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Crews persist in BA strike

By Michael Carolan
And Daniel Michaels

LONDON—British Airways PLC's cabin crews walked off the job for a second day Sunday, as the union representing the striking workers called on management to reopen negotiations and avoid another strike next weekend.

"I will be appealing to British Airways at board level to take matters in hand and restart negotiations to reach an agreement which would allow the strike scheduled for next weekend to be averted," said Tony Woodley, joint general secretary of Unite, the crew's union, in a letter to members Sunday.

The appeal came on the second day of the three-day strike, after talks between the two parties collapsed on Friday. The weekend's industrial action is the first strike by BA cabin crew in 13 years.

A four-day strike is planned to begin March 27. Mr. Woodley said in his letter he wants to avoid the second strike.

But BA Chief Executive Willie Walsh has strong support from the company's board for the hard line he has taken in pushing to change labor practices at the airline. Mr. Walsh is trying to cut costs and streamline an organization that in some areas still works along terms established before privatization two decades ago.

A BA spokesman said Sunday the company hadn't been contacted directly by Unite about restarting negotiations. He said Mr. Walsh is willing to meet with Unite at any time, but the company's current offer is less generous than a recent proposal because its terms are reduced by the cost of the strike.

Analysts have estimated the strike is costing BA roughly £10 million ($15 million) a day in revenue and many millions in profit.

But with the company already on track to post heavy losses in its fiscal year through March 31 due to the global recession, many analysts have concluded that Mr. Walsh is willing to take a hit to this year's results with the aim of achieving long-run cost reductions and better positioning the company for profits when a recovery arrives.

The airline, which long profited from flying high-paying business passengers to and from London, has been hit especially hard during the financial crisis. It has worked harder than many European rivals to bring down operating costs, industry officials say.

Unite officials and some staff argue that the changes Mr. Walsh has pushed through, such as cutting staff levels on some flights, will undermine the carrier's status as a premium airline..

The company said Sunday it had been able to reinstate some flights to its schedule at both Heathrow and Gatwick airports as crew members continued to break the strike and turn up for work.

Eight long-haul flights and 36 short-haul have been reinstated, BA said, after 52% of the company's cabin crew reported to work as normal at Heathrow, the company's main hub.

A Unite spokeswoman disputed BA's claims that large numbers of cabin crew were breaking the strike, saying just nine crew members had turned up for work Sunday out of 1,100.

Ready to hammer down U.S. health-care legislation

European Pressphoto Agency

U.S. Speaker of the House Nancy Pelosi carries the gavel used to pass Medicare legislation in 1965, as she leads Democrats to a historic health-care vote. **See article on page 7; updates at WSJ.com.**

French opposition scores a win

By David Gauthier-Villars

PARIS—President Nicolas Sarkozy suffered a setback on Sunday, more than halfway into his five-year mandate: His conservative party was crushed in the second round of regional elections as French voters appeared increasingly wary about the fate of the generous but debt-choked social welfare model.

A coalition of Socialist, Communist and green movements scored a landslide victory, garnering 53% of the votes, according to preliminary national projections from polling agency CSA.

Mr. Sarkozy's ruling Union pour un Mouvement Populaire, or UMP, and the Front National of far-right leader Jean-Marie Le Pen collected 37.5% and 9.5%, respectively, CSA said.

"Let's face it," Jean-François Copé, head of the UMP lawmakers in the National Assembly, said on French television. "It's a real defeat for us."

Preliminary results suggest the UMP would keep control of Alsace; conquer La Réunion, a French overseas territory that had been governed by a left-wing coalition; and lose Corsica, polling agency TNS Sofres said.

The president has said results of the regional vote would have no impact on national policy. Mr. Sarkozy's chief of staff, Claude Guéant, said Sunday that Prime Minister François Fillon would remain in that post, but would meet with the president on Monday to discuss what the senior aide called a "technical" cabinet shuffle.

Mr. Sarkozy is under growing pressure to clarify his policy. He was elected in 2007 on the promise that he would bring France out of a prolonged economic malaise and cut unemployment in half by diluting state intervention and introducing more free-market policies. But last year's recession and a sharp rise in joblessness have led Mr. Sarkozy to change tack and call for giving state administration a bigger role.

In Sunday's regional vote, the opposition Socialist Party won control of most regions through coalitions with Communist and green movements.

Preliminary results in some regions showed Mr. Sarkozy may have lost touch with blue-collar workers, voters he wooed in 2007. On Sunday, many returned to the Front National, the far-right movement, pollsters say.

The Quirk

In Mile High city, marijuana sparks a counterculture clash **Page 29**

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PAGE TWO

Resolving Europe's economic dilemma will require more than sleight of hand

[Agenda]

By Irwin Stelzer

U.S. President Harry Truman, weary of hearing his economists conclude "on the one hand, but then on the other hand," famously asked for a one-armed economist. He's fortunate he never found one. For any economist who feels certain about his reading of the economic tea leaves, who sees no "other hand," is, to put it mildly, more than a little overconfident.

All by way of excuse for this attempt to figure out just what is going on in the European Union and euroland.

On the one hand, things are brighter than they were last year, when the areas' economies were contracting at a rapid rate. No one is expecting that dismal performance to be repeated this year or next. But on the other, neither is anyone expecting anything like satisfactory growth. The Economist Intelligence Unit is guessing that growth will be at an annual rate of 1.0% and 1.1%, this year and in 2011, respectively.

The move out of recession is the result of an increase in exports. On the one hand that's good news: Otherwise, the EU economies would continue to shrink. But on the other hand, some of the increased exports, especially those from Germany to other euro-zone countries, are exacerbating serious imbalances. Germany's trade surplus with its EU partners is causing serious problems, especially for the struggling periphery countries.

"Germany's...trading partners cannot sustain deficits forever," notes the Economist.

Germany's surplus is its EU partners' deficits, which they have to finance by borrowing. And borrowing is precisely what Greece and similarly situated countries need less of. Europe needs Germany to base more of its growth on domestic demand, its consumers to start spending and stop paying down debt, neither of which they show signs of doing.

Associated Press

Luckily for U.S. President Harry Truman, he never found a one-armed economist

Germany's surplus is its EU partners' deficits, which they have to finance by borrowing.

As Jefferies, the securities and investment-banking firm, points out in its latest report, consumption in Germany comes to only 57% of gross domestic product, compared with closer to 70% in the U.S. and the U.K.

Then there is the news coming out of Berlin, Athens and Brussels. Greece won't cut spending unless it is guaranteed that its euro-zone partners will somehow enable it to borrow at lower interest rates. Otherwise, argues Greek Prime Minister George Papandreou, the premium the country now pays—more than three percentage points above what Germany is charged—will eat up a good portion of the savings from his austerity program.

But German Chancellor Angela Merkel, after dithering and trying to find some way to avoid becoming the banker of last resort for profligate, inefficient members of the euro zone, finally hit on an alternative. She told Mr. Papandreou to take his troubles to the International Monetary Fund, outraging her euro-zone partners who find that a humiliating admission of their inability to manage their currency without outside help.

As Mrs. Merkel's partners see it, Greece would be merely the first domino to fall. Spain might well be next. Its socialist government is having some second thoughts about the extent and speed at which it should impose an austerity program, inflicting pain on public-sector workers, or begin cleaning up the mess in its banking system. The country's 44 small regional banks, or *cajas*, have some half of their $1.8 trillion in assets tied up in property loans. Of those, somewhere between $220 billion and $330 billion (estimates vary) are loans to property developers, many of which are in no position to repay. The government says one-third of the cajas are insolvent, and is hoping to solve the problem by organizing mergers with healthy institutions, but is running into opposition from regional politicians, who would much prefer some sort of bailout. If the IMF rescue team heads to Europe it might just as well visit Madrid as Athens, pain-averse Spanish politicians might decide.

All of these problems have driven the euro down from its November peak of around $1.50 to about $1.37. With the U.S. economy recovering at a more rapid rate than Europe's, and with the Federal Reserve likely to raise interest rates sooner than the European Central Bank, experts are expecting the euro to continue to weaken against the dollar. On the one hand, this is good news. Europe's exporters now find their goods more competitive in world markets, even against those made in China, which pegs its yuan to the strengthening dollar.

On the other hand, a weaker euro raises the price of imports, especially those, like oil, that are denominated in dollars. That increases the possibility that when the EU economies do start to recover, inflationary pressures will force the European Central Bank to tighten sooner than it might otherwise want to do. On the one hand, that is good news: It would contain inflation. On the other hand, it's bad news: It would slow the recovery.

All proof that Harry Truman was wishing for something that just doesn't exist.

—Irwin Stelzer is a business adviser and director of economic-policy studies at the Hudson Institute.

ONLINE TODAY

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Reader comment

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"Willie Walsh is intent on destroying one of the last great British institutions."

Reader **Mark Prowler** on the chief executive of British Airways and a three-day strike by the airlines' crew

Video series

Our reporters in Athens look at Greek debt woes and potential solutions at **wsj.com/greekdebt**

Question of the day

Q: Should British Airways tough it out or seek a quick union settlement?

Vote online at **wsj.com/dailyquestion**

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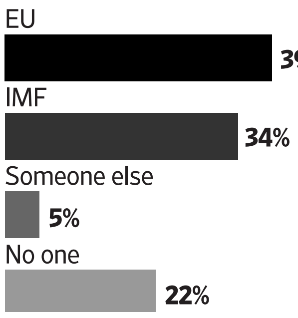
Q: Who will lead the Greece financial rescue?



What's News

■ **The leader** of the U.K.'s opposition Conservative Party pledged to introduce a levy on banks if his party wins the coming election, regardless of whether there is international agreement on such a move. **5**

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NEWS

‘That’s My Jet!’ Repossessions soar

Business takes off for reclaimer Ken Cage

By Robert Frank

SANFORD, Fla.—Ken Cage is racing through a private aviation terminal near Orlando when his BlackBerry buzzes with bad news. The plane he is about to repossess is scheduled to take off for Mexico in three minutes.

Even worse, the Cessna’s owner and pilot is on his way back from lunch—and he is rumored to be six-feet, six-inches tall.

“I’d rather not stick around to find out,” Mr. Cage says.

Mr. Cage, 44 years old, stands guard by the door as his partner Randy Craft walks onto the tarmac and approaches a shiny white turboprop. He quickly picks the lock on the door and ushers in the repo team’s pilot, Dave Larson. The plane’s propellers roar to life, and after clearance from the control tower, the $350,000 ride lifts off the runway and into the sky.

Mr. Cage and Mr. Craft climb back into their Ford pickup and tear out of the parking lot, just as the plane’s owner pulls in. “He’s a minute late,” says Mr. Cage, peering out the window. “Lucky for us.”

Ken Cage isn’t your typical repo man. Rather than snatch cars from an over-extended middle class, he takes back yachts, planes and other toys from the over-leveraged rich.

Business is thriving, even as the economy begins to improve. His company, Orlando-based International Recovery Group, repossessed over 700 boats, planes, helicopters and other property last year valued at more than $100 million. Business, he says, is up six-fold from 2007.

He has reclaimed everything from $18 million Gulfstream jets and Bell helicopters to 110-foot Broward yachts, $500,000 recreational vehicles and even a racehorse. Before the financial crisis, most luxury items he pulled in were valued between $30,000 and $50,000. Today, they are at $200,000 to $300,000—meaning defaults are hitting people at a much higher income level.

Last year, says Mr. Cage, International Recovery’s revenues soared to the eight figures, up from just a few hundred thousand when he and two partners bought the firm in 2005.

Banks hire Mr. Cage to retrieve their collateral after a borrower has defaulted. Once he grabs the property, he cleans it up or makes needed repairs and sells it to a new buyer. He then gives the proceeds, minus his fees and expenses, back to the bank. While the standard commission for most repossessions is between 6% to 10% of the resale price, Mr. Cage has lowered his fee to as little as 2% as a way to beat back growing competition.

Mr. Cage can’t name names. But he estimates that 70% of his targets made and lost their money from real estate—either as developers, Realtors or contractors. Most of his jobs are in Florida, Arizona, California, Nevada and other sun states where real estate was hit hardest.

The son of a Philadelphia-area trucking-company owner, Mr. Cage started out in the cash-management department of J.P. Morgan, then worked in the collections department at Chrysler Finance, where he hired repo firms to pick up cars.

Separating flashy toys from their owners seemed to be much easier—especially from a logistical perspective. Unlike cars, which can be hard to find and take, yachts and planes are often traceable through Federal Aviation Administration or marine records.

Occasionally, the rich rear up to protect their prizes.

Mr. Cage says that he and Mr. Craft have been hit by cars, threatened with shovels and chased on foot countless times. Recently, Mr. Cage says he was on a yacht assignment in Jacksonville, Fla., when the owner boarded another boat and zoomed after him, Bond-style. He soon gave up the chase, and Mr. Cage kept his craft.

Ken Cage

International Recovery Group’s specialty is taking back luxury craft like this $15 million jet.

EUROPE NEWS

Church faces scandal fallout

Pope apologizes to Irish Catholics, as Bavarian region grapples with wider allegations

BY VANESSA FUHRMANS

REGENSBURG, Germany—Europe's widening sexual-abuse scandal has shaken Catholics across Pope Benedict XVI's native Germany, but perhaps nowhere as much as in Bavaria, the country's Catholic heartland where some of the most sensitive allegations have emerged.

In Germany, where hundreds of allegations of decades-old abuse have come to light since January and engulfed 22 of 27 Roman Catholic dioceses, the Catholic Church faces its worst crisis in post-World War II history. Polls show a majority of Germans believe the scandal has undermined the church's credibility, and recent government data suggest the revelations have sparked a surge in Germans leaving the church, whose membership, like that of Protestant churches, has long been on the decline.

In Germany's southeastern stretches along the Danube, where the Catholic church remains a mighty social and economic force, Germans are confronting the scandal with a mix of anger and conflicted loyalty to a church that plays such a role in social services, education and other facets of daily life.

The scandal in Germany has come particularly close to German pontiff in one case in which a priest who was a known sex offender was returned to pastoral work in the Munich archdiocese while Benedict XVI presided as archbishop there in 1980. The archdiocese has said a subordinate has taken responsibility for the move and that then-Archbishop Joseph Ratzinger was unaware of it.

Over the weekend, the pope in a letter expressed "shame and remorse" for the flood of sexual abuse cases that have swept through Ireland's Catholic church but didn't mention the events in Germany and stopped short of outlining any new policies or disciplinary actions for confronting thousands of abuse cases, many decades old, that have been documented in Ireland in recent years.

The letter drew criticism from Irish victims and others for not acknowledging any responsibility of the Vatican in the scandals or acknowledging sexual abuse as a more systemic problem within the church.

Many in the Bavarian university town of Regensburg, where Benedict once taught theology, expressed disappointment that the pope left out any direct mention of the abuse allegations rooted in his homeland.

"I expect more from the church, that it opens its arms to comfort its members and to have an open dialogue about what's happened," said Marianne Pesold, 69, a devout Catholic who directed much of her ire toward the supreme pontiff. "It's not a living church to have it all around us and for it not be talked about."

But she added, "I would never leave the church. I'd rather protest."

In Regensburg, the scandal hits particularly close to home not just because some allegations are connected to the its cathedral's renowned Domspatzen, or "Cathedral Sparrows" choir, which the pope's brother, Georg Ratzinger, directed for 30 years, but because the church remains so interwoven in the region's social fabric. Here, 78% of the diocese's population belongs to the Catholic Church compared to 30% nationwide, a density reflected in the crucifixes that hang in many restaurants, shops and offices.

Agence France-Presse/Getty Images

An Irish Catholic at a Belfast church reacts the day after the pope's apology..

With more than 20,000 people working in church-supported hospitals, nursing homes, schools, libraries and other social services, the church is one of the largest employers and economic forces in the Regensburg area.

Its signature presence, though, is the 1,000-year-old Domspatzen boys choir and the local boarding and preparatory schools where its members live and attend classes. Georg Ratzinger, who led the choir between 1964 and 1993, hasn't been implicated in any of the allegations that clergy and other church staff abused young boys. He says he wasn't aware of sexual-abuse allegations.

The Domspatzen allegations are an especially painful blow, says Werner Schrüfer, cathedral vicar and the head of an inner Regensburg parish, not just because the choir is such a source of cultural and religious pride but because it has been seen within the church as a model of modern Catholic education.

On the streets, he says, parishioners stop him and talk to him about the sermon he gave a few weeks ago. "I tried to put it in theological terms: The basis of Christian faith is trust...With sexual abuse trust is destroyed," he said. "People are glad they can openly discuss it."

At the same time, he added, many feel besieged by what they view as an attack in some media and political circles on the church as an institution. "For some outside the church, this is just what they've been waiting for," Monsignore Schrüfer says.

In a letter read aloud during Sunday morning's mass in the Regensburg Cathedral, Bishop Gerhard Ludwig Müller devoted equal time to deploring sexual abuse and the manner in which the church often handled such cases in the past , and the gauntlet of reporters and television cameramen that Domspatzen children and their parents have endured recently. "The goal is to pull a jewel of the diocese into the mud," he wrote.

Accusers are still coming forward. Alexander Probst, owner of a dog training school in a Bavarian village, says that at as an 11-year-old in the Domspatzen boarding school in Regensberg in 1971, he was first beaten, then sexually abused by an aide who'd slip into the room he shared with other boys to fondle him several nights a week.

Mr. Probst, 49, said he would splash cold water on his chest at an open window in the hopes of getting sick and taking refuge in the infirmary to avoid the aide's advances. After several months, he broke down and told his father, who pulled him out of the school.

Neither Mr. Probst nor his father can remember how detailed they were in their complaints to the school at the time or how the diocese reacted. The Regensburg Diocese says that a year later, the aide was let go because another parent complained about his too close-relationship to her son, though not specifically citing sexual abuse. It's now investigating Mr. Probst's allegations and reported them to prosecutors.

After Mr. Probst went public in a German magazine last week, the former aide, now a priest, was forced to resign from his priestly duties in another Bavarian diocese, the Regensburg Diocese said.

"For the first time I feel I've been treated with respect and what happened to me has been acknowledged," said Mr. Probst.

Still, like many Bavarians, even Mr. Probst remains a Catholic officially, electing to pay a church tax that in total supplies 70% of the German church's revenues. Under German law, taxpayers pay a roughly 8% equivalent of their total income tax to whichever church they belong or can opt to "leave" the church and not pay the tax.

Many German Catholics have done just that as the abuse scandal has widened. In Regensburg, so far 70 people, overwhelmingly Catholic have opted to quit their church this month, already more than the monthly average of 66 in 2009, according to city data. In much bigger Munich, 472 people have left their church in the first two weeks of this month, 104 more than the same period a year ago.

Though Mr. Probst says although he doesn't attend church, he remained a member because it was important for his two now-grown sons to participate in a big part of community life. "It's the church's personnel that have made the mistakes," he said. "But that doesn't have to do with my belief in God."

In an interview published Sunday in the Swiss newspaper SonntagsBlick, Abbot Martin Werlen of the Einsiedeln Monastery, where some allegations of abuse have surfaced, called on Rome to "act more quickly," adding: "A word from the pope should come when the situation arises, not two months later."

Over the weekend, the head of Germany's Catholic Church, Archbishop Robert Zollitsch, apologized for not more doggedly pursuing a sexual abuse allegation two decades ago when he directed human resources and staffing at the diocese in Freiburg. Instead of handing the case over to state prosecutors, he sent the priest into early retirement because of lack of more firm evidence, the Freiburg diocese said.

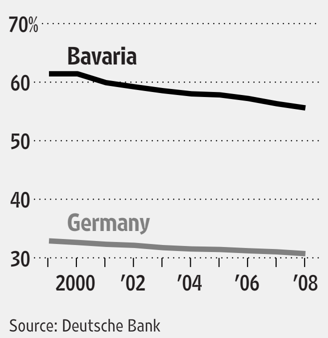
When another abuse victim came forward in 1995 with further allegations about the priest, Mr. Zollitsch confronted the priest again with plans to hand over the case to authorities. The priest subsequently committed suicide.

"I should have been more forceful in searching for witnesses and victims," the archbishop said in a televised news conference. "I apologize to the victims in the name of the archdiocese and ask for forgiveness."

—Stacy Meichtry contributed to this article.

Losing religion

Catholic Church membership as a percentage of the population in Germany has declined



Source: Deutsche Bank

EU faces pressure to address sick banks

BY ADAM BRADBERY

BRUSSELS—Pressure is growing for the European Union to develop a system for handling the failure of large cross-border banks, but the complexity of the issues involved and divergent national opinions on the details pose big challenges.

These differences could delay the creation of a system to contain the fallout from the collapse of a large bank like Lehman Brothers, which went bust in September 2008, worsening the financial crisis.

The EU was warned by the International Monetary Fund that it needs to develop a system for dealing with the failure of cross-border banks to avoid taxpayers having to foot the bill for future bank failures.

"Politicians need to rise to the challenge," said Dominique Strauss-Kahn, IMF managing director, at a European Commission conference to discuss how to develop a system for handling failing cross-border banks. "We do not have a lot of time to waste, and this opportunity should not be squandered or deferred."

The question of how to spread the cost of bank bailouts is central to the issue of dealing with failing banks that have operations in a number of countries and may hold depositors' cash in each.

Michel Barnier, the commission's head of internal markets and services, said the EU will need to find a way to create a single pool of cash from which future bailouts can be funded.

"My personal conviction is that financial institutions should contribute to a European resolution fund," he said at the meeting.

But this is a proposal that some central bankers and regulators say would encourage banks to continue taking risks because they know there would be a fund to bail them out. It would also be impossible to determine how large it should be to manage the largest crisis.

The financial crisis that emerged in mid-2007 demonstrated most European regulators lacked adequate tools to restructure firms in a short time and that any measures they did have differed across the region.

This made it difficult to deal with the failure of cross-border banking groups quickly enough to save them or stop the fallout from spreading to other parts of the financial system.

Regulators have divided the challenge into three parts: developing ways to intervene early in a bank's problems; overhauling national bank-resolution measures to handle cross-border banks; and harmonizing European bankruptcy laws.

The Committee of European Banking Supervisors, which is composed of EU banking regulators and advises the commission on supervisory issues, has proposed a "toolbox" of measures designed to ensure regulators can identify bank problems at an early stage and rescue or wind them up.

Nevertheless, some regulators feel even these rules will only work if supervisors cooperate more closely with each other.

—Matt Dalton in Brussels contributed to this article.

European Pressphoto Agency

David Cameron, the leader of the opposition Conservatives, said the tax is inspired by a proposal from President Obama.

Tories vow bank levy

Labour, banks decry it as dangerous; details, size remain vague

By Alistair MacDonald
And David Enrich

Banks moved back onto center stage in U.K. politics, as the opposition Conservative Party said it would introduce a U.S.-style bank levy if it wins this spring's general election.

The levy would repay taxpayers for bailing out banks during the credit crunch, Conservative leader David Cameron said in a speech Saturday.

In a rare pairing, bank representatives joined with the Labour government to criticize the Tory proposal as vague, populist and potentially dangerous, claiming it could make British banks uncompetitive.

The Tory announcement comes ahead of a busy week in which the government will announce its annual budget. This will include the creation of a "Green Investment Bank" that will plough £2 billion ($3 billion) into environmentally friendly energy and transport projects, according to a person familiar with the matter.

Mr. Cameron said the bank levy was inspired by U.S. President Barack Obama's proposed Financial Crisis Responsibility Fee, designed to recoup taxpayer funds used in bank bailouts and reduce risk-taking by banks.

"In America, President Obama has said he will get taxpayers back every cent they put in," Mr. Cameron said. "Why should it be any different here?"

The Labour and Conservative parties have argued for months that banks should pay a levy, with Prime Minister Gordon Brown suggesting earlier this month the money should be used to pay down country's deficits. Until this weekend, both had said it was only feasible if all the major economies agreed to a levy. The Conservatives now say they will go ahead regardless, saying bank taxes in the U.S. and Sweden showed a consensus is emerging.

An international agreement is far from certain. Canadian Finance Minister Jim Flaherty rejected "out of hand" any efforts to tax banks in this way.

Conservative officials on Sunday said the details and size of the levy would depend on the extent of international coordination. The more coordination, the bigger the levy could be.

One person familiar with the Tory proposal said its tax would more likely imitate the U.S. tax as a levy on bank's wholesale funds, or the money that banks raise from capital markets.

This would likely fall hardest on companies like **Barclays** PLC that have large investment-banking businesses.

If the tax applies to any bank with a presence in the U.K., major Wall Street firms such as **Goldman Sachs Group** Inc. could be vulnerable due to their reliance on wholesale funding.

The proposed tax, like its U.S. counterpart, could become another factor leading banks world-wide to intensify their quests for deposits—one of the few funding sources that would be exempt from the proposed levies. That trend already is being encouraged by pending regulations requiring banks to hold more deposits, which are considered a more stable, less risky source of funding.

A bank tax is another potential blow to the banking sector in the U.K., which frequently is on the end of political criticism and was hit late last year with a one-time tax on bankers' bonuses. The industry is facing tighter capital and liquidity requirements from both U.K. and European regulators.

Some U.K. bank officials were dismissive of the Conservative plan, saying it appeared so vague as to be meaningless. "It's political kite-flying," one bank official said.

Bank officials also disputed Mr. Cameron's rationale for such a tax. They pointed to forecasts from the Treasury that the government is on track to fully recoup the hundreds of billions of pounds that were pumped into the banking sector.

The British Bankers' Association said banks already pay a larger share of taxes than their share of overall economic activity, and the best way to reduce risk taking is through capital requirements.

Treasury Chief Alistair Darling said the proposal was taking a "hell of a risk" with the international competitiveness of an industry that employs one million people in Britain.

But the tax will likely win support from the British public, which remains bitter over the banks' role in the country's worst post-war recession and has been angry to see bankers receiving bonuses.

Mr. Cameron's proposal is likely to further raise the question of whether U.K.-based banks will consider moving their headquarters or parts of their operations abroad, to tax-friendlier domains. Countries such as Switzerland have attempted to lure banks and other financial firms with low taxes.

Mr. Darling said his budget Wednesday will include measures to encourage private industry. That will include a £1 billion investment in the Green Investment Bank, financed through the privatization of state assets, which the government hopes to see matched with £1 billion of private finance, the person familiar with the matter said. This bank will invest in projects such as rail links, offshore energy and nuclear power, which the private sector has been slow to back.

With international investors calling on the U.K. to cut debt, Mr. Darling has said there will be no populist giveaways in what will be a sensible budget. Prime Minister Brown also will promise Monday to save billions of pounds in public spending through smarter use of digital technology, his office said.

—Sara Schaefer Muñoz contributed to this article.

German competitiveness is villain for Greek economy

[The Outlook]

By Brian Blackstone

FRANKFURT—Greece and Europe's other intensive-care economies face a threat that can't be solved by cutting public spending or raising taxes: a loss of competitiveness.

In the eyes of those struggling economies, the villain is Germany—the euro zone's largest economy—which has emerged as the region's most competitive. By raising the competitive bar, Germany makes it harder for its neighbors to compete to sell their goods and services at home and abroad, a factor that in turn affects their ability to grow out of their current debt-laden holes.

To be sure, German wages are high, but even higher productivity means it is relatively cheaper to hire workers and produce high-value manufactured products there, even compared with traditionally lower-cost Greece, Portugal or Spain.

"Competitiveness is the key issue in the whole debate" over state finances, says Peter Jungen, chairman of Peter Jungen Holding GmbH, a company that invests in start-ups, and chairman of Columbia University's Center on Capitalism and Society.

France's finance minister, Christine Lagarde, caused a stir in Europe last week by openly questioning Germany's export-dependent growth model, and suggested it consider policies to spur domestic demand.

By keeping a lid on labor-cost growth, Germany's exports are able to compete on price despite a high euro. But that comes at the expense of market share for others in the euro zone, critics say. Whereas Germany rang up a €136 billion ($185 billion) trade surplus last year, Spain, Greece and Portugal ran sizable deficits.

Germany countered swiftly. Economics Minister Rainer Bruederle called it "unfair" to be criticized when other countries "lived beyond their means and neglected their competitiveness."

There are three ways for countries to make their products attractive globally: rein in labor cost growth; boost productivity; and devalue currencies. The last option isn't available to the euro zone, which has a single currency that is, by most measures, overvalued. The first two, though helpful over time, imply economic pain for years.

Germany suffered through that process. Faced with the tech-bubble collapse a decade ago and low-cost competition from Eastern Europe—and tagged as Europe's "sick man" in the early 2000s—German industry trimmed wage growth while the government enacted tough policies aimed at getting people off long-term unemployment.

It paid off. According to the European Commission, since monetary union in 1999, unit labor costs in Germany have fallen about 15%. They rose 3.5% in Greece over the same time period, 10% in Spain and 13% in Ireland and Portugal. That doesn't mean German workers come cheap. Their manufacturing wages and benefits are among the highest in Europe, at about €34 an hour, according to the Institute for the German Economy in Cologne. Greece's are half that; Portugal's even lower. But those countries still lost ground because productivity in Germany rose more quickly than in much of Southern Europe. That means German companies could produce more for less.

Europe's fringe has to do much more than restrain labor costs, economists say. Spain needs to find new sources of growth to replace the housing bubble that drove growth—unsustainably, in hindsight—over the past decade. Ireland will have to make due with smaller contributions from real estate and finance. Greece must cut the size and salaries of its public sector. Until that happens, growth will be slow, as evidenced by sharply higher unemployment in all three countries.

That has a big effect on state budgets. Spending cuts and tax increases, especially by Ireland and Greece, have been heartily endorsed by European officials. The aim is to bring double-digit deficits as a share of GDP to less than the EU's 3% limit in three years. There is just one problem: They won't do much good unless economies are growing, bringing in tax revenue and easing pressure on social spending.

"If countries are not competitive enough and cannot devalue their currencies, economic growth declines, and so does the ability to bring their fiscal houses in order," said Nicolaus Heinen, an economist at Deutsche Bank Research. That risk is even more acute if economic growth plus inflation—or nominal GDP—doesn't keep pace with interest rates governments must pay on their debt, a particular problem for Greece given the high premium Athens must pay to sell its bonds.

Germany isn't making things any easier. The metalworkers union IG Metall recently accepted a new contract with very low wage growth to protect jobs, an indication Germany is doing all it can to maintain its cost edge. "It's good for German exports, but the flip side is Greece and Ireland and Spain have to do even more in terms of labor-cost deflation to catch up," said ING Bank economist Carsten Brzeski.

Even Germany's economy faces some headwinds. Productivity fell about 5% in 2009 as employment stayed high in the face of a big output drop. But, productivity in the U.S. and China, two big competitors in the global market for high-value manufactured goods, continues to rise.

Meanwhile, Germany's politically popular job-support measure, known as Kurzarbeit, may turn out to be a major drag on competitiveness. Under that program, Berlin picks up the tab for some of workers' wage and social-insurance costs, keeping them in their jobs. But it prevents resources from being moved from one sector to another.

"We're buying social peace, but we're facing a future loss of innovation," Mr. Jungen said.

EUROPE NEWS

Merkel disputes Greek-aid need

Tensions mount ahead of Brussels summit

By Marcus Walker

BERLIN—German Chancellor Angela Merkel said that Greece doesn't need financial support and that European Union leaders shouldn't make the question of aid for Greece the focus of their summit in Brussels later this week.

In an interview with Deutschlandfunk radio, Ms. Merkel warned other European leaders against unsettling financial markets by raising "false expectations" that there will be a decision on aid for Greece this week. She insisted that Greece should sort out its own debt problems despite growing calls from other European policy makers for Germany to back stronger support for Greece.

Later, the German government issued a statement saying Greek Prime Minister George Papandreou told Ms. Merkel in a telephone conversation Sunday that his country doesn't need financial help. "The Greek prime minister confirmed that Greece needs no financial aid," the German statement said.

Ms. Merkel praised the tough austerity measures that Mr. Papandreou's government has undertaken and reiterated readiness to defend the euro-zone's stability, the statement said. A spokesman for the German government, who declined to be named, said Ms. Merkel stressed her readiness to do "everything necessary to preserve the stability of the euro zone."

Tensions between Germany and other EU countries over how to handle Greece's debt crisis and the bloc's wider economic strains have been growing ahead of the EU's two-day summit in Brussels on Thursday and Friday. Other European policy makers have been growing increasingly frustrated at Germany's blocking of stronger action within the 16-nation euro-currency zone to end uncertainty over whether Greece can repay its debts.

Germany's government faces strong domestic resistance from voters and lawmakers to any bailouts of euro-zone members that, unlike Germany, have pursued loose spending policies in recent years.

Ms. Merkel's comments Sunday were an implicit rebuke of European Commission President José Manuel Barroso, who on Friday urged EU member states to agree to a standby-aid package of bilateral loans for Greece at this week's summit after Athens said last week that it might have to turn to the International Monetary Fund for help.

"There's no looming insolvency," Ms. Merkel said Sunday. "I don't believe that Greece has any acute financial needs from the European community, and that's what the Greek prime minister keeps telling me."

While Greek officials say they aren't asking for money, Prime Minister George Papandreou said last week he would like other European governments to put a money offer on the table so that financial markets can see that Greece has a safety net. That would allow Greece to borrow on bond markets at less-punitive interest rates, Mr. Papandreou argued. He warned that Greece will struggle to deliver promised deficit cuts if its borrowing costs remain unusually high and that it might have to seek help from the IMF if the euro zone remains aloof.

Mr. Barroso responded on Friday by saying that euro-zone governments should be ready to offer bilateral loans to Greece. He said that the situation couldn't be allowed to continue for much longer and that action was needed rapidly.

Ms. Merkel, whose approval is vital for any aid because of Germany's financial muscle, flatly rejected that assessment. "I don't see that Greece needs money at the moment, and the Greek government has confirmed that. That's why I'd urge us not to stir up turbulence in the markets by raising false expectations for Thursday's council meeting," she said. "I believe that as long as Greece doesn't need help this issue doesn't have to be at the forefront of our talks," she added. "Aid will not be on the agenda at the meeting on Thursday because Greece says itself it doesn't need help right now."

EU leaders are nevertheless expected to discuss the issue, with many countries keen to end the months of uncertainty surrounding Greece.

Ms. Merkel recognized that Greece's government is pressing the EU to make its contingency plans more explicit. "Greece would like to have a certain clarity for an eventuality it can't completely rule out," Ms. Merkel said. She added: "The best solution for the euro is for Greece to resolves its problems by itself—naturally with political support from European leaders."


European Pressphoto Agency

A taxi driver shouts slogans during a protest in Athens on Friday.

Greek woes dim the euro zone's appeal

By Brian Blackstone

FRANKFURT—The Greek debt crisis has upended expectations about the euro zone, causing the currency bloc to cast a more wary eye on potential additions—and leading some countries to question joining anytime soon.

Europe's leaders have long envisioned a currency region that would slowly expand to include all the formerly Communist countries on the European Union's eastern border. Such an expansion, they said, would allow the EU to realize the full benefit of its economic union.

Many countries on the doorstep of the 16-nation euro zone have battled deep recession and rising budget deficits in the wake of the financial crisis. Three have had to turn to the International Monetary Fund for help.

The candidate countries include Poland, along with the Baltic states, Czech Republic, Bulgaria, Hungary and Romania. As a condition of their EU membership, all are required to pursue euro adoption, though there is no deadline to join. The Baltics, which grew rapidly in the years before the financial crisis, were once expected to be quick additions but are now struggling. As recently as 18 months ago, Poland was aiming for the euro by 2011, but today optimists say it could be several years before the country adopts the euro.

The eastern countries' economies remain too fragile to be included in the common currency, even if they manage to meet the area's entrance requirements on debt and deficits, critics of rapid expansion say.

For the euro zone, the potential rewards of enlargement— but also the greatest uncertainty—lie in Poland. Poland's central bank Gov. Slawomir Skrzypek recently called the zloty "a very good shock absorber." Officials say joining the euro remains the goal, but they emphasize that economic overhauls must come first, a process that could take years. In addition, budget deficits and inflation, both of which are well above euro-entry limits, must be brought down.

Aided by strong exports, Poland's gross domestic product again bucked Europe's weak trend in the fourth quarter, growing at an annualized rate of 4.9%. The euro zone, by contrast, grew at a 0.4% pace last quarter.

"Unless we make far-reaching reforms in fiscal policy, labor and product markets...a rush into euro area seems to be hardly justified," says Pawel Kowalewski, who heads the central bank's euro-area integration office.

Popular support for accession in the candidate countries, meanwhile, has cooled. Four-tenths of respondents to a European Commission survey want the euro introduced in Poland as late as possible, more than double the share that wants it soon. In the Czech Republic almost 50% want to wait.

For some, Greece's troubles highlight the benefits of an independent currency outside the euro that can depreciate in bad times and boost exports. Still, for most countries, the promise of a stable currency, low interest rates and unfettered access to the world's second-largest market outweighs the cracks Greece has exposed.

Latvia, whose roughly 25% GDP decline since the crisis is among the worst in the world, remains undeterred in its desire for euro entry despite Greece's woes, for example, even as its pegged exchange rate forces painful drops in wages and prices.

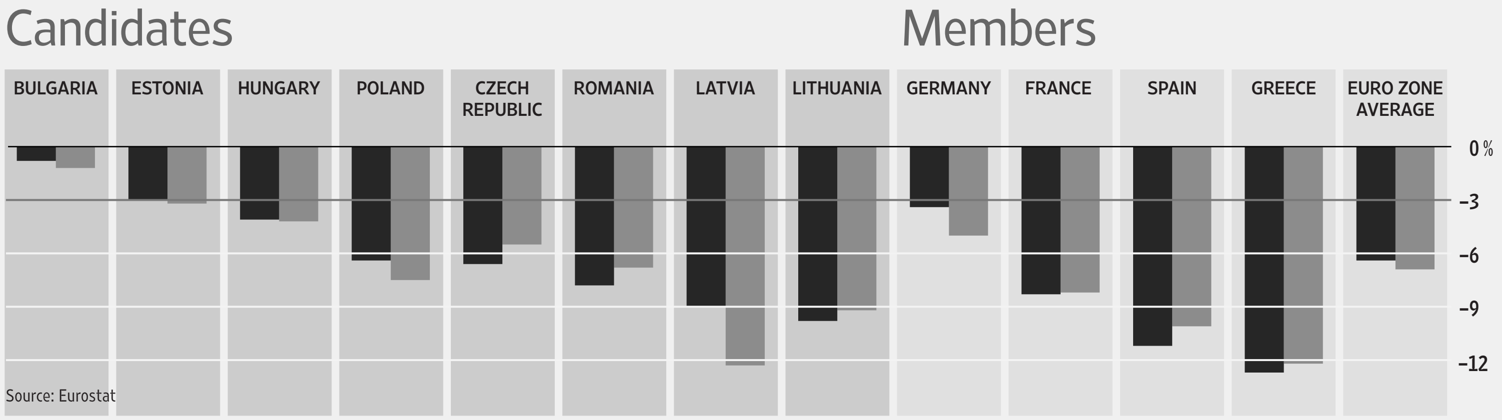
Government and central-bank officials say the lesson from Greece is that euro-zone membership alone can't erase a country's underlying structural problems, such as low productivity.

—Geoffrey T. Smith in Frankfurt contributed to this article.

Danger zone

Six of eight Eastern European candidates to join the euro zone—like many of the currency bloc's members—fail to meet its requirement of a deficit no more than 3% of GDP.

Deficit as a percentage of gross domestic product 2009 estimate 2010 forecast



Health-care vote at hand in House

Democrats push to secure support of wavering antiabortion lawmakers; Republicans say fight will continue

WASHINGTON—Democratic leaders raced Sunday afternoon to sew up final votes from antiabortion lawmakers with the hours ticking down to a historic vote on a health-care overhaul.

By **Janet Adamy, Greg Hitt** And **Siobhan Gorman**

An aide said leaders reached a deal with antiabortion Democrats that was likely to win votes from at least some of them. Rep. Bart Stupak (D., Mich.), the leader of the antiabortion bloc, said he was "close" to reaching a deal over an executive order that President Barack Obama would issue affirming that federal funds couldn't be used for abortions.

But he said there were "provisions in there that need to be strengthened" and added, "We've got work to do."

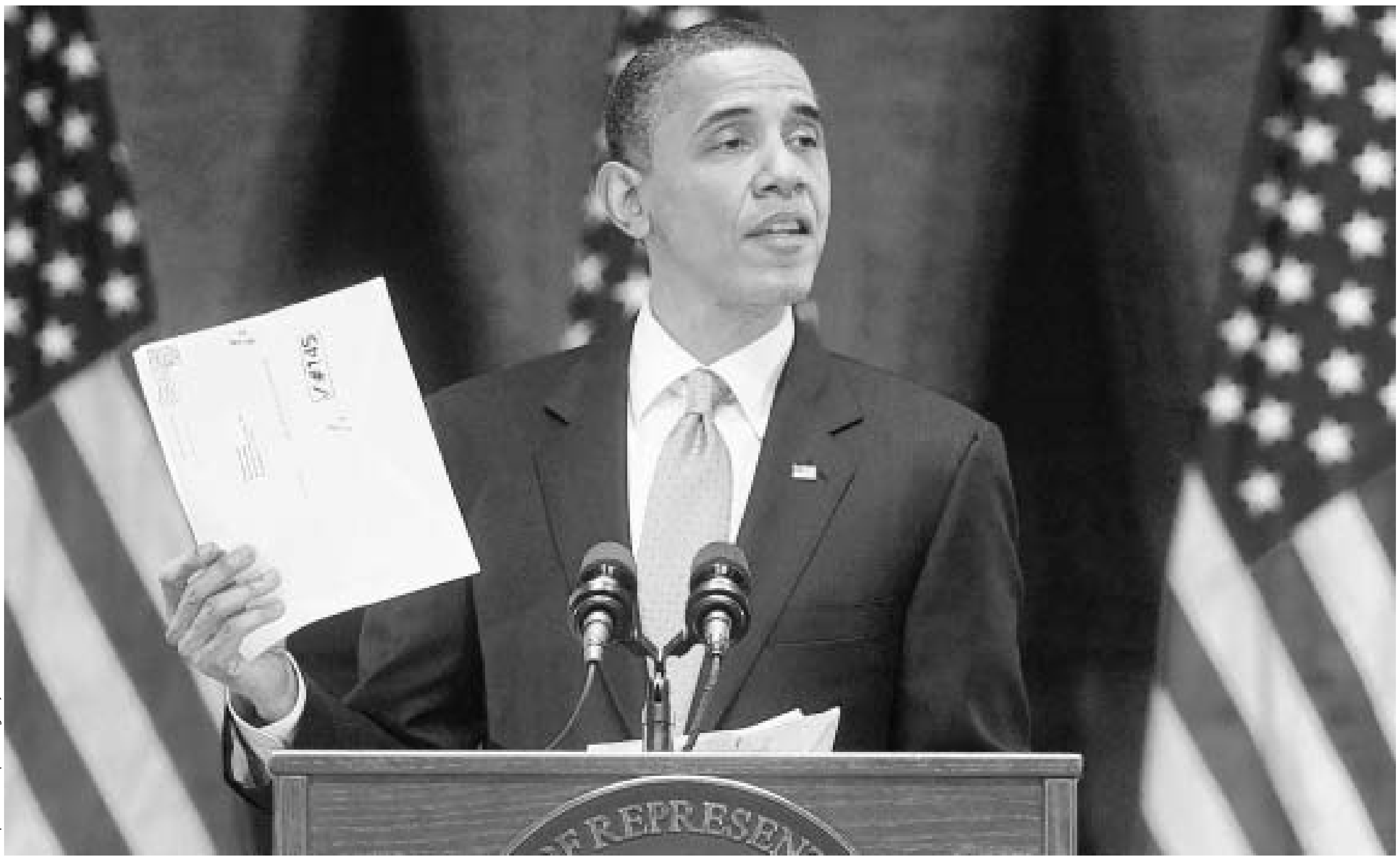
A top House Democrat said his party had rounded up enough votes to approve the bill later in the day. "We've got the votes," said Rep. John Larson (D., Conn.), the chairman of the House Democratic Caucus, speaking on CNN. He reiterated that assessment on ABC's "This Week."

But other leading Democrats cast some doubt on that assessment, saying the vote count was in flux and they were still rounding up votes. House Democrats' deputy vote-counter, Rep. Debbie Wasserman Schultz (D., Fla.), told "Fox News Sunday" that the count was "in flux." She added, "We don't have a hard 216 right now," referring to the number of votes required to approve the bill.

Some lawmakers remain on the fence over the pending vote, said House Majority Leader Steny Hoyer on Maryland, adding that the number of votes Democrats still needed to corral before the vote was in the "low single digits." He spoke on NBC's "Meet the Press."

The House planned to vote later Sunday on the bill to provide millions of Americans health-care coverage that has tied Congress in knots for nearly a year.

European Pressphoto Agency



President Barack Obama addresses the House Democratic Caucus on Saturday as part of efforts to unify the party behind the health-overhaul bill.

Republicans vowed a strong fight.

"We're going to use every means at our disposal to oppose this government takeover of health care," said Rep. Mike Pence (R., Ind.), speaking on CNN.

Rep. Marcy Kaptur, an antiabortion Democrat from Ohio, on Sunday said she would support the measure after receiving an assurance Saturday night from Mr. Obama and his top health official that existing abortion law would apply to the legislation.

At the White House, discussion was under way over issuing a statement later in the day that would promise an executive order on abortion. Even if a deal were reached, the executive order itself wasn't expected Sunday.

"The bill overall addresses a serious problem before the country today, which is that people are finding their current insurance plans unaffordable," Ms. Kaptur told a local television station.

The White House said the president was making and taking calls from members of Congress.

In advance of the final maneuvering, Mr. Obama spoke to House Democrats on Saturday afternoon, telling them they must take a tough vote to bring about a health overhaul that has eluded presidents for decades.

Democratic leaders put an end to a storm of Republican protest and agreed to hold separate votes on the two core elements of the package headed to the House floor Sunday: the sweeping bill that passed the Senate Dec. 24 and a smaller companion package making changes to that bill.

Earlier, House Democrats had talked of holding a vote only on the companion package and passing a rule deeming that to be a vote in favor of the larger Senate bill. The "deem-and-pass" tactic would allow Democrats to claim that they never voted for the larger bill, which has some unpopular elements, but Republicans denounced the idea as a parliamentary trick designed to let lawmakers off the hook for their votes.

The president addressed a House Democratic caucus that is nervous about possible major losses in November's midterm elections.

He stressed that the bill is designed to help Americans who have trouble finding affordable insurance, and countered Republican contentions that the bill represents a bid by the Democratic left wing to carry out a government takeover of health care.

Republicans said the U.S. can't afford the new spending in the bill, which is projected to cost $940 billion over a decade. The bill includes new taxes on health industries and the wealthy as well as curbs to the growth of Medicare spending.

The legislation is designed to extend health insurance to 32 million Americans now without coverage.

—Siobhan Hughes contributed to this article.

Big push to overhaul financial regulation

By Michael R. Crittenden

Administration officials are intensifying their appeals to overhaul U.S. financial regulation as the Senate Banking Committee prepares to take up Sen. Christopher Dodd's legislation on Monday.

Treasury Secretary Timothy Geithner is scheduled to deliver a speech at the American Enterprise Institute Monday afternoon, making the case for the legislation.

Federal Reserve Chairman Ben Bernanke joined the White House push for regulatory changes on Saturday, calling the existence of "too big to fail" financial firms "pernicious" and an "insidious" barrier to competition. "It is unconscionable that the fate of the world economy should be so closely tied to the fortunes of a relatively small number of giant financial firms," Mr. Bernanke said at the Independent Community Bankers of America conference in Orlando, Fla.

The existence of large, systemically risky firms skews competition in the financial-services industry, suggesting that the current marketplace "falls substantially short" when it comes to open competition, Mr. Bernanke said. "Having institutions that are too big to fail also creates competitive inequities that may prevent our most productive and innovative firms from prospering," he said.

Lawmakers are considering legislation to let the government wind down failing financial-services companies that are deemed to be systemically risky. Mr. Bernanke said having an agency to deal with large firms that get into trouble was key. "The resolution agency should not be allowed to protect shareholders and other capital providers, and it should have clear authority to impose losses on debt holders, override contracts, and replace managers and directors as appropriate," he said.

Bloomberg News

U.S. Fed chief Ben Bernanke at a community bankers' convention in Florida on Saturday criticized the existence of 'too big to fail' financial firms..

Among the ideas he suggested was a "living will" for systemically risky companies. Requiring companies to develop such a plan would give regulators a road map for winding down a company if stresses became too intense, Mr. Bernanke said.

Mr. Bernanke also continued the central bank's push to retain oversight of thousands of community banks. The legislation introduced last week by Mr. Dodd, the Connecticut Democrat, would shift much of the Fed's oversight of community banks to the Federal Deposit Insurance Corp. The Fed has responded by campaigning to retain its authority, and on Saturday Mr. Bernanke said the Fed "has always had a special relationship with community banks."

President Barack Obama used his weekly radio address Saturday to support the financial-regulation overhaul. He promised to use "every tool at my disposal to see these reforms enacted" and to ensure that changes serve the public interest, "not the special interests of Wall Street" seeking to preserve the status quo.

U.S. NEWS

Reuters

U.S, Secretary of State Hillary Clinton joins a wreath-laying ceremony at the Tomb of the Unknown Soldier in Moscow on Friday, the final day of a rocky visit to the Russian capital.

Nations decline to follow U.S.'s lead

Leaders from Brasilia to Beijing sling arrows at Obama administration; Americans deny opposition is growing

By Jay Solomon And Peter Spiegel

MOSCOW—A string of public rebukes of U.S. foreign policy in recent weeks, from Jerusalem to Red Square, is highlighting how the global goodwill President Barack Obama enjoyed on taking office last year has often failed to translate into foreign-policy wins.

U.S. Vice President Joe Biden's recent trip to Israel was poisoned upon touchdown with news that Israel will proceed with new settlements in East Jerusalem—a direct challenge to the peace process advocated by Washington.

Turkey, Brazil and China have in the past month each delivered timely snubs of Washington's push for sanctions against the Iranian regime. And earlier administration efforts to reach out to Tehran and "reset" sour relations with Russia ruffled feathers with usually reliable allies in Europe.

U.S. officials reject the idea that there is a growing wave of opposition to Mr. Obama's policies. "We have reset relations with a number of countries around the world, and this has opened the way for much more cooperation," says State Department spokesman P.J. Crowley. "Notwithstanding political posturing, our international cooperation has expanded greatly over the past year with many of these countries."

Many foreign diplomats say George W. Bush's administration faced a much more hostile reception in foreign capitals because of its prosecution of the Iraq war.

There have also been some notable advances for the Obama administration: Pakistani cooperation with the U.S. in the pursuit of terrorists is better than it has been in years, and the State Department is lauding its ties to the Kremlin.

On balance, however, U.S. diplomacy hasn't led the administration where it hoped to be.

Mr. Obama has made the forging of a comprehensive Arab-Israeli peace a cornerstone of his foreign-policy agenda. But Israeli Prime Minister Benjamin Netanyahu has continued to defy the White House's calls for a total freeze of settlement activity in lands jointly claimed by Israel and the Palestinians.

U.S. and Arab diplomats openly fear a breakdown in the Middle East peace process, which could stoke a new round of violence in the Palestinian territories. Amid the recent diplomatic dispute between the U.S. and Israel, Jerusalem saw its worst Palestinian street unrest in years.

White House diplomatic initiatives aimed at wooing adversaries such as Iran, Syria, and North Korea into renouncing their weapons systems and support of terrorism are also showing little signs of progress.

That leaves the U.S. heading into two key international conferences on nonproliferation this spring with the fear of the spread of atomic weapons rising.

Washington hopes the expected signing next month of a Strategic Arms Reduction Treaty with Moscow will reverse this trend. But U.S. officials say a failure to contain Iran's nuclear activities—which Tehran says are peaceful in nature but the U.S. says are military—could prove fatal to the Nuclear Nonproliferation Treaty, which aims to stop the spread of atomic weapons.

Both the promise and challenges of the Obama administration's approach were evident in Secretary of State Hillary Clinton's two-day trip to Russia last week. Mr. Putin surprised the U.S. delegation Thursday by announcing that Russia plans to help Iran launch its first nuclear reactor by July.

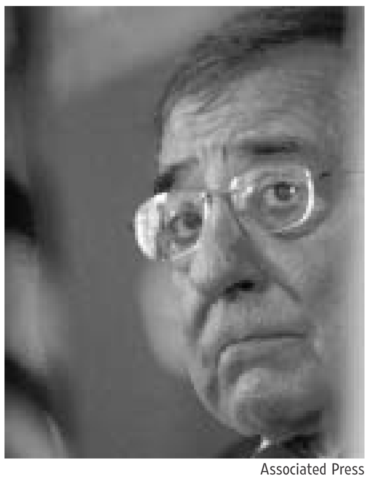
Mr. Putin's comments undercut Washington's message that increased financial pressure is needed on Tehran, and drew a quick rebuke from Mrs. Clinton.

International incidents

Some recent snubs to U.S. foreign policy

- **Feb. 25:** Syrian President Bashar Assad appears with Iran's Mahmoud Ahmadinejad and Hezbollah chief Hassan Nasrallah, defying U.S. calls to loosen ties with Tehran and the militants.
- **March 3:** President Luiz Inácio Lula da Silva of Brazil speaks against Iran sanctions during a visit by Hillary Clinton.
- **March 9:** Israel, during a visit by Vice President Joe Biden to promote the peace process, announces plan to build homes in disputed East Jerusalem.
- **March 14:** Chinese Premier Wen Jiabao calls U.S. currency policy 'trade protectionism' and says an Obama meeting with the Dalai Lama and U.S. arms sales to Taiwan 'violated China's territorial integrity.'
- **March 18:** Vladimir Putin, during a Clinton visit, says Russia will help Iran launch its first nuclear-power plant this summer.

Political skills aid U.S. spymaster



Associated Press

CIA Director Leon Panetta cites improvements with Pakistan..

By Siobhan Gorman

WASHINGTON—Intelligence reports landing on CIA Director Leon Panetta's desk last July made the alarming claim that the Pakistani Taliban could have a nuclear device.

Mr. Panetta soon called his Pakistani counterpart with an offer, according to a senior intelligence official. The Central Intelligence Agency would hunt down Pakistan's top terrorist target, but Mr. Panetta needed information on any nuclear threat. The nuclear threat didn't check out. But a month later, a CIA drone killed Pakistani Taliban chief Baitullah Mehsud.

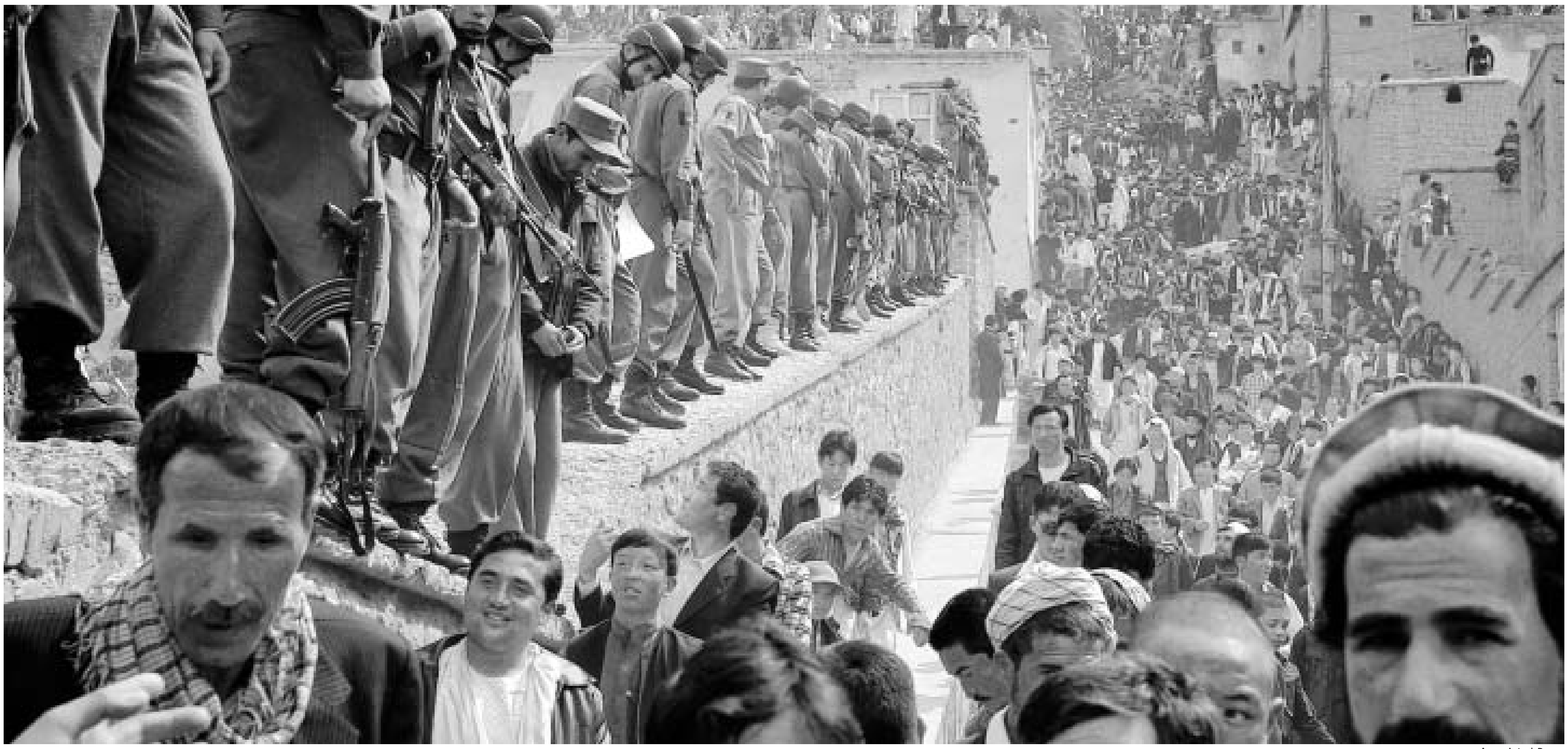
Since then, Pakistani information long sought by CIA headquarters at Langley, Va., has flowed with greater regularity, assisting a string of operations that have significantly weakened Osama bin Laden's al Qaeda terror network, intelligence officials said.

The 71-year-old Mr. Panetta, a former congressman and White House chief of staff under Bill Clinton, has brought to Langley a politician's focus on repairing strained relationships, especially with mercurial Pakistan. Pakistani and U.S. officials say it has paid off—notably with the capture of 20 al Qaeda and Taliban militants in recent months.

When Mr. Panetta was appointed by President Barack Obama to lead "The Agency" over a year ago, some lawmakers and CIA officers worried his political background would be a liability. But his experience forging relationships and cutting deals seems to be helping his evolution to spymaster.

After visiting Pakistan, Mr. Panetta made sure to keep in regular contact with the chief of Pakistan's Inter-Services Intelligence agency, Lt. Gen. Ahmed Shuja Pasha. Their relationship reached a turning point in August with the CIA's killing of Mr. Mehsud, believed to be responsible for the assassination of former Pakistani Prime Minister Benazir Bhutto. The U.S. had long been debating whether to go after Mr. Mehsud since he hadn't attacked the U.S. directly, said an official familiar with the debates. But the intelligence reports provided Mr. Panetta an opportunity to give the Pakistanis something they'd long sought: Mr. Mehsud's demise.

WORLD NEWS



Associated Press

Afghan policemen stand atop a wall as crowds of people pack a road during a celebration marking the start of spring and the traditional New Year in Afghanistan, Iran and other countries in central Asia.

Afghan militants pursue peace deal

Overture from group known as Hezb-i-Islami could weaken insurgency and prompt some Taliban to negotiate

By Yaroslav Trofimov

KABUL—Afghanistan's second-largest insurgent group after the Taliban said it sent a delegation to Kabul to negotiate a peace deal with the government and coalition forces, possibly marking the biggest split in insurgent ranks since the war began.

The five-member delegation of Hezb-i-Islami, a movement led by warlord Gulbuddin Hekmatyar, has already arrived in Kabul, said the group's spokesman Haroon Zarghoon, who is based in Pakistan. The delegates plan to meet President Hamid Karzai, U.S. officials and others "to discuss Hezb-i-Islami's agenda on how to bring durable peace to Afghanistan," Mr. Zarghoon told The Wall Street Journal.

As Hezb-i-Islami's representatives held meetings in Kabul, the Taliban fired a series of rockets against the city Sunday night, hitting the military side of Kabul's international airport and the capital's Pul-e-Charki district, U.S.-led international forces said. There were no immediate reports of casualties.

Though the Afghan insurgency is dominated by the Taliban and the affiliated Haqqani network, Mr. Hekmatyar's group boasts thousands of fighters and has carried out hundreds of attacks against coalition forces and Afghan troops.

A reconciliation between Hezb-i-Islami and the Kabul government won't end the eight-year-old war by itself. But, if achieved, it would weaken the insurgency—and likely prompt some senior Taliban commanders to cut their own deals with Mr. Karzai.

The former United Nations representative in Kabul, Kai Eide, has already discussed a possible settlement with Taliban representatives over the past several months—contacts that, he said, were interrupted by last month's arrest of the Taliban's second most senior official, Mullah Abdul Ghani Baradar.

U.S. Army Maj. Gen. Bill Mayville, the coalition forces' deputy chief of staff for operations, pointed out in a presentation released last week that the Taliban's recent statements may indicate "that some Taliban may be starting to consider participation in a coalition government as a possible resolution to the war."

Mr. Karzai himself has repeatedly reached out to insurgent leaders, seeking a peaceful solution to the conflict. A spokesman for Mr. Karzai, Ahmad Zia Herawi, said, however, that he was unaware of Hezb-i-Islami officials' visit to the Afghan capital. A spokesman for the U.S. Embassy in Kabul said that "the U.S. government is currently not in any meetings or discussions with the Taliban or Hekmatyar." A U.S. military official also said he didn't know about the delegation's arrival.

—Habib Zahori contributed to this article.

Afghan bombs are bigger

By Yochi J. Dreazen

WASHINGTON—Militants in Afghanistan are building bigger and bigger roadside bombs, eschewing the kinds of sophisticated munitions that were used in Iraq in favor of mammoth explosives capable of destroying any U.S. armored vehicle.

Improvised explosive devices, or IEDs, have become the signature weapon of the Afghan war, as they were in Iraq. The number of IED attacks in Afghanistan rose to more than 8,000 last year from 2,677 in 2007. They are the single biggest killer of U.S. and North Atlantic Treaty Organization troops, accounting for 275 of the 449 coalition fatalities in Afghanistan in 2009. So far this year, Afghan IEDs have killed 68 NATO troops.

U.S. commanders expect IED casualties to rise as the new forces in the U.S. troop surge move deeper into southern and eastern Afghanistan, areas with the highest concentrations of roadside bombs.

The U.S. is devoting billions of dollars to find better ways of protecting its troops from IEDs, including a crash effort to buy thousands of specially configured armored vehicles capable of driving on Afghanistan's unpaved roads. The Pentagon spent more than $30 billion buying an earlier model of the IED-resistant trucks, only to discover that they were largely useless in Afghanistan because of its harsh terrain.

The Afghan IEDs are at least twice as large as bombs seen in Iraq; some contain hundreds of kilos of homemade explosives. Bombs that size are virtually guaranteed to cause injuries or deaths.

"A large quantity of explosives takes on a physics of its own," said Army Lt. Gen. Michael Oates, who runs the command devoted to studying and countering IEDs. "When you put enough munitions beneath the vehicle, you can essentially defeat any vehicle that's in our inventory and probably anything that we could design."

Militants continue to make bigger bombs. Maj. Gen. Michael Flynn, the top U.S. intelligence officer in Afghanistan, said in a recent PowerPoint presentation that in May 2008 less than half of all IEDs in Afghanistan used 25 pounds (11.4 kilograms) or more of explosives. By November of last year, three-quarters of the bombs were that big.

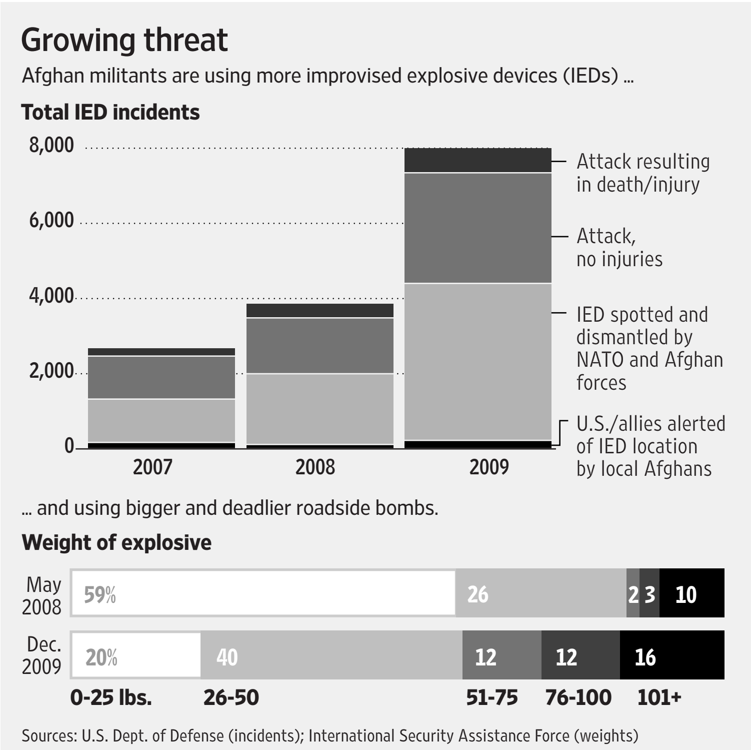
The dangers posed by the large IEDs were driven home to many in the military by a roadside bombing in southern Afghanistan in October that wiped out an entire squad of soldiers from the 5th Brigade of the Army's 2nd Infantry Division.

Military explosives experts who did a forensic examination of the blast site later estimated the IED was one of the largest makeshift bombs seen in either Iraq or Afghanistan.

IEDs were the main killer of U.S. troops in Iraq as well, but the bombs there were very different. In Iraq, insurgents used technological innovations, from radio-controlled bombs triggered by cellphones or garage-door openers.

The Afghan IEDs are set off with simple "pressure plates" that detonate the IEDs as soon as a vehicle drives on top of them.

American military officials say the Taliban are constantly recalibrating their tactics in response to new U.S. defensive measures.



The government of Afghan President Hamid Karzai issued a decree this year banning the use, production, storage or sale of ammonium nitrate.

U.S. commanders are cautiously optimistic the ban will eventually make it harder for militants in the south to build new IEDs.

Iraq commission rejects recount

Close vote could unseat incumbent premier

By Margaret Coker

BAGHDAD—Iraq's electoral commission brushed aside increased pressure from Prime Minister Nouri al-Maliki and other politicians demanding a recount in the close parliamentary race that could unseat the incumbent leader and other officials who have dominated Iraq's transition to democracy.

The March 7 vote to elect the 325-member parliament proceeded smoothly, with minimal violence, but Iraq's leading political parties are increasingly agitated over the uncertain outcome. Partial results released so far make it impossible to tell whether Mr. Maliki's alliance or the bloc led by his closest challenger, former Premier Ayad Allawi, will win the most seats and thus the chance to form the next government. At least one-third of current members of parliament are in danger of losing their seats.

Amid a slow and confusing counting process, politicians from across the spectrum have flooded local airwaves leveling vague accusations of fraud. On Saturday Mr. Maliki joined the fray. In a statement, he called on the electoral commission to instigate a manual recount of the ballots "to preserve the political stability and avoid the deterioration of security."

In the run-up to the elections, Mr. Maliki's challengers accused him of abusing his power after security forces under his direct command launched a wave of arrests among competing political leaders. The prime minister also intervened in a controversial decision to ban hundreds of candidates from the race for alleged ties to Saddam Hussein's former party, a decision seen as adversely affecting Mr. Allawi's slate.

Faraj Al Haidari, head of Iraq's independent election commission, rejected Mr. Maliki's demands, which were echoed Sunday by Iraq's ceremonial president. In a televised news conference, Mr. Haidari reiterated that no evidence existed that would necessitate a recount.

"It is not possible that a political entity, which believes there might have been a mistake at a particular polling station, can demand a manual recount for an entire city or for the whole of Iraq," said Mr. Haidari.

Western diplomats and election observers agree that the vote was free and fair. U.S. State Department spokesman P.J. Crowley said the Iraqis have established procedures to work through electoral questions.

Associated Press

Faraj Al Haidari, chairman of Iraq's independent election commission, on Sunday rejected calls for a recount.

Partial results show Mr. Maliki's political coalition in the lead in seven of Iraq's 18 provinces, with Mr. Allawi's bloc leading in five. However, in Iraq's complex system of proportional representation, winning the most populous provinces could prove more favorable than winning smaller provinces, which control fewer seats. By that measurement, Mr. Maliki and Mr. Allawi appear to be in a dead heat.

There has been an intense backlash by voters against many incumbents. Leading Shiite clerics turned politicians and some close allies of the U.S. coalition authority here appear to have received too few votes to keep their seats. The March election, the second national vote since the fall of Saddam Hussein, is being closely watched as a barometer of Iraq's path to stability and democracy ahead of the planned U.S. troop withdrawal this summer.

Obama, Netanyahu to meet on Tuesday

U.S. President Barack Obama and Israeli Prime Minister Benjamin Netanyahu will meet Tuesday in a bid to quell a diplomat row that has left the U.S.-Israeli relationship at its lowest point in decades.

*By **Charles Levinson** in Jerusalem and **Jay Solomon** in Washington*

Mr. Netanyahu paved the way for White House visit, said U.S. and Israeli officials, by offering Washington a series of concessions aimed at underpinning a Middle East peace process that Mr. Obama has placed at the center of his foreign-policy agenda.

Specifically, Mr. Netanyahu agreed that the indirect peace negotiations with the Palestinians the U.S. is brokering could deal with the conflict's core issues, such as borders, refugees, and the status of Jerusalem, said government spokesman Mark Regev. Previously, Israel had insisted indirect talks would only address procedural issues.

Mr. Netanyahu also pledged to take steps to strengthen the political position of Palestinian Authority President Mahmoud Abbas, Israel's principal partner in any future peace talks. Israeli security forces will begin easing a blockade of the Gaza Strip, said Israeli officials, as well as release some prisoners from Mr. Abbas's Fatah Party.

Still, Mr. Netanyahu appeared unwilling to back down on the issue that sparked his government's current diplomatic standoff with Washington: Israeli construction in disputed East Jerusalem.

Two weeks ago, during a visit by U.S. Vice President Joe Biden, Israel's Interior Ministry announced the building of 1,600 new Jewish homes in an East Jerusalem neighborhood. The White House said it viewed the announcement as direct challenge to U.S. foreign-policy interests, and Secretary of State Hillary Clinton called Mr. Netanyahu and demanded a cessation of the construction, according to U.S. officials.

"Our policy on Jerusalem is the same policy followed by all Israeli governments for the 42 years, and it has not changed," Mr. Netanyahu said Sunday at his weekly cabinet meeting. "As far as we are concerned, building in Jerusalem is the same as building in Tel Aviv."

Mr. Netanyahu did, however, pledge to put in place mechanisms to ensure that there would be no more embarrassingly timed announcements about building projects in East Jerusalem, according to Israeli officials.

U.S. officials Sunday appeared pleased with Mr. Netanyahu's concessions and backed off earlier suggestions that the Israeli leader might not get a meeting with Mr. Obama.

Still, it is uncertain if Mr. Netanyahu's concessions will be enough to revive the peace process. A spokesman for Mr. Abbas said the Palestinian leader will meet Monday with U.S. envoy George Mitchell and decide then what steps to take.