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THE WALL STREET JOURNAL.

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European Pressphoto Agency

Chancellor of the Exchequer George Osborne, left, and U.S. Treasury Secretary Timothy Geithner presented themselves as natural allies as Mr. Geithner outlined his agenda for Europe.

Geithner says Europe needs stimulus still

By Bob Davis
And Ian Talley

LONDON—U.S. Treasury Secretary Timothy Geithner told Europe Wednesday that "markets want to see action; they want to see governments come together and act."

His words reflected greater self-assurance from U.S. policy makers about what Europe should do next as the continent's debt woes deepen. Mr. Geithner was most explicit as to what Europe should do in response to how much fiscal support European governments should supply amid anemic economic growth and what form financial regulations should take across borders.

The U.S. advice to Europe starts with encouraging countries that can afford it to keep pumping stimulus into their economies—U.K., Germany, France—as a way to make sure there is sufficient demand to keep the European economy expanding while economically troubled countries like Spain and Greece make wrenching cutbacks to reduce out-of-control deficits.

The turnaround from late 2008, when Asian and Europeans blamed the U.S. for dumping the world in recession, was on display on Wednesday at 11 Downing Street, home of Britain's new treasurer.

Mr. Geithner's comments about markets wanting action weren't directed at his British counterpart, George Osborne, whom he clearly viewed as an ally. Rather, he was focusing on a continental European audience, especially Germany, where Mr. Geithner stops on Thursday after starting his trip in China.

He is likely to push the Germans to rethink their ban on short selling certain financial instruments, which caught European and U.S. officials off-guard. (See related article on page 6.) Messrs. Geithner and Osborne said they agreed on the need for fiscal stimulus to keep economies growing for now and for broad financial regulation.

"There is a broader challenge to Europe on where is the growth going to come from" over the coming years, Mr. Osborne said, as so many heavily indebted European countries ratchet back their spending.

The Organization for Economic Cooperation and Development said in its latest global economic outlook Wednesday that the euro-zone economy should grow by something like 1.2% this year, compared with 3.2% growth in the U.S. But "there is considerable uncertainty about the strength and pace of the recovery," the multinational think tank said.

Mr. Geithner has been concerned that continental European countries were late to recognize the debt problems

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Apple, H-P to investigate Hon Hai over suicides

Amid a furor over suicides at a major supplier, **Apple** Inc., **Hewlett-Packard** Co. and other electronics companies said they are examining conditions at the Chinese factory and how the supplier has responded to the spate of workers' deaths.

By Jason Dean in Beijing and Ting-I Tsai in Taipei

The suicides at **Hon Hai Precision Industry** Co., which assembles iPads for Apple, computers for H-P and cellphones for **Nokia** Corp., have put unprecedented scrutiny on the secretive company and have highlighted the changing nature of China's manufacturing work force.

Reuters

Workers at a Hon Hai factory

The tech companies' promises to investigate came before another Hon Hai worker died Wednesday night in an apparent suicide attempt and as the company's hard-charging chairman, Terry Gou, moved to contain the widening fallout.

Wednesday's incident, reported by state-run Xinhua news agency, marks the tenth time an employee at Hon Hai's sprawling Longhua complex in the southern city of Shenzhen has plunged to their death this year, most since April, with two more injured in failed attempts.

Given China's overall suicide rate—about 14 per 100,000 people—the deaths

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Uncle Sam wants you to bid for this fine pair of ostrich-skin boots. Page 33

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PAGE TWO

Innovation, innovation, innovation

[Agenda]

By William Lyons

On Friday, consumers across Europe will finally be able to get their hands on **Apple**'s long-awaited iPad. The 9.7-inch touch-screen device allows users to play games, listen to music, check emails and even read newspapers. Gadgets such as the iPod and iPhone have helped Apple post record earnings, and the next chapter in its redefinition of the multimedia landscape promises to be as lucrative as the last. Sales of iPads are forecast to add about $1 billion of revenue to the company's coffers next quarter.

Apple already has secured a reputation for extraordinary innovatio,n but in reality much of its success lay not in traditional Research and Development (R&D) but in fields such as complex system integration, design, marketing and integrating the hardware it created with the software it assembled. In the case of the iPod, Apple was hugely successful in persuading the music industry, in particular the big record labels, to allow them to put their songs in the iTunes music store.

Apple is one of a swath of companies including **Amazon.com** Inc and **easyJet** that in recent years have pioneered a growth strategy based on smart innovation. They have harnessed and ruthlessly exploited often-intangible factors such as design, marketing, supply-chain sales and organizational capital. In short, they have redefined their respective marketplaces without actually inventing anything new.

It might have an application in a public sector that is about to be squeezed by spending cuts. The stories of Apple and Amazon ought to be studied by European governments looking to foster innovation and strengthen growth. As policy makers look for ways to recover from the impact of the economic crisis and cut deficits, innovation should be at the forefront of every European finance minister's mind. How can better services be delivered for less?

Bloomberg News

A concierge uses an iPad to help direct a guest at a London hotel on Tuesday.

The Organization for Economic Cooperation and Development has been examining such questions for several years. It will attempt to provide some answers when Secretary-General Angel Gurría unveils its blueprint for Innovation Strategy in Paris on Thursday.

Apple and Amazon ought to be studied by governments looking to foster innovation and strengthen growth.

The OECD will attempt to explain what government can do to help accelerate innovation-led growth in the private sector. This will include a compendium of indicators followed by a policy handbook. It will draw on the Oslo Manual for innovation that the OECD began working on in 1996 and that was last updated in 2005. This in turn is a descendent of the Frascati Manual, which for the past 40 years has measured international comparisons of the resources each country devotes to R&D.

Historically, expenditure on R&D was seen as the principle measure of innovation. But Thursday's OECD report will argue that governments grappling with the question of how best to funnel investment and resources into creating inventions and sound businesses will have to look more broadly than traditional R&D.

"It as though there has been an R&D fetish," one of the report's contributors told me. Since 2000, Europe has set an objective to make R&D expenditure 3% of gross domestic product by 2010. It is known as the "Lisbon target" because it was set at a meeting of the European Council in the Portuguese capital, and EU states are on course to miss the deadline.

While the report certainly does not call for an end to R&D spend (it argues that it remains vitally important), it points out that many highly innovative firms don't engage in R&D at all. Increasingly, firms in services and manufacturing create value through a wide range of complementary technological and non-technological changes and innovations.

Nespresso is a compelling example. The coffee maker, which has built its success on the sale of capsules of espresso that are made for stylish coffee machines, is **Nestlé**'s fastest-growing business. Much of its growth lies in the success of its marketing, its online presence, retail outlets, design and its simplicity and ease of use. The original R&D was undertaken by Nestlé long ago—in the 1970s.

Andrew Wyckoff, director of the directorate for Science, Technology and Industry at the OECD, argues that servicing the needs of the consumer in the here and now is what matters.

"There has been a tendency for a lot of government policy in the innovation sphere to focus primarily on the supply side," he says. "But what we are seeing through examples such as the iPod and Nespresso is that appealing to consumers, having consumers understand your product is equally important.

"While R&D and having highly trained capital such as scientist and engineers is important it is also vital to look at innovation as a system where the demand is also a key factor."

Against this background, European ministers will attempt to frame new policies to promote growth.

The OECD calls for the cutting of red tape, reform of universities to give them greater independence and the opening up of access to more public research data from mapping the human genome to weather maps. The aim: to encourage entrepreneurship.

Entrepreneurial spirit and human ingenuity are the backbone of innovation. As global players such as China, Brazil and India grow their economies rapidly, the question for Europe is how it keeps up.

Of course there should not be an end to the funding of scientific R&D. But the OECD's findings suggest that a change is required in how governments and more European companies think about innovation. When Sir Stelios Haji-Ioannou redefined the low-cost aviation model in Europe with easyJet, he did so not by creating a product in a laboratory but by listening to the consumers and providing them with a service they couldn't refuse.

What's News

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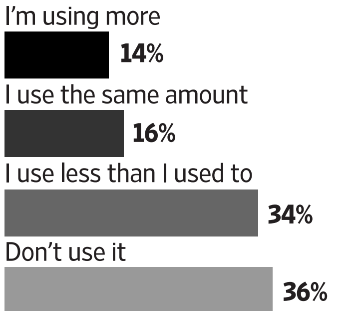

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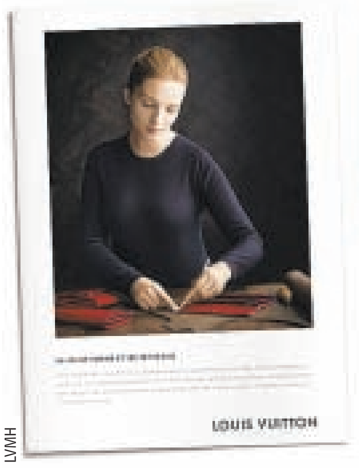
NEWS

Louis Vuitton ads called misleading

U.K. regulator says the artisan pitches implied products were handmade, when machines do some of the work

By Christina Passariello

Bad pitch | Ads that have run into trouble with regulators and the public



LVMH

Louis Vuitton (May 2010)

U.K. Advertising Standards Authority said campaign misleadingly implied the bags were stitched by hand. The text read: "infinite patience protects each overstitch."

ASA

Danone (2009)

Claim that Actimel was "scientifically proven to help support your kids' defenses" was found to be misleading by ASA .

Agence France-Presse

Dolce & Gabbana (2007)

Print ad showing a bare-chested man holding down a woman was withdrawn amid heavy criticism.

ASA

L'Oreal (2007)

A TV and press ad for L'Oreal mascara claiming "up to 60% longer lashes" was found misleading by ASA as actress Penelope Cruz wore fake eyelashes.

Source: Advertising Standards Authority

PARIS—The U.K.'s Advertising Standards Authority Wednesday banned two Louis Vuitton print ads that it says could dupe consumers to believe its products are handmade, when in fact the luxury brand also uses machines.

In the ads, artisans fold the leather of a wallet and hand-stitch the handle of a handbag. "What secret little gestures do our craftsmen discreetly pass on?" an ad asks. "Let's allow these mysteries to hang in the air. Time will provide the answers."

The authority, which investigates complaints from the public, said the two Vuitton ads breached its truthfulness code and were "misleading." "We considered that consumers would interpret the image of a woman using a needle and thread to stitch the handle of a bag ... to mean that Louis Vuitton bags were hand stitched," the agency said in its ruling.

Vuitton must pull the print campaign, produced by **WPP** PLC's Ogilvy & Mather and launched world-wide in November. A third ad from the campaign, in which a man paints the sole of a shoe, didn't draw objections and wasn't reviewed, an ASA spokesman said.

Vuitton, part of LVMH Moët Hennessy Louis Vuitton, said it complied with the authority's requests to clarify its manufacturing process. "This decision is not about the truth of the claim—but whether there was sufficient documentation available to prove to the ASA the 'extent to which LV products are made by hand,'" the company said in a statement. The campaign ended its run several weeks ago, the company added.

Luxury brands' emphasis on history and authenticity is an advertising trend that has emerged in the post-economic-crisis period. Italian fashion house Gucci, part of France's **PPR** SA, launched a "Forever Now" print campaign in February, which uses black-and-white photographs taken in its Florence workshop in 1953. Consumers have been favoring labels with deep roots and a rich heritage—Vuitton, Gucci, Hermès—because they're seen as more enduring than newer brands., experts say

Vuitton factories in France, Spain and the U.S. are a model for modern luxury-goods industrial production—essential for a brand with an estimated $6.17 billion (€5 billion) in sales. Yet the Vuitton ads, evokes paintings from the Dutch masters, with a dark setting, soft light illuminating the craftsmen,with titles such as "The Seamstress with Linen Thread and Beeswax," mimic Johannes Vermeer, who painted "Girl with the Pearl Earring."

Vuitton moved away from traditional fashion advertising three years ago when it launched its "Core Values" campaign focusing on the label's travel heritage. Vuitton's fashion ads continue to feature its latest runway collection.

The British advertising authority said it received three complaints about the two Vuitton ads.

During four months of discussions with the authority, Vuitton provided step-by-step guides about the manufacturing of some of its goods and the use of sewing machines. However, Vuitton didn't detail what proportion of the process was done by hand or by machine, the authority said, leading it to conclude the ads were misleading.

■ Hermès parts ways with designer Jean-Paul Gaultier 21

Apple, H-P to probe Hon Hai after suicides

Continued from first page

aren't statistically exceptional, but the quick succession is unusual.

Earlier Wednesday, the company gave a tour of Longhua, a walled-off complex with guarded gates and about 400,000 workers, to a group of journalists, and announced plans to outfit worker dormitories with safety nets to prevent more workers from jumping to their deaths.

"These last two months, I've been afraid to answer the phone late at night or early in the morning, because we've been unable to prevent these incidents from happening," the 59-year-old Mr. Gou told reporters at Longhua, which has dozens of factory buildings and dormitories. He expressed "regret" over the incidents, but defended Hon Hai's response. "We need time. But we have confidence and strong determination" to address the issue, he said.

The statements Wednesday from Apple, H-P and others were the first public comment on the suicides by customers of Hon Hai, which also goes by the trade name Foxconn. The Taiwan-based company, employs some 820,000 workers throughout China, is the world's largest electronics contract manufacturer by revenue.

"We are saddened and upset by the recent suicides at Foxconn," Apple said, adding it had assigned a team to evaluate Hon Hai's efforts to address the suicides. The Cupertino, Calif., company said it is in contact with Hon Hai's senior management and "we believe they are taking this matter very seriously."

Agence France-Presse/Getty Images

Workers walk past the Foxconn plant in Shenzhen on Wednesday.

H-P, the world's biggest maker of PCs, said it "is investigating the Foxconn practices that may be associated with these tragic events." Nokia said "we have contacted Foxconn to ensure any issues are identified and addressed."

The deaths at Hon Hai have defied simple explanation. Their pattern resembles what psychologists call a "suicide cluster," where one suicide triggers copycats—often in schools or groups of young people.

Other companies have experienced suicide waves. **France Télécom** SA, which has around 180,000 staffers, has been under scrutiny after 35 suicides in 2008 and 2009, and another 13 this year.

Amid widening public concern, Chinese government officials have said they are looking into the deaths at Hon Hai. But so far authorities have suggested no wrongdoing by the company.

Labor rights activists say the deaths demonstrate problems with the way Hon Hai treats its staff. Workers are paid a base salary of 900 yuan a month, or about $132, the legal minimum wage, but most work overtime, which can pay 1.5 times or more the standard hourly rate. Critics say Hon Hai compels or allows employees to work more than the legal number of overtime hours, and that its military-style rigor and repetitive working conditions create excessive stress on workers.

Still, the labor activists say Hon Hai's conditions are better than those at many factories in China, and that conditions have been improving in recent years.

Hon Hai says its compensation and overtime practices follow local labor laws and the guidelines of the Electronic Industry Citizenship Coalition, a group that promotes a code of conduct for international supply chains. The company has launched a series of antisuicide measures, from establishing a suicide hotline to hiring academic experts and counselors to inviting a group of Buddhist monks to pray for the factory.

Li Qiang, executive director of China Labor Watch, a New York-based group, says another problem is that Hon Hai's Longhua plant has simply become too large. "These young workers feel like there's no one caring for them," he says. Hon Hai's methods have failed to keep up with changes among the migrant workers who staff coastal factories like Longhua, he says.

Mr. Li and other Chinese scholars and labor experts say workers from earlier generations, who hailed mainly from poor farms in China's hinterland, were accustomed to hard farm work and more single-mindedly focused on making money. Today's young workers are less firmly rooted and more aware of the chasm that separates their own arduous lives from the wealth and comfort of others in Chinese society.

After 19-year-old Li Hai jumped to his death Tuesday from a fifth-floor window of a training center, police found a suicide note apologizing to his family. The note indicated that Mr. Li had "lost confidence in his future," and that "his expectations of what he could do at work and for his family far outweighed what could be achieved," Xinhua reported.

While labor activists refer to Longhua as a sweatshop, it hardly has the look of Dickensian squalor the term connotes. On Wednesday, thousands of workers walked the tree-lined streets in colored uniforms bearing identification badges, while others ate in canteens boasting different regional cuisines.

The factory has a hospital and a bookstore amid the countless, squat factory buildings. A banner advertised a company karaoke contest. Liu Risheng, a 22-year-old employee who stood outside a cafeteria smoking a cigarette, said the pressure was manageable. "People complain from time to time," he said, but "it doesn't affect me much."

—Juliet Ye and Nan Wu in Shenzhen, China, Bai Lin in Shanghai and Justin Scheck in San Francisco contributed to this article.

EUROPE NEWS

Risk of stalemate after Czech vote

Key reforms, budget-cutting could be delayed if parliamentary elections fail to produce a clear winner

By Sean Carney
And Leos Rousek

PRAGUE—Friday's elections for the lower house of the Czech parliament are unlikely to produce an outright winner, ushering in a period of coalition-building and horse-trading that will probably delay—and may even halt—much-needed economic reforms, such as cutting the government's deficit and overhauling the state-funded pension system.

Recent polls show neither of the two major parties, the conservative Civic Democratic Party, or ODS, and the left-of-center Social Democrats, or CSSD, anywhere near a gaining a majority of the chamber's 200 seats.

This means new, smaller parties, gaining support from voter disgust with big parties' inability to root out alleged political corruption in rigged public procurement contracts, may play a key role in the formation of a new government. Such a scenario appeared possible as the final pre-election poll from the Factum Invenio agency, published Monday, showed an increased preference for the smaller, center-right parties. That suggested a center-right parliamentary majority, together with the Civic Democrats, is possible.

"I'm particularly afraid of what happened four years ago repeating; a stalemate and inability to form a government in time to draw up [the 2011] budget," said Raiffeisenbank chief economist and former finance minister Pavel Mertlik.

It took seven months to assemble a government after the last election in 2006.

If the government doesn't have a draft 2011 budget ready by late summer, it means spending cuts, needed to lower the deficit from about 5.5% of gross domestic product this year to just above 4% next year, could be delayed or fall by the wayside at a time when, for the first time, fiscal responsibility is an election issue.

Several opinion polls show the Social Democrats, champions of the welfare state, with most support, at about 30%. The party has put reform of the loss-making pension system on the back burner and instead seeks to raise taxes and increase social spending.

The Civic Democrats, trailing with roughly 20% of voter support, are calling for no new taxes, cuts in government spending, increased fees at state-run medical facilities and lower social spending.

Much of the remaining electorate is likely to vote for two new parties. The fiscal-responsibility-focused TOP 09, has between 10% and 14% of likely voter support, closely followed by the Public Issues Political Party, or VV. That party focuses on combating alleged government corruption, perhaps the biggest issue in the election after deficit reduction and pension reform.

According to the Czech Association of Small and Medium-sized Enterprises and Crafts, or AMSP, bribes account for 15% of the value of all public contracts awarded by local Czech government offices and agencies. In 2009 some $29 billion of public contracts were awarded by state institutions in the Czech Republic.

Both TOP 09 and VV are centrists, and given an option to partner with the Social Democrats or Civic Democrats, they are most likely to move to the right, as both new parties are vehemently opposed to joining a government that relies on the support of the far-left Czech Communists, which garner about 13% of likely voter preference.

The final party that could swing the balance are the centrist Christian Democrats which will likely get about 5% of the vote. This is right on the threshold to get into parliament. If they do get seats, they could go either way, although they've also said they won't join a coalition that requires Communist support.

Reuters

A pre-election poster in Prague last week pictures ODS leader Petr Necas, left, and CSSD leader Jiri Paroubek.

Hungary law irks Slovakia

*By **Leos Rousek** in Prague and **Veronika Gulyas** in Budapest*

Hungary's new conservative-dominated parliament passed a law making it easier for ethnic Hungarians living in other countries to become citizens, prompting neighboring Slovakia to tighten its own citizenship legislation in retaliation—underlining the continuing power of ethnic divisions to roil regional politics.

The Hungarian law, passed Wednesday in fulfillment of a campaign pledge by the center-right Fidesz party, which won a landslide in April elections, would allow nearly three million Hungarians in neighboring countries to become Hungarian citizens without requiring them to live in Hungary.

Lawmakers in Slovakia, where ethnic Hungarians account for roughly 10% of the country's population of 5.4 million people, responded by amending their own citizenship statute to say that any Slovak who accepts the citizenship of another country would lose his or her Slovak citizenship.

Significant Hungarian populations also live in Romania and Serbia, a legacy of the post-World War I division of the Austro-Hungarian empire that left large numbers of ethnic Hungarians outside the borders of modern-day Hungary.

Analysts predicted that Hungary's move would raise fewer hackles in Serbia, where the ethnic Hungarian population is proportionately smaller, and Romania, where most Hungarians live in the center of the country and are unlikely to seek Hungarian citizenship.

In Slovakia, however, where the sizable Hungarian population is concentrated along the border with Hungary, a coming national election has helped fan the political flames. Politicians are appealing to Slovak's patriotic impulses in what has turned into a close race between right- and left-leaning parties.

Many Slovak politicians say they see the idea of dual citizenship for its large ethnic Hungarian minority as an attack on the small nation's sovereignty.

The new Hungarian law also stokes deep-seated memories of Hungarians' rule over today's Slovakia in the days of the Hapsburg empire. Slovakia became independent following a peaceful division of Czechoslovakia in 1993.

There are equally strong feelings in Hungary, where people still talk about what they consider the unfair treatment of their homeland after World War I.

"I support the government's notion of dual citizenship, as I believe Hungarians, wherever they live in the world, shouldn't be forced to keep their nationality a secret," said Jozsef Erdos, 43 years old, a taxi driver and martial-arts instructor.

"Unlike in Slovakia, the dual-citizenship law isn't likely to become too hot an issue for Romania and Serbia," said Filip Tesar, a researcher on Balkan issues at the Prague-based Institute for International Relations.

European Pressphoto Agency

Hungarian Prime Minister-elect Viktor Orbán, left, after the citizenship vote.

Europe's fiscal woe buffets drug agency

By Jeanne Whalen

Europe's fiscal troubles will probably lead to cuts in the European Medicines Agency's budget, the head of the EMA said in an interview on Wednesday, adding that the drug-review body will probably have to charge pharmaceutical companies more for its services as a result.

The EMA — Europe's equivalent of the U.S. Food and Drug Administration — already gets about 80% of its €217 million ($265 million) annual budget from companies that pay fees to have their products reviewed for marketing approval. The remaining 20% comes from the European Commission.

The EMA is currently negotiating with the Commission for its 2011 budget and there are signs the Commission could cut its contribution by about €10 million, Thomas Lönngren said in an interview.

"The whole issue of the budget situation in the European Union will of course affect the European Commission and European institutions," he said. "It's the member states who are paying into the pocket of the European Union and of course when member states are getting into trouble ... the whole system has to contribute in some way."

A spokesman for the European Commission said he believed the EMA's budget would be "roughly the same" in 2011, but that the budget isn't finalized yet.

Mr. Lönngren said he has already "alluded to" the issue in conversations with drug companies, warning them that their fees could rise. He said he didn't feel that increased industry funding would hurt the EMA's independence.

"We are already financed by fees," he said, calling the EMA's decisions "totally independent" of industry. The FDA is also partly financed by drug-company fees.

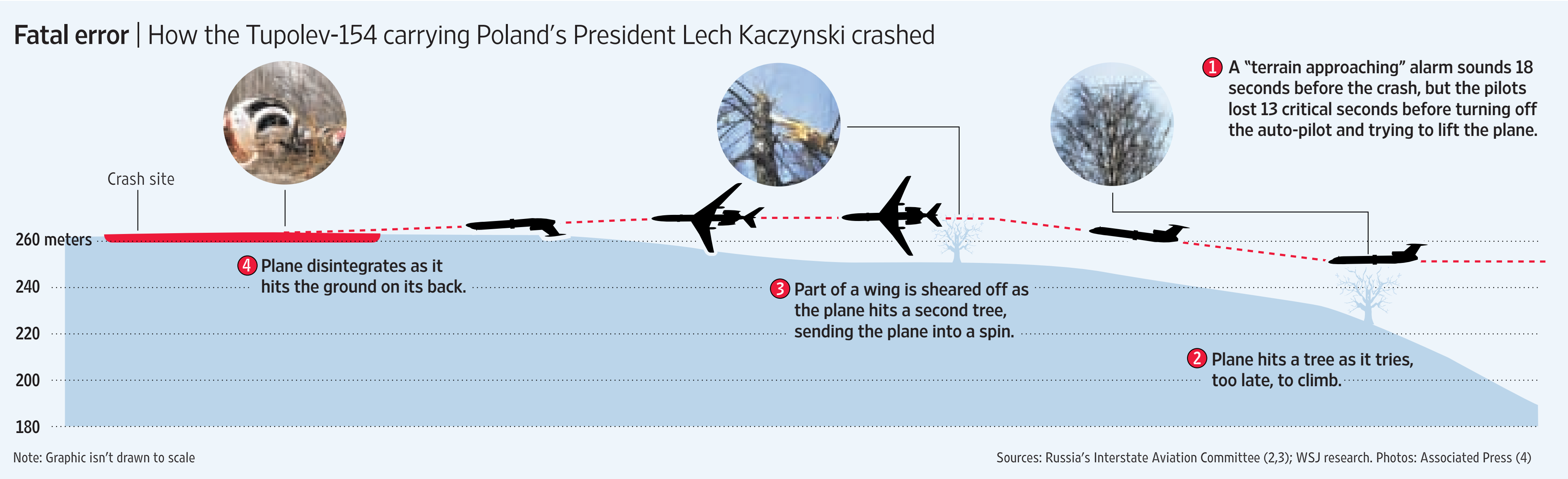
The EMA chief said budget cuts might force the agency to delay some investments, including improvements to its information-technology systems.

Mr. Lönngren said the crisis may have contributed to something else the EMA has noticed lately— a rise in poorly prepared applications from drug companies. Usually, the agency rejects about 20% of the drugs submitted to it.

"It was typically the small companies who had the highest rejection rate," he said. "Maybe these companies have a lack of competence, maybe they have the wrong people on board," he said, adding that it could also reflect "the tough economical climate that we have for several years, that has affected the small biotech companies."

The companies have generally failed to design their clinical trials properly or to uncover problems with their drugs before submitting them to the regulator, he said.

EUROPE NEWS



Polish crash probe nears completion

Investigation focuses on impact of general's visit to cockpit on pilots in disaster that killed president, 95 others

By Marcin Sobczyk

WARSAW—The investigation into the April plane crash that killed Poland's president and 95 others is close to finished, with the remaining focus on whether the Polish air force chief's presence in the cockpit contributed to pilot error, said the top Polish official involved.

Investigators have now confirmed that one of the passengers, Gen. Andrzej Blasik, was in the cockpit with the door open as the pilots approached the runway in thick fog around Smolensk, in western Russia. Investigators also say the crew of the presidential Tupolev-154 delayed trying to lift the plane for 13 seconds after an alarm warned them they were too close to the ground.

"Pretty much everything is clear right now and nearly all evidence has been gathered," with just some background noise on the voice recordings still to be deciphered "if possible," said Edmund Klich, head of the Polish body that investigates civil-aviation disasters, in a phone interview from Moscow. The final report should be released within weeks, Mr. Klich said.

President Lech Kaczynski, his wife and a high-level delegation were en route to commemorate the World War II Katyn forest massacre of thousands of Polish officers by Russian agents when their plane crashed April 10, killing everyone on board. Mr. Klich said those on board were subjected to forces of 100 times gravity on impact.

The disaster wiped out Poland's top military command and sank the nation into mourning. Moscow's sensitive handling of the tragedy also boosted reconciliation between the two ancient rivals.

The outcome of the joint Russian-Polish crash probe remains politically charged, however, with just weeks to go before Polish presidential elections, which are set for June 20. Jaroslaw Kaczynski, the late president's twin, is running in his brother's place. Mr. Kaczynski is trailing his main opponent, Bronislaw Komorowski, in opinion polls.

There has been persistent speculation in Poland and Russia that President Kaczynski may have pressured the pilots to land. In August 2008, during the war between Russia and Georgia, he gave orders to the military pilot flying his presidential aircraft to land in the Georgian capital, Tbilisi. The pilot refused.

One other passenger on the doomed Tupolev, still not identified, entered the cockpit 16 minutes before the crash, Mr. Klich said. Polish media have carried unconfirmed reports that the person was a presidential aide, asking if the crew would land on time for the president to make it to the commemoration.

"There's no specific command to land on the record," said Mr. Klich. "Psychologists will have to assess the stress levels the pilots were subjected to." That review is a part of the investigation that remains to be completed, he said.

The Tupolev's pilots ignored multiple warnings from the Smolensk control tower that visibility was poor and they should divert. Just four minutes from impact, another Polish flight crew already on the ground told the pilots that horizontal visibility at the airport was down to 200 meters, and vertical visibility was just 50 meters, according to details recently released by investigators in Moscow.


Russia's Interstate Aviation Committee

Investigators assembled the wreckage of the Tupolev-154 jet that crashed in western Russia on April 10, killing Poland's president and 95 others.

The military airport wasn't equipped to work with the Tupolev's landing system, and the safety visibility threshold for landing was 1,000 meters, the investigators said.

Unable to see, the pilots flew their Tupolev into a depression one kilometer from the airport. The plane was 15 meters below the elevation of the runway when its "terrain approaching" alarm went off, indicating the aircraft was less than 100 meters from the ground. Yet the pilots appear to have switched off the autopilot and sought to pull up only after the plane shuddered on hitting a 10.8-meter-high tree. That was 13 seconds after the alarm and just five seconds before impact.

A five-meter-tall birch tree sheared off part of the left wing and sent the plane into a spin before it landed on its back and disintegrated, according to the investigation.

Mr. Klich said there appeared to have been coordination problems among the crew in the cockpit, but didn't elaborate.

He also said Poland's laws, which make the pilot of a military aircraft its commander-in-chief, should be amended to rule out the possibility of a civilian influencing the pilot's decisions. The president is by law the supreme commander of the military even though he holds no military rank.

Human factors in air disasters have been a central focus of aviation safety for at least 15 years.

Specialists in the U.S., Western Europe and other highly developed aviation markets have worked to understand issues such as the stresses flight crews face and how well they interact, particularly in crisis situations.

Big strides have been made in raising awareness of how important it is for crews to focus on key tasks.

"On the face of it, 13 seconds appears a long delay to respond. You should react to a terrain warning immediately with full power and a pull-up," said Paul Hayes, director of safety at Ascend Ltd., an aviation consulting firm in London, who has reviewed the investigation materials released so far.

Mr. Hayes also questioned the presence of Gen. Blasik in the cockpit. "You should have a sterile cockpit during final approach. You should just have the crew talking about the work at hand. But there's no indication yet whether the non-crew members were a distraction," he said.

—Daniel Michaels in Brussels contributed to this article.

EU plans bank levy to support crisis funds

By Matthew Dalton

BRUSSELS—The European Commission on Wednesday proposed that each European Union government levy a tax on its banks and use the proceeds to create a fund dedicated to ensuring the "orderly failure" of troubled banks.

The proposal would create a European network of such funds that would follow the same rules, although the commission, the EU's executive arm, didn't provide details on how high the tax should be.

But the commission was adamant that the funds shouldn't be used to pump capital into banks or for other measures that could benefit bank shareholders and creditors, saying that otherwise banks might be encouraged to take bigger risks, knowing the funds are there to support them if they run into trouble.

The commission also wants to prevent the funds from being tapped for general public purposes, a provision that the U.K. and some other EU governments oppose.

Michel Barnier, the EU's commissioner for financial regulation, plans to discuss the idea with leaders at the Group of 20 industrial and developing nations meeting next month in Toronto. But other governments have their own ideas on bank crisis funds, and Canada opposes an additional tax on banks altogether.

The fund proposal will likely be included in legislation, expected early next year, to ensure EU governments have the powers to "resolve" an ailing bank. This includes changing management, wiping out shareholders, imposing discounted asset values or "haircuts" on creditors, orchestrating bank mergers and paying for the whole process without relying on taxpayer money.

The idea is to maintain the crucial functions of a weak bank without governments being forced to choose between allowing a bank to go bankrupt, at great economic cost, or bailing out a bank through repeated recapitalizations using taxpayer money, as governments did throughout the financial crisis.

"Without these funds, what we will see is an uncontrolled falling apart of large financial institutions, which can have disastrous secondary effects," said Mr. Barnier.

The funds would be used to pay for the costs of restructuring, such as setting up a "bridge bank" that would temporarily own and operate a failed bank to preserve its vital functions.

The commission is expecting some opposition from EU national governments to its proposal that the funds be reserved for restructuring costs, particularly at a time when EU governments are desperately searching for revenue to shrink their large budget deficits.

U.K. Chancellor of the Exchequer George Osborne welcomed the commission's proposal for a bank tax but said governments should have the power to spend the funds as they want. "We are clear that the purpose of that bank levy is to raise money that can ... be used for general expenditure purposes," he said.

German Finance Ministry spokesman Michael Offer said the levy could work as long as it doesn't unduly curtail a bank's competitiveness.

—Laurence Norman and Marietta Cauchi in London, and Parick McGroarty in Berlin contributed to this article.

EUROPE NEWS

Berlin defends ban on short selling

By Marcus Walker

European Pressphoto Agency

European Central Bank President Jean-Claude Trichet, left, German Finance Minister Wolfgang Schäuble, center, and IMF chief Dominique Strauss-Kahn hold a news conference at the Finance Ministry in Berlin in April.

BERLIN—German Finance Minister Wolfgang Schäuble is expected to get a dressing-down from U.S. Treasury Secretary Timothy Geithner on Thursday about Germany's unilateral actions on financial regulation. Mr. Schäuble is unlikely to show any remorse.

The veteran German politician, a crucial ally of Chancellor Angela Merkel, has drawn fire from financial-market participants as well as European and U.S. officials over Germany's sudden decision to ban certain types of financial bets against euro-zone governments and German banks, a move that sent nervous global markets into a tailspin last week just when a measure of calm seemed to be returning.

Yet Mr. Schäuble and other German officials are increasingly dismissive of criticism from financial markets, and view the unilateral ban on some kinds of short selling as a political victory at home, and an important signal to other countries.

"The financial market is only concerned with itself, instead of fulfilling its purpose and financing sensible, sustainable economic growth," Mr. Schäuble said in an interview with German newspaper Frankfurter Allgemeine Sonntagszeitung on Sunday, adding: "We have to change that."

The ban on some "naked" short selling, which Berlin plans to broaden to similar betting against all German stocks, has helped the 67-year-old German finance minister demonstrate to his domestic audience that he is up to the job of managing the euro currency area's growing financial crisis. Mr. Schäuble missed much of Europe's financial drama this spring due to health problems, leading to speculation in Germany that Ms. Merkel might have to replace him.

Mr. Schäuble, confined to a wheelchair since a mentally ill attacker shot him in the back during a 1990 election campaign, has missed a succession of high-level crisis talks since February due to unforeseen hospital visits, including the May 9 meeting in Brussels at which European Union finance ministers agreed on a nearly $1 trillion bailout fund for euro-zone countries struggling with heavy public debts. Ms. Merkel sent her interior minister to represent Germany at the meeting.

Mr. Schäuble said on Sunday that questions about his absences were "legitimate," but that he has proved for 20 years that "a seriously physically disabled person" can hold high office.

The finance minister's physical frailty is a headache for Ms. Merkel, who picked Mr. Schäuble for the second-most powerful post in her cabinet in the hope that his experience and reputation for political toughness would help her to repair Germany's public finances, battered by last year's recession.

Ms. Merkel has suffered a string of setbacks this month, including a defeat in important regional elections in Germany's most populous state, North Rhine-Westphalia, which cost her center-right coalition control of Germany's upper house of parliament.

At the same time, financial-market panic over public debts in Southern Europe forced a reluctant Germany to come to the rescue, first of Greece, then of the euro as a whole—much to German voters' chagrin. Support for the conservative-led government has been sinking fast in opinion polls.

The euro-zone bailout fund was running into resistance from lawmakers in Ms. Merkel's center-right camp last week, potentially endangering the euro zone's financial stability as investors looked for signs that the EU agreement might fall apart. On Tuesday Mr. Schäuble instructed Germany's financial regulator Bafin to ban naked short sales of euro-zone government debt, in a move that helped win over his Christian Democratic party, German officials say. Germany's parliament passed the bailout fund on Friday.

The short-selling ban helped, and greatly lifted morale among conservative lawmakers who were hearing voter anger about euro-zone bailouts, and about Germany's seeming impotence in the face of financial-market speculation against the euro, officials say.

However, the price was renewed fears in financial markets about an uncoordinated and ineffectual European response to the debt crisis in the euro zone, say economists. Privately, some German officials admit they had underestimated the reaction in financial markets—but most insist the German move was needed to inject momentum into international talks on financial regulation.

At a high-level international conference in Berlin last week, Mr. Schäuble warned representatives of other governments in the Group of 20 leading economies that Germany will press ahead with other national or European initiatives of global agreements can't be reached.

"The German government has decided that very stringent rhetoric on financial speculators is necessary to manage the coalition," says Nicolas Véron, a research fellow at Brussels think tank Bruegel. But what works for Ms. Merkel and Mr. Schäuble at home isn't helping reassure investors, he says: "There's a disconnection between the decision-making in Germany and the dynamics of the marketplace."

Geithner lays out his policy vision for Europe

Continued from first page

of Greece and were even later to ask the International Monetary Fund for financial help and expertise. By the time Europe and the IMF put together a €110 billion program for Greece, the problems had worsened.

An even larger program for other troubled European nations—as much as $1 trillion—hasn't managed to ease market concerns. Part of the reason, Mr. Geithner believes, is that European nations haven't spelled out the details of how the procedure would work.

"What Europe should do is implement the program they laid out," Mr. Geithner said.

"The basic lesson of financial crises is that you have to come in and act quickly and with force," he continued. The U.S. believes that without the heavy involvement of President Barack Obama and Mr. Geithner that Europe wouldn't have been willing to put together the kind of enormous bailout package that would impress markets that government had a handle on the problem.

Mr. Osborne complimented the U.S. administration's so-called Volcker Rule, which would bar banks from trading for their own accounts and from owning private equity firms and hedge funds. President Obama named the principle for former Federal Reserve Chairman Paul Volcker, who lobbied to limit the activities of banks. Congressional negotiators are now considering whether to include the rule in financial-industry regulation.

The greater U.S. involvement is reminiscent of the days of the Asian financial crisis of a decade ago when many current Obama economic officials including Mr. Geithner and White House economic adviser Lawrence Summers, travelled to Asia, doled out advice, and worked behind the scenes at the IMF to keep bailout funds flowing.

For Geithner critics, the new U.S. assertiveness is misplaced—and even dangerous. Desmond Lachman, a former senior IMF European official who is now a researcher at the American Enterprise Institute, said, "I find it rich that someone like Geithner is going around telling people how to handle their business."

Mr. Lachman feels the repeated bailouts engineered by Mr. Geithner have made the overall problem worse and that the U.S. advice of providing even more financing for heavily indebted countries like Greece is bound to fail.

He says Greece's debt needs to be restructured and that weaker euro zone countries should consider dropping the euro and reverting to their national currencies. "Geithner is part of the problem," he said. "It's obvious this can't work."

Christina Romer, Chairman of the White House Council of Economic Advisors and head of a US delegation to a meeting at the Organization for Economic Cooperation and Development in Paris accompanied Mr. Geithner on a plane from Beijing. She told reporters that she too would warn European and other countries against pulling out of their stimulus plans too quickly.

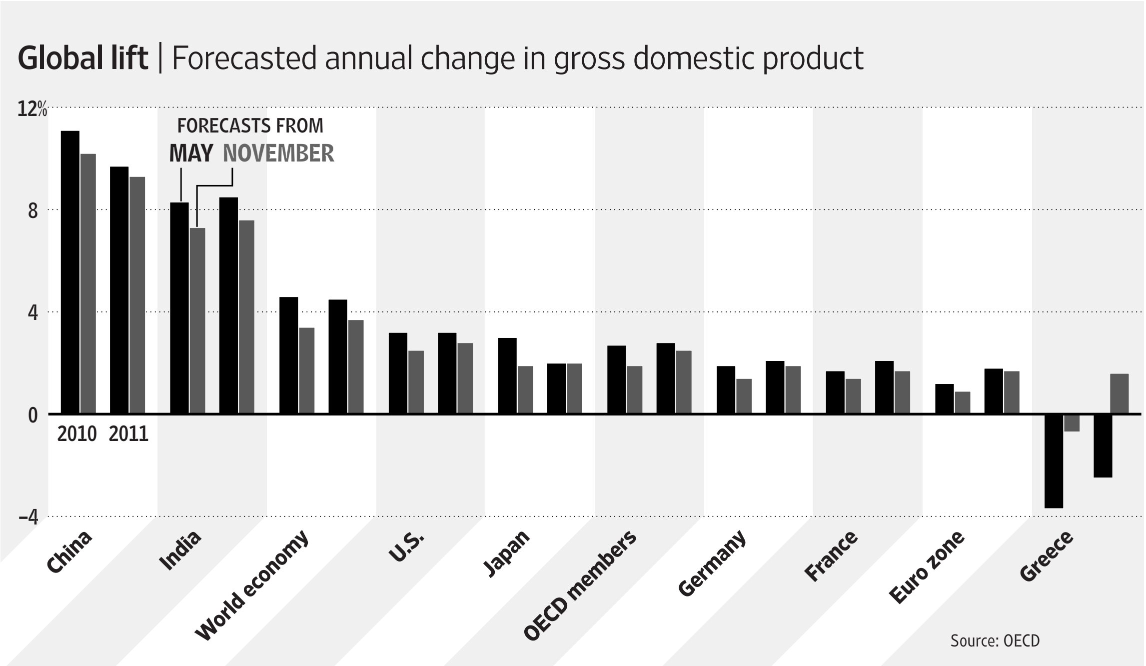
"There's a certain amount of rush for the exits on fiscal policy," Ms. Romer said. Treasury officials are also worried that Germany's proposal to ban trading on some financial products is damaging market confidence, spooking investors and suggesting that German officials aren't taking market reaction sufficiently into account. That's a message Mr. Geithner plans to deliver.

The difference in Washington's tone with Europe and with China was also striking. On the question of revaluing the renminbi, Mr. Geithner and other U.S. officials were careful to say they weren't going to public reprimand Beijing over its policy, fearing it could backfire politically.

Indeed, they only mentioned the currency fight after Chinese President Hu Jintao brought it up, and even then, U.S. officials took care to repeat that it was China's choice. But the U.S. is more direct with its European allies, especially as it looks to create common ground before a G-20 leaders summit in Canada at the end of June.

—Laurence Norman in London contributed to this article.

Treasury officials are also worried that Germany's proposal to ban trading on some financial products is damaging market confidence, spooking investors and suggesting that German officials aren't taking market reaction sufficiently into account.



OECD raises forecast for global economic growth

By Paul Hannon And William Horobin

LONDON—The Organization for Economic Cooperation and Development raised its forecast for economic growth this year and next, amid risks to recovery posed by euro-zone debt and possible economic overheating in some parts of Asia.

In its twice-yearly outlook published Wednesday, the Paris-based think tank cited strong growth in developing economies and the rapid rebound in world trade to predict that the organization's 31 members will see their combined gross domestic product increase 2.7% this year and 2.8% next year. In November, the OECD forecast growth of 1.9% this year and 2.5% next.

The OECD also raised its growth forecasts for the global economy. Having previously expected world GDP to rise 3.4% this year and 3.7% next, it now expects growth of 4.6% in 2010 and 4.5% in 2011.

The OECD, however, acknowledged concerns about the ability of some European nations to repay their debts and the risk of overheating in some Asian economies.

"While originating in some euro-area economies, instability has spread to other euro-area members and sovereign debt markets in other parts of the world," Chief Economist Pier Carlo Padoan said. "Overheating in emerging-market economies also poses a serious risk. A boom-bust scenario cannot be ruled out."

But the OECD said growth could be even stronger than estimated among its 31 members.

"Fixed investment could bounce back more robustly and household consumption could recover more rapidly with household savings rates having risen more slowly than previously anticipated, especially in Europe," Mr. Padoan said. "The spillover from growth in...Asia could be stronger than expected, especially in the United States and Japan."

The OECD raised its growth forecast for the euro zone despite government-debt problems, although it still expects the currency area to lag behind other leading economies. The combined GDP of the 16 countries that use the euro is expected to rise 1.2% this year and 1.8% next, while the U.S. economy is expected to grow 3.2% in each of those years, and the Japanese economy to expand 3% this year and 2% next, the OECD said.

The OECD said governments should start to cut their budget deficits now, arguing the need has become more pressing since investors began to demand higher interest rates. For every one percentage point increase in yields on government bonds, the organization said, economic growth would be reduced by half a percentage point in the current and subsequent year.

Body urges U.K. rate hike

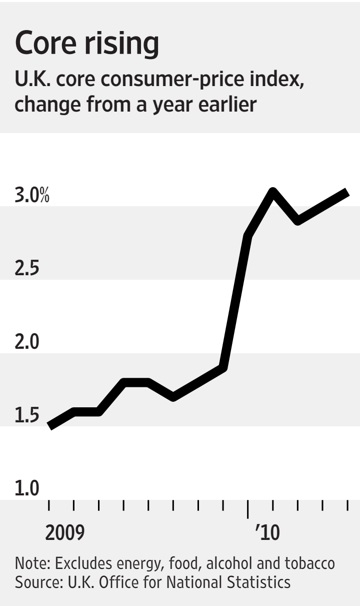
By Natasha Brereton

The Bank of England should raise its key interest rate to 3.5% by the end of 2011, with rate increases and a scaling back of quantitative easing starting in the second half of this year, the Organization for Economic Cooperation and Development said Wednesday.

The OECD acknowledged that loose monetary policy was appropriate to support economic activity. But, in a significant shift, it said the British central bank should start normalizing conditions soon to respond to a likely gradual rise in underlying inflation, and to help preserve its credibility.

Inflation stood at 3.7% in April, compared with the central bank's target of 2%. Core inflation, which excludes volatile energy, food, alcohol and tobacco prices, was 3.1%.

"The gradual drift up of some measures of inflation expectations implies a need to increase interest rates earlier than previously thought and no later than the last quarter of 2010," the OECD said. "The projected increase of core inflation to the Bank of England target warrants an increase of the policy rate to 3.5% by end-2011."



Some economists responded with a degree of incredulity.

"The view is so extreme that it looks like a typing error," said Lena Komileva, of Tullett Prebon.

Such aggressive action, she warned, could destroy confidence in British economic policy. She said the need for substantial fiscal tightening, amid banking-sector strains and economic weakness in the U.K.'s largest trading partner, the euro zone, demands extremely accommodative policy for some time.

The new British government is under intense pressure to tighten its fiscal belt, with international ratings agencies threatening to cut the country's triple-A credit rating unless it slims down its debts. The Treasury announced spending cuts Monday of £6.25 billion ($9 billion) for the current financial year, but the reductions are only a beginning in paring back a £156 billion deficit.

In its latest inflation report earlier this month, the Bank of England's Monetary Policy Committee said inflation would be below but close to its medium-term target of 2%, assuming its stock of asset purchases is maintained at £200 billion and the key interest rate is kept at 0.5%. Market interest rates suggest investors expect the bank's key interest rate to be no higher than 1.5% by the end of 2011.

Europe's woes threaten confidence world-wide

[Capital]

By David Wessel

Looking at the economy from Australia is like falling through Alice in Wonderland's looking glass.

Unlike the U.S. and Europe, Australia is at full employment (5.4% unemployment) and its central bank is raising interest rates (now 4.5%) to cool off the economy. It has things that China can't get enough of—iron ore and coal. And its bankers and their regulators fret that there aren't enough government bonds for banks to buy to meet new liquidity rules; government deficits have been too small to produce a lot of government debt.

So why do Australian officials look so worried? Well, the Australian dollar is down 13% since mid-April and the Australian stock market is down 15%.

What happens in Europe, it turns out, doesn't stay in Europe.

When the Australian central bank's policy committee met May 4, members spent "considerable time discussing the disturbances in financial markets arising from concerns about sovereign debt in parts of Europe, with their focus particularly, but not only, on Greece," recently released minutes of the meeting reveal. "So far at least, there had not been significant contagion to debt markets outside Europe."

But since then, reaction to Europe's struggles in places as far away as Sydney, Beijing and New York has turned from *schadenfreude* to angst about a double-dip recession.

Part of this is the simple story: If European government austerity and credit crunches slow growth, Europe will buy less from the rest of the world. But Europe accounts for less than 9% of Australia's exports. Europe does buy about 20% of U.S. exports, but exports are a much smaller slice of the mighty U.S. economy. Yet it's easy to predict improvements in the domestic U.S. economy, do a little arithmetic, predict that slower growth or even recession in Europe would shave a few tenths of a percentage point off U.S. growth and find other things to worry about—like the Koreas.

But that's the kind of logic that led almost all forecasters to shrug off the subprime mortgage debacle as too small to sink the U.S. economy.

The global finance crisis—they call it "the GFC" in Australia, and are startled to discover that a visiting American doesn't recognize the acronym—taught a few enduring lessons: Financial markets are very efficient at spreading anxiety from one continent to another. The market mood can swing from cautious optimism to panic very quickly. When banks, institutional lenders and other big-money investors all grow cautious, the rest of us have a hard time borrowing and the economy sputters. And the worst-case scenario is worse and more likely than most of us imagined.

The past few weeks in Europe have hardly inspired confidence. Watching European leaders respond to doubts about their governments' ability to repay debts, the health of their banks and the viability of the euro itself has been like watching a bunch of firefighters hold a conference call before dispatching firetrucks. Doubts about the true health of Europe's big banks persist, and Europe hasn't found a way to bolster confidence in them or boost their capital cushions the way the U.S. did with the much-maligned, now much-celebrated "stress tests" of 2009.

In one important way, the global reaction helps the U.S. Money is fleeing other places—Australia and Europe—for the safety of the U.S., pushing down the yields on Treasury debt. That makes it cheaper for the U.S. government to finance its big deficit. It pulls rates on 30-year fixed-rate U.S. mortgages toward 4.5%, which should buoy house prices and prompt refinancing, which, in turns, provides a little oomph to consumer spending.

Reaction to Europe's struggles in places as far away as Sydney has turned from *schadenfreude* to angst.

But, unfortunately, those effects may be offset by a bigger one: The reluctance of investors and lenders to take risks. All the gauges that measure financial anxiety are turning up. Banks are charging more to lend to each other, for instance. Risky U.S. companies have to pay more to sell junk bonds. Anxiety isn't back to the levels of fall 2008, but it's worse than it was six weeks ago—and no one can be sure whether this is a blip or a step toward something even more significant.

The route to a double-dip recession runs through the banks and other lenders. If they pull back, either because they can't get money because no one trusts them or because they are hoarding money because they're uneasy about the future, then there will be less fuel for growth. This time, unlike fall 2008, world governments are unlikely to offset that with another massive round of tax cuts and spending increases, or world central banks with more interest-rate cuts and monetary expansion. They see themselves as tapped out.

Confidence is an important and fragile commodity. Confidence in big U.S. banks and the resilience of the U.S. economy and in the remarkable vigor of China and other Asia economies was bolstering confidence and beginning to breed a self-fulfilling optimism from Australia to America. Europe has undermined that, prompted a "here we go again" sense in markets and bank lending committees that will—unless reversed—hurt economic growth around the world. Even in Australia.

U.S. NEWS

California rivals fight for the right

In GOP primary race for governor, a 'Schwarzenegger' is code for 'bad Republican'; Silicon Valley face-off

By Stu Woo

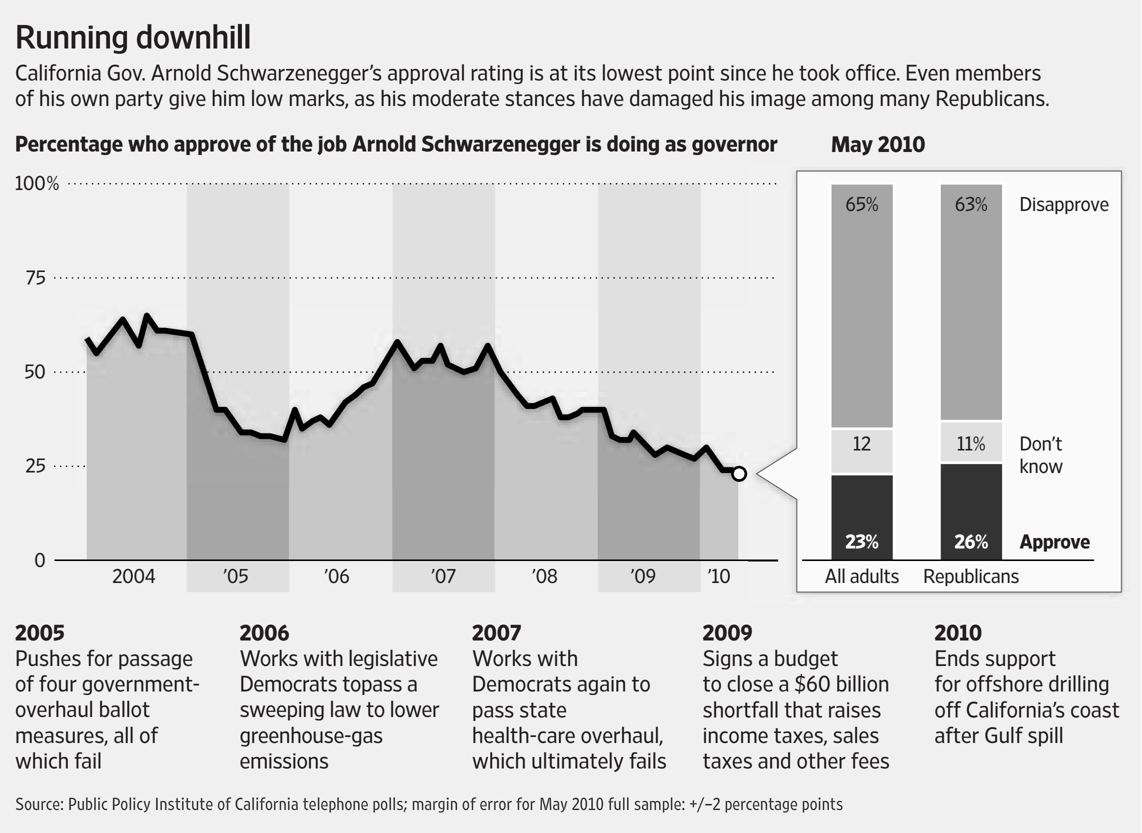
California's major GOP gubernatorial hopefuls, Meg Whitman and Steve Poizner, aren't just running against each other in the June 8 primary. They are also running against the Republican they want to succeed, Gov. Arnold Schwarzenegger.

The Whitman and Poizner campaigns are so eager to distance themselves from Mr. Schwarzenegger that they use the former movie star's name to attack their opponents. They have taken turns labeling each other a "Schwarzenegger," which in this race has come to mean "bad Republican."

The race features two former Silicon Valley executives in Ms. Whitman, who was eBay Inc.'s chief executive, and Mr. Poizner, currently the state's insurance commissioner. Each multimillionaire candidate has tried to paint the other as an insincere conservative.

A poll last week showed Ms. Whitman leading Mr. Poizner, 38% to 29%. The winner is expected to face Democrat Jerry Brown, the state's attorney general and a former governor, in November.

The two Republicans' low views of Mr. Schwarzenegger, the former pride of the California Republican Party, stems from his falling popularity and his moderate stances—in an election cycle where moderation isn't sitting well with many conservative voters.



Mr. Poizner has run three television ads comparing Ms. Whitman with Mr. Schwarzenegger, who is subject to term limits.

One shows Mr. Schwarzenegger's face morphing into Ms. Whitman's face. After the transformation, U.S. Rep. Tom McClintock, a Poizner endorser, appears onscreen with this message: "California can't afford Arnold Schwarzenegger's third term, and that's Meg Whitman."

The Whitman campaign has responded to the attacks with its own name-dropping charges.

"There's only one candidate in the race who has spent $20 million [in previous campaigns] trying to convince voters that he's the Schwarzenegger politician, and that's Steve Poizner," Mike Murphy, a Whitman strategist, said. The commercials have been "entertaining, but it's an ineffective thing for the Poizner campaign, so I hope they keep on doing it."

To win California's Republican primary, Mr. Poizner and Ms. Whitman must woo hard-core conservatives, who even in such a liberal state make up a disproportionate chunk of the GOP primary electorate, political analysts said.

Mr. Schwarzenegger, who likes to call himself a centrist, isn't popular among these diehards for many positions taken during his six-year term. Among those positions: championing a gas-emissions regulation bill that passed in 2006, signing a tax-raising budget in 2009 and supporting a ban on offshore drilling earlier this year.

"Conservatives want to make him look like a Democrat as much as possible, so they can distinguish their own mantra from what they feel to be an establishment that caters to liberal causes," said Larry Gerston, a San Jose State University political scientist. "To conservatives, he's the classic definition of a RINO: a Republican in name only."

The governor's unpopularity—his approval rating has dropped to 23% amid the state's budget woes—and the anti-incumbent bent around the country have also fueled the GOP candidates' attacks.

Gubernatorial spokesman Aaron McLear said Mr. Schwarzenegger doesn't pay attention or care about the attacks.

"It's not that they're running from the governor," he said of the Republican candidates. "It's that they're trying to outdo each other in running to the extreme right on traditional red-meat issues like immigration, abortion and who supported which Democrat in the past."

Tax incentive fuels sales of new homes

By Sara Murray

Sales of newly built homes soared in April as buyers rushed to take advantage of an expiring tax credit.

The Commerce Department said Wednesday that sales of new single-family homes rose 14.8% from the prior month to a seasonally adjusted annual rate of 504,000.

Demand for new homes had also surged in March, when sales climbed 29.9% from the prior month. Sales in April were 47.8% higher than a year earlier.

The recent surge was likely the result of expiring government incentives, which provided an $8,000 tax credit for first-time buyers and a $6,500 credit for repeat homeowners. Contracts for those homes had to be signed by April 30. Buyers have to complete purchases by June 30.

The housing market is stabilizing after both sales and prices plummeted during the recession. Sales of existing homes, a far bigger number than newly built homes, jumped 7.6% in April, the National Association of Realtors said.

Construction of new homes also is picking up. Starts for single-family homes rose 10.2% in April from a month earlier, the fourth-straight monthly increase.

Indices of home prices are no longer dropping precipitously; the closely watched Case-Schiller index has fallen for the past six months, but is above year-ago levels.

Some economists say the April tax-credit deadline pulled forward some sales that, with the absence of the tax incentive, might have taken place later this summer. That could cause home sales to sag in the next couple of months.

"Sales are on a mildly upward trend if you kind of look through those numbers," said Peter Newland, a Barclays Capital analyst, "but certainly that won't be apparent in the next few months, as you see the payback from the tax credit."

The increase in sales brought the backlog of new homes down to five months, based on the current rate of sales, from 6.2 months in March.

The median price of a new home fell to $198,400 last month from $219,600 in March, which was likely influenced by the tax credit also.

"Those who wanted to tap the tax credit tended to buy cheaper houses," said Aichi Amemiya, a Nomura Securities International Inc. economist.

U.S. NEWS

BP starts 'top kill' effort to plug leaking Gulf well

BY GUY CHAZAN AND ANGEL GONZALEZ

BP PLC said it had started its "top kill" operation Wednesday to plug the leaking well that has gushed hundreds of thousands of barrels of crude into the Gulf of Mexico since April 20.

The procedure involves injecting heavy drilling fluids into the broken well via the blowout preventer, the shut-off valve that stands on the seabed. BP said it started pumping early Wednesday afternoon and the operation was continuing.

The company previously ran a battery of tests to gauge whether the procedure, which has never been tried at these depths, could work. The company earlier received authorization to proceed from U.S. Coast Guard Rear Adm. Mary Landry.

Much is riding on the procedure. Success could mark a turning point for BP and its beleaguered chief executive, Tony Hayward, who has been pilloried in public for his company's handling of the spill.

But failure could mean that oil continues to spew from the floor of the Gulf for at least another two months, until a relief well can be completed. BP appears to be running out of ideas for containing the spill in the short term.

BP said that the top-kill procedure could take up to two days to implement, and it was unclear how long it would take for BP to find out the results, the company said.

The deepwater well is estimated to be leaking at a rate of at least 5,000 barrels of oil a day, resulting in one of the worst oil spills the U.S. has ever seen.

The effort is being closely watched by federal authorities and by the entire oil industry, which faces an onslaught of regulation in the wake of the spill, one of the worst ever seen in the U.S.

The effort is being closely watched by U.S. authorities and by the entire oil industry, which faces an onslaught of regulation in the wake of the spill.

At a shareholders' meeting in Dallas on Wednesday, **Exxon Mobil** Corp.'s Chief Executive Rex Tillerson said that Exxon continues to provide assistance to BP in dealing with the disaster. "We are eager to support efforts to determine how such an incident can be prevented in the future," he said.

Chevron Corp. Chief Executive John Watson said at his company's shareholders' meeting in Houston on Wednesday that the industry is going to learn "a great deal" out of the spill.

"If there's something we have to adopt, we will adopt it," he said.

BP said that if the top-kill operation fails, it will move a containment system over the spill to try to capture the oil.

To do that, the company will first have to remove a damaged pipe, known as the riser, that was bent when the **Transocean** Ltd. rig sank last April. Then BP would place a "cap" atop the pipe leading out of the blow-out preventer, a large valve that sits atop the well, and siphon the oil to a surface vessel.

The cap is already on site and could be deployed by the end of May, BP said.

BP is also mulling lowering a second blow-out preventer. Concurrently, the company is drilling two relief wells, but they are expected to take months to complete.

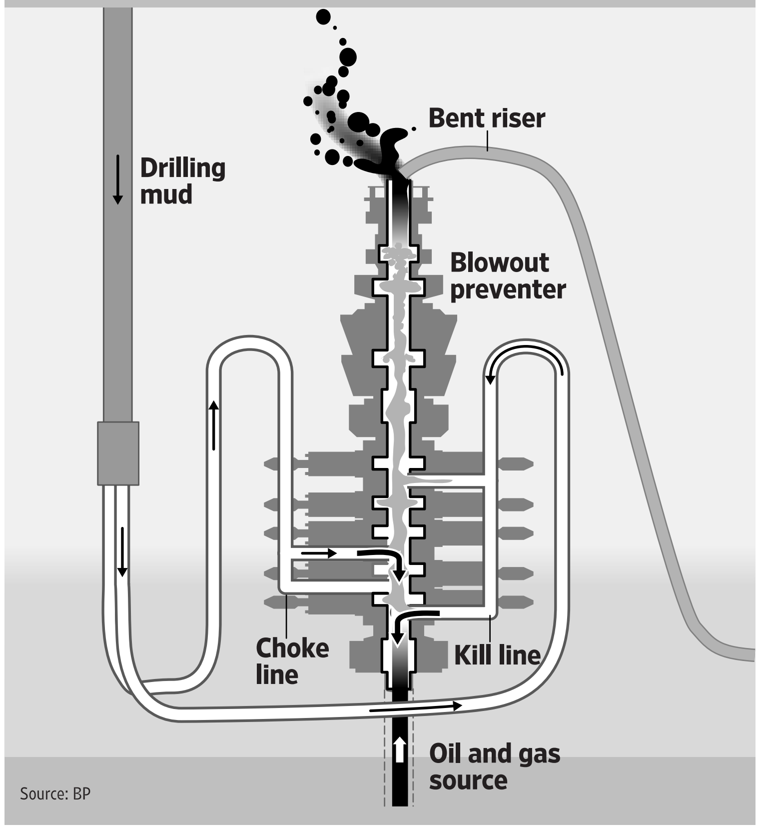
A BP spokesperson said that in the past 24 hours the company had captured 2,600 barrels of crude through a tube connecting a surface vessel to the damaged underwater infrastructure.

—Isabel Ordonez and Susan Daker contributed to this article.

Choking the source

BP engineers plan to try a **'top kill'** Wednesday, using drilling mud to plug the gushing well.

The drilling mud is pumped from a ship, down 5,000 feet to the choke and kill lines of the blowout preventer. If successful, workers will next pump in cement to seal the well.



Source: BP

Heated argument on rig before blast

BY MIGUEL BUSTILLO

KENNER, La.—More details have emerged about a disagreement between employees of rig operator **Transocean** Ltd. and oil giant **BP** PLC over how to begin shutting down a well just hours before it exploded in the Gulf of Mexico last month.

Testimony about the disagreement Wednesday, in a joint hearing here held by the U.S. Coast Guard and the Minerals Management Service, which jointly regulate offshore drilling, is likely to bring increased scrutiny to the decisions BP made aboard the rig the day of the explosion, April 20. There is also likely to be more focus on whether Transocean should have done more to ensure proper procedures were carried out.

Douglas H. Brown, Transocean's chief mechanic on the Deepwater Horizon rig, said key representatives from both companies had a heated argument in an 11 a.m. meeting on April 20. Less than 11 hours later, the well had a blowout, an uncontrolled release of oil and gas, killing 11 workers.

Mr. Brown said Transocean's crew leaders including the rig operator's top manager, Jimmy W. Harrell, strongly objected to a decision by BP's top representative, or "company man," over how to start removing heavy drilling fluid and replacing it with lighter seawater from a riser pipe connected to the well head. Such pipes act as conduits between the rig and the wellhead at the ocean floor, and carry drilling fluid in and out of the well.

Removing heavy drilling fluid prior to sealing a well is normal, but questions have emerged about whether the crew started the process without taking other precautionary measures against gas rising into the pipe.

It isn't clear what Mr. Harrell objected to specifically about BP's instructions, but the rig's the primary driller, Dewey Revette, and tool pusher, Miles Randall Ezell, both of Transocean, also disagreed with BP, Mr. Brown said.

However, BP was in charge of the operation and the BP representative prevailed, Mr. Brown said.

"The company man was basically saying, 'This is how it's gonna be,' " said Mr. Brown, who didn't recall the name of the BP representative in question.

"He pretty much grumbled in his manner, `I guess that is what we have those pinchers for,' " Mr. Brown testified. He said it was a reference to the shear rams on the drilling operation's blowout preventer, which are supposed to sever the main pipe in case of a disaster.

The blowout preventer failed to stop gas from rising to the surface during the explosion, BP has said.

Mr. Harrell hasn't testified and declined repeated requests for comment.

Donald Vidrine, listed on Transocean's documents as BP's "company man" on April 20, couldn't be reached for comment. Mr. Revette was among the 11 workers who were killed. BP declined to comment on the testimony.

Transocean didn't immediately have comment but has previously said that BP was responsible for major decisions made on the rig.

WORLD NEWS

Koreas have yet to dismantle industrial link

By Evan Ramstad

SEOUL—As South and North Korea traded economic sanctions and criticism this week, leaders in both countries stopped short of interfering with the biggest economic connection they have: a joint industrial zone where about 120 South Korean companies employ more than 40,000 North Koreans.

On Wednesday morning, just hours after North Korea lashed back at South Korea by declaring it would "completely halt" inter-Korean cooperation, the North allowed 818 South Koreans to go to work as usual at the Kaesong Industrial Complex.

That step eased some of the tension created when North Korea late Tuesday lashed back at South Korea for accusing it of sinking a South Korean warship and announcing penalties against it Monday. In its rejoinder, Pyongyang said it would cut off communication with the South and all economic ties. But it left itself an exception: The North said it would expel South Korean government officials from the Kaesong project in North Korea, a ban that apparently didn't cover corporate workers.

"Neither side wants to be the one who loses the Kaesong complex," says Lim Eul-chul, a professor at Kyungnam University in Seoul and author of a book on the project.

Later Wednesday, U.S. Secretary of State Hillary Clinton, after meetings with South Korean President Lee Myung-bak and Foreign Minister Yu Myung-hwan in Seoul, said South Korea's response to the sinking was "prudent" and "absolutely appropriate."

She said the U.S. would support South Korea as it seeks penalties against the North at the United Nations Security Council, where the U.S. is one of five permanent members. Mr. Yu said South Korea hasn't decided when to begin that process.

Even as the two Koreas spar verbally over the sinking of the Cheonan warship two months ago, the Kaesong complex emerged as too important for either country to close.

South Korean officials worry about the symbolism and political fallout of severing that last connection with the North. South Korean President Lee Myung-bak decided to cut other trade with the North but said the Kaesong complex has "unique characteristics."

North Korea's government needs the money and jobs the complex brings, analysts say. The factories there account for more than half of the $1.6 billion trade relationship between the two Koreas and some of them are among the biggest employers in Kaesong, North Korea's third-largest city.

Economic survivor | A look at the Kaesong Industrial Complex by the numbers:

Even as the two Koreas lashed out at each other this week, both sides left their chief economic project alone.

Year opened:	South Korean companies in complex*:	North Koreans employed at complex*:	South Koreans employed at complex*:	Value of 2009 production at complex
2004	121	43,804	886	$250 million

*As of May 2010

Sources: WSJ reporting; Reuters (photo)

The industrial zone emerged out of the first-ever inter-Korean summit meeting in 2000, which was between South Korean President Kim Dae-jung and North Korean dictator Kim Jong Il.

But the complex hasn't grown nearly as fast or as large as the two leaders originally envisioned because it became a bargaining chip in many inter-Korean disputes. For a few months late last year, North Korea prohibited South Korean government workers from entering the complex.

And on Wednesday, after permitting operations to continue at the site, North Korea said it may close the complex if South Korea follows through with its stated plan to put up loudspeakers along the inter-Korean border and blast propaganda messages.

Meanwhile, South Korean officials this week encouraged companies to reduce the number of people they send into Kaesong and said the country wouldn't permit South Koreans to stay for multiple days there.

Shim Sun-seok, president of Daesun Tech Co., a maker of clock parts with a factory at the complex, cut the number of South Korean managers commuting there to two this week from the usual four. "I don't expect Kaesong to be totally closed," she said. "A total shutdown seems too extreme to actually happen."

Korea Micro Filter Co., a maker of auto parts, also cut the number of South Korean managers on-site, said Song Ki-suk, the company's chief executive. That step may create some problems in production scheduling, he said.

"Since the Kaesong compound has been opened, we have had the situation a few times when people thought it might close," Mr. Song said. "We always have a contingency plan in case something happens."

—Jaeyeon Woo contributed to this article.

China, split on Korea issue, may be set to join critics

By Jay Solomon And Andrew Browne

BEIJING—North Korea's new belligerence has exposed cracks in the thinking of Chinese officials toward their erratic neighbor, but its leaders appear to be edging toward criticizing Pyongyang for its alleged role in sinking a South Korean warship.

China is the chief supplier of food, energy and arms to impoverished North Korea, its traditional socialist ally.

Yet official views on North Korea in China have appeared divided, according to U.S. officials who said they spent "hours" trying to gain China's insights into North Korea's recent actions, and the calculations behind the actions of its ailing leader, Kim Jong Il, during a trip to Beijing for a high-level U.S.-China dialogue this week.

"The Chinese seem frustrated" with Mr. Kim, said a senior U.S. official who took part in the talks.

On Wednesday, senior U.S. officials said they expected China to join international criticism of the North and carefully move closer to South Korea's position that Pyongyang must be held accountable for the March attack, news agencies reported from Elmendorf Air Force Base in Alaska, where Secretary of State Hillary Clinton's team stopped on its return to the U.S.

Many Chinese analysts say they believe Chinese leaders have grown exasperated with Mr. Kim, who embarrasses them with his nuclear theatrics and has shown little inclination to copy Chinese market-led overhauls, even though Beijing has tried to dazzle him with tours of showcase cities and development zones.

North Korea's trade

Annual trade between North Korea and its two biggest trade partners

Sources: KOTRA; China's Ministry of Commerce

Beijing's loyalties toward its impoverished ally have been tested as it weighs its response to the sinking of the Cheonan with the loss of 46 lives.

China's noncommittal position so far on the findings of an international investigation, which determined that a Northern torpedo ripped apart the vessel, threatens to sour its relations with Seoul, an increasingly important trade partner, and undermine its prestige as a responsible regional and global player.

"China is more than ever before in a dilemma," said Shi Yinghong, a professor of International Relations at Renmin University of China.

The issue will provide a challenge for Premier Wen Jiabao this weekend when he attends a three-nation summit with leaders from South Korea and Japan. The U.S. officials cited in news-agency reports said they believed Mr. Wen would begin to express its shift during these meetings.

The splits inside Beijing on North Korea appear to be based both upon the age of Chinese officials and their place in government.

One U.S. official said older Chinese officials who dealt with Mr. Kim's father, Kim Il Sung, remember him as largely predictable and responsive to Chinese influence. "He was more pliant," the official said they were told.

Kim Jong Il, in contrast, appears to the Chinese as unpredictable and elusive. U.S. diplomats acknowledged that the Chinese appeared reluctant to share too much information. A Chinese freeze on military-to-military relations with the U.S. means American officials are cut off from one of the best sources of intelligence on Pyongyang—the Chinese People's Liberation Army.

Washington accelerated its efforts to try to discuss North Korea with the PLA in 2008 following reports that Kim Jong Il suffered a stroke. George W. Bush's administration believed the U.S. and China needed to initiate contingency planning in the event Mr. Kim died or his country faced political instability. The Pentagon still deploys 29,000 American troops to South Korea to guard against a North Korean attack.

The Chinese leadership rebuffed the Bush administration's overtures, however, according to current and former U.S. officials. Beijing feared such discussions could alienate Pyongyang or be viewed as China plotting against its military ally.

This week in Beijing, Mrs. Clinton included Admiral Robert Willard, the head of the Pentagon's Pacific Command, in her delegation. U.S. officials said Mrs. Clinton again hoped to signal to Beijing that Washington wants to engage militarily with China on the North Korea question.

Still, the U.S. is trying to engage more. "The military is key to understanding North Korea," said a U.S. official.

Beijing's response to the ship sinking is further complicated by calculations over a looming succession to Mr. Kim, says Jasper Becker, the author of "Rogue Nation," a recent book on North Korea. "The thing they're really debating is what to do about the succession."

Mr. Kim is positioning his third son, Kim Jong Eun, to succeed him. Some analysts believe he was lobbying China to support his dynastic succession plans when he visited Beijing earlier this month to meet President Hu Jintao.

China has given no indication about its preferences on who should succeed Mr. Kim, although as Pyongyang's main supporter, it has a role to play, and its leverage is growing as South Korea, Japan and other countries turn their backs on Mr. Kim's beleaguered regime.

Nevertheless, Beijing is acting with extreme caution even as North Korea threatens to "totally freeze" relations with South Korea and pull out of a nonaggression pact. China's instincts are to "sit it out and keep a lid on things," says Mr. Becker.

That response sits badly with public opinion in South Korea. Kang Joon-young, who heads the China Research Institute of Hankook University of Foreign Studies in Seoul, says that when South Korea announced the results of the investigation into the Cheonan sinking "it hoped China would send its full support—but it didn't. It gave a lukewarm response....It even seems like China is taking Pyongyang's side. The South Korean government is deeply disappointed."

Beijing's strategic goal has long been to prevent a collapse of North Korea, which provides a buffer against South Korea and U.S. military bases there. Its nightmare is that internal chaos in the North could spill millions of refugees across its border.

Shi Yongming, a researcher at the International Strategy Research department of the China Institute of International Studies, says Beijing's support for Pyongyang is "not open-ended." He adds that China, which has long played the role of benefactor to North Korea, now sees long-term economic opportunity there.

Chinese companies are positioned to reap rewards from preferential access to North Korea's rich mineral resources, as well as operating port and other facilities.

—Jaeyeon Woo and Gao Sen contributed to this article.