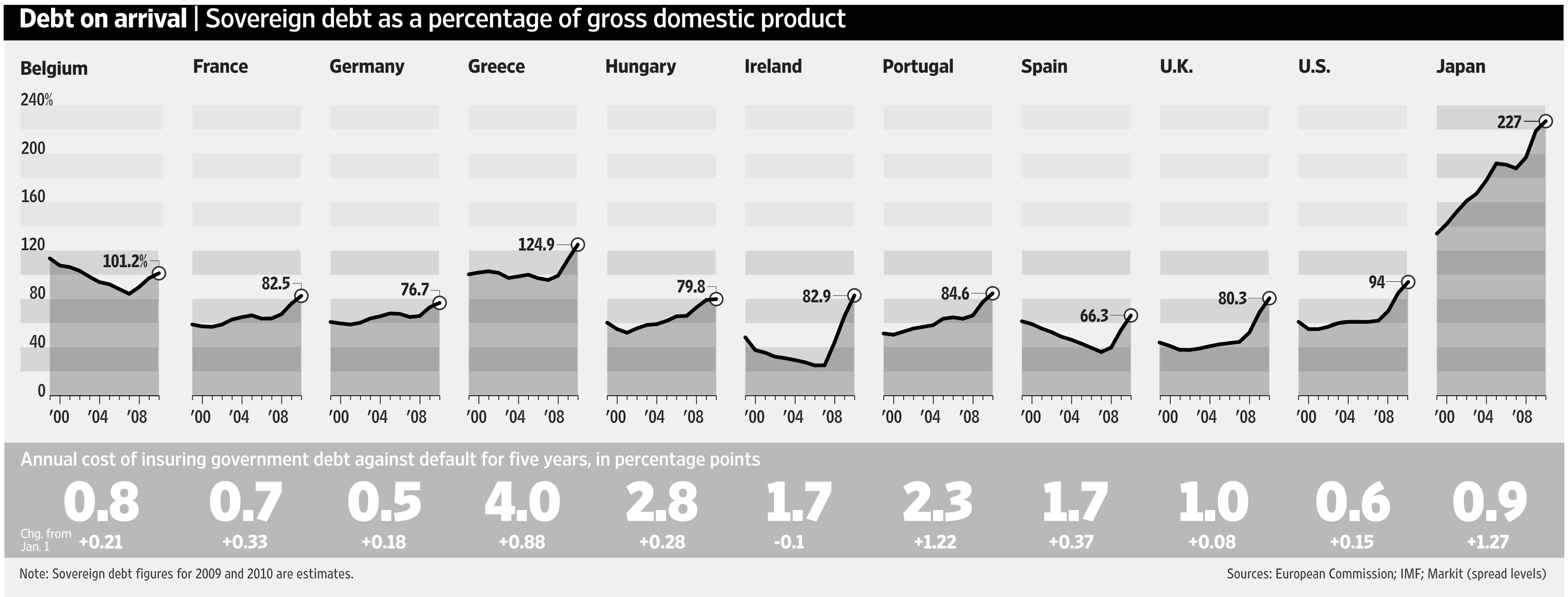
"It's not the whole horizon in which you have this optimism. Probably at the end, it's a little bit optimistic, but for 2010, 2011 we may discuss half a point but no more than that, and that means any potential deviation could be adjusted by additional measures."

The government forecasts a GDP contraction of 0.3% in 2010 and growth of 1.8% in 2011. It also projects 2.9% growth for 2012 and 3.1% growth in 2013.

He backed a government proposal to gradually raise Spain's retirement age to 67 from 65. "It helps a lot to re-establish sustainability in the long run of public finances. ... Spain has a serious problem with aging," he said.

Such a change would complement overhauls to make the labor market more flexible. However, he said the central bank was "not so satisfied" with the fiscal and pension measures. The government had raised the possibility of gradual overhaul of the labor market, he said, adding, "We think that the situation of the Spanish economy would have improved much more with a bold reform."

EUROPE NEWS: THE DEBT AND DEFICIT CRISIS



Germany, EU weigh steps to calm fears

Continued from first page

Mr.Trichet would cut short a meeting in Australia to travel to Brussels for the summit led the beleaguered euro to gain strength against the dollar and and sent Greek bonds trading higher, as investors interpreted the move as a sign that a bailout for Greece could be on the horizon.

Hopes deflated after Mr. Trichet's office said he had been planning to go since at least last month.

In the 90 minutes after stock markets closed in Europe, a flurry of reports indicated that German leaders had started seriously considering a Greek rescue plan. The euro quickly added to its gains against the dollar, rising above $1.38 and credit spreads tightened further. While European stocks were closed, U.S. shares shot higher, with the Dow Jones Industrial Average gaining more than 200 points to cross back over the psychologically crucial 10,000 level.

The cost of insuring Greek debt, as measured by credit-default swaps, plunged. Insurance for €10 million of five-year Greek debt dropped €80,000 to €340,000. Similarly measured Portuguese debt insurance dropped €45,000 to €200,000 while Spanish debt insurance fell €35,000 to €135,000. Portugal, earlier on Tuesday, announced plans for a long-term bond offering, but didn't specify a date.

As markets jumped and credit insurance costs plunged, a German government spokesman declared that no decision on a rescue had been reached. This reversed some of the market action momentarily, but by late in Europe's day investors had become convinced that serious discussions were under way in Germany to bail out Greece.

News that French President Nicolas Sarkozy would meet with Greece's Prime Minister Giorgos Papandreou on Wednesday added to the growing belief that a bailout was getting closer.

EU policy makers say the tumult in Greece poses the first real test of the credibility of the euro, the bloc's decade-old common currency.

In a sense, the euro is a risky experiment, an economic alliance built on common monetary policy but independent fiscal management, coupled with a weak political pledge that no individual country will spend too much—a rule that Greece has repeatedly violated over the past decade.

Greece's budget deficit for 2009 is expected to come in at close to 13% of its gross domestic product, far above the EU's ceiling of 3% of GDP.

—Adam Cohen and Dave Kansas contributed to this article.

Debt markets 'hyperventilate' over Greece

BY LAURENCE NORMAN

LONDON—Nobel Laureate Joseph Stiglitz on Tuesday brushed aside the debt-market pressures facing Greece, saying they reflected irrational investors "hyperventilating" over a country whose fiscal situation is in hand.

In an interview, Mr. Stiglitz, who is acting as an informal adviser to the Greek government, said Prime Minister George Papandreou had adopted a smart plan for paring back the debt.

"If anyone looks at the [debt] program they have put forward, it's actually a very thoughtful program and a comprehensive program," he said. "It's not actually clear to me that there is any fundamental problem other than a speculative attack."

Faced with spiraling borrowing costs, Greece's Socialist government has presented plans to the European Commission that aims to reduce the budget deficit to 3% of gross domestic product by 2012 from 12.7% in 2009.

The European Union backed those plans last week but has so far resisted committing to intervene on Greece's side if the financial pressures intensify. But news reports suggesting some form of aid was in the works soothed market tensions, reducing Greece's borrowing costs and the cost of insuring investors against a possible default on Greek debt.

However, the yield on 10-year Greek bonds remained some 3.15 percentage points above German bund yields.

Mr. Stiglitz said the EU should make explicit its support for Greece and other countries, like Spain and Portugal, facing debt-market pressures. He said the EU could consider some kind of contingency fund that could be tapped in an emergency by member states.

"I think the euro zone now realizes this is not an issue of Greece alone. It's an issue for the EU because of what's at stake in Spain, Portugal and possibly ... other members," Mr. Stiglitz said. "Europe has to make a commitment to support these countries and there are a variety of forms which it could take," he said.

Mr. Stiglitz, who is in London to promote his book on the financial crisis and sat down Monday with Prime Minister Gordon Brown, was scathing in his assessment of the recent behavior of investors.

He said debt-market investors "are in the process of hyperventilating," and he described the recent price moves in the credit-default-swap market, which measures the cost of insuring against default, as "absurd."

However he said that with irrationality gripping debt markets, the failure of Europe's leaders to stem speculative pressures could have a high price.

"Unfortunately, I've seen enough of this kind of pattern to know that they can strike anywhere. So nobody's immune," he said.

Mr. Stiglitz's attacks on investor behavior are nothing new for an economist who has long criticized orthodox Washington consensus policies and pointed up flaws in free-market theories.

Nobel laureate Joseph Stiglitz, in London on Tuesday, called the prospect of a default by the U.S. or the U.K. 'absurd.'

However, the former World Bank chief economist and winner of the 2001 Nobel Prize for economics, offered kinder words for another of his traditional bête noires—the International Monetary Fund.

Mr. Stiglitz said the more relaxed conditions the IMF is imposing on lending programs these days means Greece shouldn't close off the option of approaching the IMF for funding if needed.

"I think that things have changed. Ten years ago my view would have been quite different," he said.

Mr. Stiglitz acknowledged his role in advising the Greek government hasn't been central. He said he had offered Mr. Papandreou "strategic" advice on economic policy ahead of the October election, which the Socialist party won handily.

Now, Mr. Stiglitz said he stays in touch with the Greek leader and members of his team but is not in daily contact.

And Mr. Stiglitz said that, at a time when Greece's government is trying to woo bond-market investors, it is probably for the best that he keeps his distance.

"That's why I think it's good that [Papandreou] has gotten a whole range of people involved and is not relying on just one perspective," he said.

"That's one of the marks of a good leader, I think."

Tymoshenko to challenge poll results

Near-complete returns show win by Yanukovych, who urges challenger to concede; her chances seen as 'close to zero'

By James Marson

Agence France-Presse/Getty Images

Supporters celebrate Viktor Yanukovych's poll victory at a rally in front of the central election commission, in Kiev on Tuesday.

KIEV, Ukraine—Supporters of losing candidate Yulia Tymoshenko said they were preparing legal challenges to returns from Ukraine's presidential vote, as her rival's party maneuvered to have parliament oust her as prime minister.

Ms. Tymoshenko remained out of public view for a second day, refusing to concede defeat in Sunday's runoff vote. Near-complete returns give opposition leader Viktor Yanukovych a winning margin of more than 3% in balloting that international observers judged to be fair.

Mr. Yanukovych urged Ms. Tymoshenko on Tuesday to acknowledge that he had won a clean election. In an interview on CNN, he recalled her leading role in the Orange Revolution, the street demonstrations against electoral fraud that overturned his tainted victory in the 2004 presidential race.

"If Tymoshenko doesn't accept the will of the Ukrainian people, doesn't accept the results of the elections, but continues to push Ukraine into political chaos, she risks turning from the hero of the Orange Revolution into its executioner," Mr. Yanukovych said.

Ms. Tymoshenko canceled a scheduled news conference Tuesday. Her spokeswoman couldn't be reached for comment.

Members of her party said they planned to call for recounts at 1,000 of the 33,000 polling stations, claiming irregularities there favored Mr. Yanukovych. They said the party was also preparing an appeal asking the courts to nullify the overall result as fraudulent.

"We will recognize defeat only after a decision by the courts," said Andriy Shkil, a member of parliament from Ms. Tymoshenko's party. "We will appeal both the preparation and conduct of the election."

The challenges would be filed after the Central Election Commission certifies the election results next week and could delay the handover of power from President Viktor Yushchenko to a successor.

Meanwhile, Mr. Yanukovych's Party of Regions is trying to lure members of parliament to abandon Ms. Tymoshenko's coalition and vote to dismiss her as prime minister. If successful, the effort would remove her as an obstacle to his legislative agenda, which includes budget-busting wage and pension increases that she opposed.

A potential new coalition began to take shape last month after the Party of Regions gained support from three other factions to dismiss the interior minister, an ally of Ms. Tymoshenko.

Neutral election observers gave Ms. Tymoshenko's legal challenges little chance of success, in light of positive assessments of the vote by international monitoring teams and Western governments. "Her chances are minimal, if not close to zero," said Oleksandr Chernenko, head of the Committee of Voters of Ukraine, an independent monitoring group.

The U.S. Embassy issued a statement Tuesday saying the vote took place "in a calm atmosphere" and marked "another step in the consolidation of Ukraine's democracy."

Russian President Dmitry Medvedev called Mr. Yanukovych and congratulated him on "success in the elections." Mr. Medvedev stopped short of calling him the winner, as the Kremlin rushed to do in 2004 when it openly supported him against Mr. Yushchenko in the presidential election.

Mr. Yushchenko won a court-ordered revote in that race and named Ms. Tymoshenko prime minister. But their alliance quickly descended into enmity and bickering, stalling promised overhauls and disheartening their supporters.

Many voters in the Orange strongholds of western Ukraine stayed home Sunday, enabling Mr. Yanukovych to win with slightly fewer votes than he gained in the 2004 revote. Most of his support both times came from Russian-speaking regions of eastern and southern Ukraine.

European airlines seek new state financing rule

Continued from page 1

example of Irish budget carrier **Ryanair Holdings** PLC, a major Boeing customer and one of the biggest users of U.S. Ex-Im Bank guarantees. Ryanair competes directly with Britain's **easyJet** PLC and Germany's **Air Berlin Group**, neither of which can tap export credit.

Air Berlin and easyJet said they are among the nine carriers in the lobbying effort but declined to comment. Ryanair Finance Director Neil Sorahan denied the company has an unfair advantage.

U.S. carriers also can't use export credit financing for Airbus and Boeing orders, but none is yet part of the protest. That is partly because all U.S. airlines are restricted, so there is less distortion within the U.S. than within Europe. Still, officials from the nine European carriers said they hope to enlist U.S. airlines, which face competitors from the Middle East, Latin America and Canada that use export credit.

The European carriers last month sent a letter to their governments and EU trade officials spelling out both their grievance and a proposed resolution, say executives involved in the lobbying campaign. The proposal calls for opening export credits to all airlines world-wide, while limiting all carriers to funding at most 20% of their fleets with the guarantees. The carriers said officials are still assessing the issue.

Several of the carriers involved have previously complained that export credit financing distorts the airplane market and still argue that ideally it should be stopped. But they say advocating its elimination now is unrealistic, so instead are pushing for equal treatment. They hope that by organizing many of the world's biggest airlines in this push, they can make a stronger point.

The home-market rule is an unofficial and nonbinding agreement struck between the U.S. and EU in 1986 to level the playing field between Boeing and Airbus. Both sides have adhered to it because export credit was long used mainly by weak carriers in emerging markets. Financial markets in the five home countries, meanwhile, were highly developed and carriers there could arrange commercial loans at rates below the cost of government-backed borrowing.

The issue has become a sore point since the global credit crisis hit in late 2008 and commercial rates to fund jetliner purchases soared. Carriers from highly developed economies—including oil-rich Norway and the United Arab Emirates—joined airlines from less-developed countries in aggressively tapping export credits.

U.S. Ex-Im Bank Vice President Bob Morin, at a conference on aviation finance in Dublin last month, noted that export credit agencies' avoidance of the five home countries means they "have ceded 45% of the world's aircraft market to private financing, which is a good thing". Mr. Morin and counterparts from Europe said that changing the home-market rule would be difficult, in part because the agencies don't finance domestic sales.

Giving the U.S. and the four European countries access to export credits could significantly increase the amount of funding the government agencies do for jetliners—a shift many officials say they don't welcome because it would be expensive and airplanes already dominate their portfolios. Other assets they finance include farm machinery, medical equipment and power plants.

Officials from Boeing and Airbus, a unit of **European Aeronautic Defence & Space** Co., declined to comment.

Officials from some of the protesting airlines argue that export credits keep airplane production levels artificially high. "It creates the next bubble," said Markus Ott, head of corporate finance at Lufthansa. At the conference in Dublin, Mr. Ott cited Dubai's Emirates Airline, which recently secured a U.S. Ex-Im Bank-backed loan paying an interest rate of 3.47% and soon after issued bonds without government backing on which it had to pay a rate more than twice as high, 8.68%. He said the gap demonstrates how government support artificially lowers the cost of buying airplanes for airlines with access. An Emirates spokeswoman declined to comment.

Marc Verspyck, Senior Vice President for Finance at Air France, said that export guarantees allow recipients to place larger orders than they otherwise could, which in turn allows them to bargain down prices by "a couple of million euros" per plane. "For an airline buying 10 or 15 aircraft a year, it's a lot of money," Mr. Verspyck said.

Export credit guarantees are also "crowding out" loans to airlines that don't have government support, because banks prefer lending to airlines with state guarantees, said Ignacio De Torres, Finance Director at Spain's **Iberia Lineas Aereas de Espana** SA.

EUROPE NEWS

FSA in turmoil as Sants to leave

Opposition Conservatives have vowed to dismantle the U.K. regulator if, as expected, they win the next election

By Alistair MacDonald

Hector Sants said he will step down as chief executive of the U.K. Financial Services Authority, the regulator that he led through the credit crisis but which faces an uncertain future.

Mr. Sants took over as CEO in July 2007, just as the financial crisis was starting, with plans to stay three years. "I intend to stick to that timetable," Mr. Sants said in a statement Tuesday.

Mr. Sants will depart this summer, not long after a general election in which the current favorite, the opposition Conservative Party, has said it would dismantle the agency and split its powers between the Bank of England and a new consumer-finance agency.

Mr. Sants has been critical of the proposals, saying they will lead to disruption. In a speech in November, Mr. Sants said it would be "grossly irresponsible" to split up the FSA and so lose the lessons it has learned in the crisis. Resources shouldn't be diverted to look at "structural questions" at a time when the financial system is still under stress, he said in that speech.

According to people familiar with the matter, the Conservatives have sought to reassure Mr. Sants about his future. Tory Treasury chief George Osborne met Monday with Mr. Sants to deliver the message that he would have a role under a Conservative government.

Bloomberg News

Hector Sants's departure is likely to hasten a sense that the agency is doomed.

Mr. Sants's departure reflects uncertainty across the U.K. as investors, companies and policy makers try to plan ahead of an election that must be called by early June. U.K. government bonds have come under pressure this week in part as investors worry that no party will get a clear majority, making it harder to cut Britain's record deficit.

Some FSA officials have complained that the Tory proposals run the risk of prematurely rendering the agency a lame duck at a time when it should be making an impact at the international negotiating table. Now, Mr. Sants's departure is likely to hasten a sense that the agency is doomed.

The FSA now faces the task of sounding out candidates to head an organization that ultimately may not exist. Names mentioned by regulatory experts Tuesday included Sally Dewar, the head of the regulator's Risk Business Unit, and Jon Pain, the FSA's head of supervision.

The agency said it will name a successor in "due course."

Mr. Sants, a former head of Credit Suisse AG's European investment-banking operation, joined the FSA in 2004 and had been head of the regulator's wholesale markets division before become CEO. He was one of the last senior FSA executives remaining from a period in which the regulator exercised its now-discredited "light touch" and "principles-based" regulation.

Critics say that system, with its emphasis on companies following broad principles rather than exact rules, made Britain vulnerable to the financial crisis. The FSA has admitted that it had made mistakes in regulating banks like Northern Rock, the mortgage lender that in 2007 triggered the U.K.'s first bank run in centuries after it was forced to turn to the Bank of England for cash.

"He managed to distance himself from that...but it's difficult for him to disentangle himself entirely," said Andrew Shrimpton, a former FSA regulator now at asset management consultancy Kinetic Partners.

Mr. Sants is credited for recognizing and apologizing for the FSA's culpability and launching changes that sometimes put it ahead of others in reshaping global financial regulation. In that task, he has been joined—and sometimes overshadowed—by Adair Turner, who was appointed chairman of the FSA at the height of the credit crisis with a mandate for regulatory reform.

The FSA now requires some of the country's largest banks to provide it with weekly disclosures on risk and performance, compared with the monthly, or even quarterly, requests of old. Under Mr. Sants's direction, it hired about 280 additional supervisors, began sending the police to arrest insider-dealing suspects, and last year levied £35 million ($54.6 million) in fines, over a third more than in 2008. In a move away from the FSA's old style of putting faith in management, executives are kept on a tighter leash and large banks must get the FSA's approval for key hires.

Under Mr. Sants's watch, the FSA also unveiled proposals for banks' pay practices that are designed to minimize risk-taking.

—Sara Schaefer Muñoz contributed to this article.

EU parliament accepts slate of new commissioners

By John W. Miller

BRUSSELS—The European Union's parliament ratified the appointment of a new slate of leaders for the European Commission, the EU's executive office of 20,000 elite civil servants.

The 26 commissioners, appointed by President José Manuel Barroso, were approved Tuesday by a vote of 488 to 137, with 72 abstentions. The European Court of Justice in Luxembourg will swear in the new commission for a five-year term on Wednesday.

Confirmation of the commissioners, one of the European Parliament's main responsibilities, was delayed a month when Bulgaria's nominee for humanitarian-affairs commissioner, Rumiana Jeleva, was pressured to resign amid allegations of her husband's improper relationships with organized crime, although Mrs. Jeleva and her husband denied the allegations. Other commissioner-designates, notably Neelie Kroes of the Netherlands, the former competition commissioner who will take the information-technology post, struggled in their appearances before committees, but none posed a serious issue. Bulgaria quickly nominated a new commissioner, World Bank Vice President Kristalina Georgieva.

Mr. Barroso's second term promises to be far different from the previous five years. Those years were spent crafting complex regulations on chemicals, carbon emissions and mobile-phone rates, admitting Romania and Bulgaria to the EU and waging minor battles with member states over their government spending and debt levels.

Now the challenge is more daunting and serious: how to climb out of the worst economic crisis to date in the EU's history. Government budgets are bleeding red across the EU, especially in the 16-nation euro zone. Greece is on the verge of needing a massive bailout. Spain, Portugal, Italy, the U.K. and others face massive deficits. Total investments in the EU are down around 10% from year-earlier levels, and gross domestic product volume was down 4.1% in the third quarter of 2009 from the year-earlier period. EU unemployment is at 10%.

The commission is staffed by economists and thinkers who draft papers laying out proposals for Europe to create more-innovative, environmentally friendly industries, shore up public finances, boost research investment and deal with the pension liabilities of an aging population.

The challenge, say officials and analysts, will be overcoming political unwillingness in EU countries.

Mr. Barroso "will need to provide a coherent approach to things," says Janis Emmanouilidis, an analyst at the Brussels-based European Policy Centre. Offering a forceful response to globalization "is the only way" for the EU "to avoid gradual marginalization," he says.

Mr. Barroso told the European Parliament on Tuesday that "stronger economic coordination is the only way forward" to overcome the financial crisis.

The EU in a rut

As a new 27-member European Commission takes office, its challenge will be to reverse the most difficult economic situation in the EU's history. Some key figures, from the most recent data available:

GDP volume, 3Q '09 vs. 3Q '08:
–4.1%

Investments, by volume, 3Q '09 vs. 3Q '08:
–11.5%

Industry production, Nov. '09 vs. Nov. '08:
–6.1%

Expected total government budget deficit, 2010:
7.5%

Unemployment, ages 15-24:
21.5%

Unemployment all ages:
10%

External trade balance, first 11 months of 2009:
–€105 billion

Current-account balance, first nine months of 2009:
–€129 billion

Sources: Eurostat; EU commission

Associated Press

José Manuel Barroso, president of the European Commission, at the European Parliament in Strasbourg, France, Tuesday.

He promised to "build a competitive and sustainable economy, tackle climate change and modernize the EU's industrial base."

The commission will also have to draft a new budget for the EU. The EU has a budget of around $150 billion a year.

The EU must also decide if it wants to enlarge its current size to include countries on its periphery like Turkey, Ukraine and Moldova.

Snowed-in capital braces for more

Congress struggles to conduct business as another storm barrels into city still largely shuttered by weekend blast

By John D. McKinnon

WASHINGTON—The U.S. government—still all but shuttered by a weekend blizzard—braced for a second major storm expected to arrive Tuesday afternoon.

Federal agencies remained closed Tuesday, and many expected that would be the case Wednesday as well because forecasters predicted the new storm would bring a fresh 10- to 20-inch layer of snow. The government shutdown itself isn't cheap. Officials estimate that it costs about $100 million a day in lost productivity for the government.

So many lawmakers remained absent Tuesday afternoon that the House canceled all votes for the remainder of the week.

House Majority Leader Steny Hoyer (D., Md.) said the snow had created a "huge challenge" for local officials tasked with clearing roads and suggested "there may be" the need to provide some federal assistance.

Senate Majority Leader Harry Reid (D., Nev.) said work would continue in that chamber, though. He said he intended to move a much-discussed jobs bill by the end of the week.

"We really need to finish the bill this week," he said.

But some lawmakers privately questioned whether that would be possible and suggested next week might be a more likely time frame for the vote. Senate and House versions would then need to be reconciled before a final vote.

The Senate was scheduled to hold two votes late Tuesday on pending nominations. No formal action has been scheduled for the balance of the week, which covers the last scheduled work days before Congress leaves town for a long-planned recess. "I hope we don't have to put things over," Mr. Reid said.

Travel was so difficult following the weekend blizzard that it took Sen. Charles Grassley (R., Iowa) 12 hours on Monday to reach Washington from Des Moines. He wound up spending the night in his office so he would be available for an early-morning TV interview. "It's not easy to get around," Mr. Grassley said.

Associated Press

Workers clear sidewalks in Racine, Wisc. Snow from the same storm was expected to hit Washington later.

The weather-related delays only added to the problems of Democrats as they seek to regain their political footing following the loss of their supermajority in the Senate and the subsequent collapse of negotiations over Mr. Obama's health-care overhaul.

The weather also had more immediate consequences for the Washington area. The Washington area's three major airports, still plowing runways from the weekend storm, prepared for a full schedule of canceled flights Tuesday night and Wednesday. Tara Hamilton, spokeswoman for the Metropolitan Washington Airports Authority, which oversees Reagan and Dulles airports, said crews have worked day and night since Friday to remove the 18 inches of snow that fell at Reagan and the 32 inches at Dulles. "We've had 60 dump trucks literally hauling the snow away," Ms. Hamilton said. "It's just a huge amount of snowfall. We're hauling, snow-blowing, everything."

Amtrak, battling not only heavy snow but also fallen trees and power outages, began canceling many trains early Tuesday in anticipation of a second heavy snowfall. Southbound service from Washington to Richmond, Va., already was halted because of the earlier storm, and many trains heading north to New York and Boston were canceled Tuesday.

Small businesses bit more optimistic

By Sara Murray

Small businesses grew slightly more optimistic last month, though they are still climbing out of a funk brought on by a credit crunch and a severe recession.

The Index of Small Business Optimism, released Tuesday by the National Federation of Independent Business, rose 1.3 points to 89.3 in January. It is up 8.3 points from March, the index's low since the recession began at the end of 2007 and its second-lowest reading in history.

Separately, a new report showed businesses cut wholesale inventories in December.

Economists are keeping a close watch on the mood of small businesses, which typically create jobs rapidly during economic expansions.

"Despite the marginal increase in January, small businesses continue to lag the overall economic recovery," RDQ Economics analysts wrote in a note to clients. "Historically, small businesses have created much of the hiring in an economic expansion and the weak state of small business confidence remains a roadblock to faster recovery."

The report found the fraction of small businesses making capital expenditures rose from the prior month but remained weak.

Regular borrowers said credit was still difficult to obtain. The businesses surveyed said lackluster sales was their top problem and this meant they didn't need to hire. Just 9% of owners added employees; 19% cut jobs.

A larger employment survey confirmed that employers didn't feel any urgency to add workers. The number of job openings in the U.S. rose 2.6% to a seasonally adjusted 2.5 million in December, the Labor Department's Job Openings and Labor Turnover survey showed Tuesday. The number of hires fell 1.3% to 4.1 million, and layoffs and firings rose 3.4% to 2.1 million in December.

There were 6.1 job seekers per open job in December, down a bit from 6.3 job seekers chasing each job in November, the left-leaning Economic Policy Institute noted.

"To absorb the over 15 million officially unemployed workers in this country, plus the nearly 2.5 million 'marginally attached' workers...job openings and hiring must rebound dramatically," said Lawrence Mishel, president of the institute. "This report offers no indication that that is happening."

Meanwhile, wholesale inventories decreased 0.8% to $383.57 billion in December, compared to a 1.6% increase in November, the Commerce Department said Tuesday. Stockpiles for both durable goods, meant to last three years or more, and nondurables declined.

Companies slashed inventories deeply in the first nine months of 2009 to rid excess supply accumulated during the recession. The inventory drawdown forced businesses to increase production to replenish inventories.

—Jeff Bater contributed to this article.