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THE WALL STREET JOURNAL.

VOL. XXVIII NO. 64 — EUROPE — Monday, May 3, 2010

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Greece seals bailout deal

Greece reached a historic deal with other euro-zone countries and the International Monetary Fund for a three-year, €110 billion ($146.5 billion) bailout, as the country's prime minister on Sunday exhorted his nation to bear the sacrifices needed to mend broken public finances and vowed that his government won't "allow the country to become bankrupt."

By Charles Forelle in Brussels and Nick Skrekas in Athens

The rescue involves outside aid on a scale not attempted in Europe since the U.S.-led effort to reanimate the Continent after World War II. No euro-zone country has ever taken a bailout from a peer. Besides its 2008 rescue of Iceland, the IMF's last intervention in Western Europe was in 1976, when it lent £2.3 billion ($3.5 billion at current exchange rates) to the U.K.

"We have no other choices and no time, so accessing the bailout is inevitable," Prime Minister George Papandreou said in a televised speech. Greece needs cash to pay back €8.5 billion in borrowings due May 19. A years-long fiscal spiral of debt and deficits has only gotten worse, cutting the country off from capital markets.

On Sunday, the finance ministers of the 16 euro-zone nations agreed that the 15 other countries would lend €80 billion over three years, after receiving a positive assessment of the need for a bailout by officials at the European Commission, the bloc's executive arm, and the European Central Bank. The IMF will, in parallel, offer a €30 billion package.

The EU countries will lend as much as €30 billion this year. Jean-Claude Juncker, the president of the council of euro-zone finance ministers, said the first tranche will be delivered before the May 19 redemption.

The price of the aid is a set

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European Pressphoto Agency

Jean-Claude Trichet, Jean-Claude Juncker, and Europe's monetary-affairs commissioner, Olli Rehn, in Brussels Sunday.

Boards set to OK airline merger

By Susan Carey And Gina Chon

UAL Corp. United Airlines is expected to announce early Monday that it will acquire **Continental Airlines** Inc. in a share swap valued at more than $3 billion, a deal that would create the world's largest airline.

The boards of UAL and Continental met Sunday and were expected to sign off on a merger agreement that would pay Continental shareholders a price higher than the airline's current market capitalization of $3.1 billion, people familiar with the matter said.

Continental has a heavy market presence in Europe and Latin America, while United is strong across the Pacific.

The combined company—which would use the United name—would be nearly 8% larger than **Delta Air Lines** Inc. in traffic, as measured by the number of miles flown by paying passengers world-wide, including commuter affiliates. It would command 21% of seats in the U.S. market, versus Delta's 20% share since it vaulted to the top spot with its 2008 acquisition of **Northwest Airlines**.

Related article on page 19.

Spill could challenge Valdez disaster

The **BP** PLC oil spill in the U.S. Gulf of Mexico was potentially "catastrophic" and could turn out to be worse than the Exxon Mobil Corp. Valdez spill in Alaska, U.S. Interior Secretary Ken Salazar said Sunday.

By Ian Talley, Alicia Mundy And Jeffrey Ball

"The worst-case scenario is we could have 100,000 barrels [a day] or more of oil flowing out," Mr. Salazar said on CNN's "State of the Union."

The spill occurred after the Deepwater Horizon drilling rig blew out on April 22, killing 11 people and leaking crude oil into the Gulf of Mexico. The slick is threatening the coastal region's fishing, tourism and shipping industries.

BP and the U.S. government have over the past week stuck to their raised estimate of 5,000 barrels a day spilling out of the deepwater well. But Homeland Security chief Janet Napolitano on Sunday told ABC News's "This Week" that the current spill rate could currently be much higher.

"Right now that could be in the tens of thousands of gallons per day, of barrels per day," she said, without elaborating which figure was more accurate. One barrel of oil is 42 gallons.

The Valdez spill, caused by a wrecked tanker, spilled 11 million gallons of crude over three months in 1989, devastating part of Alaska economically and environmentally.

Associated Press

Scientists collect a dead sea turtle from a beach in Mississippi.

U.S. Coast Guard Commandant Admiral Thad Allen, who was named Saturday to oversee the federal oil-spill response, said the worst fear was that the Deepwater well could leak at 100,000 barrels a day if the well head were to break. Industry experts said the well pipe appeared to be crimped, curbing the potential leak rate.

Adm. Allen said three leaks have been found at the well, adding that the U.S. government and BP needed to "fight this thing offshore" before the slick reached the wetlands. He said this was currently being done "remotely" with robotic tools, until a relief well could be drilled.

The spill is one of the most "asymmetrical, anomalous, and one of the most complex things we've ever dealt with," he said.

On Sunday, President Ba-

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PAGE TWO

Even if bailout ends contagion, euroland will be forever changed

[Agenda]

By Irwin Stelzer

The future course of events in euroland is now more or less clear. The International Monetary Fund and Greece's euroland colleagues will come to the aid of Greece to the tune of a bit more than €100 billion ($132 billion), but it remains more rather than less likely that there will be some sort of restructuring, with creditors probably taking a haircut—a.k.a. a loss—on the order of 30%. German officials are so frightened of a euro-zone-wide meltdown—and the possibility of deep losses for its banks that have lent generously to Greece—that they are prepared to ignore their voters who, by 57% to 33% (10% don't know), oppose aid. In the future, says Germany's Angela Merkel, miscreants should be hit with sanctions. The words "moral hazard" apparently weren't mentioned.

It is difficult to tell just how effective the Greece bailout will be in stemming the contagion spreading to other euroland countries. There are too many *if*s. Spain's debt-to-GDP ratio is only about half that of Greece's, and it might escape further downgrading of its debt *if* its socialist government can be frightened out of its lethargy. But with president José Luis Rodríguez Zapatero insisting the worst is over, stasis is more likely than action. Italy tapped the bond markets for €6.5 billion last week, and found investors relatively eager to buy its IOUs at rates below those on outstanding debt. *If* it can stick with the spending cuts engineered by finance minister Giulio Tremonti, and bring down its deficit, running at 5.2% of GDP (Greece's is 13.6%), Italy might avoid a downgrade. Portugal has tightened and accelerated its austerity program, and might avoid a further downgrade *if* it follows through. Ireland's economic-stabilization program and its recapitalization of its banks are deemed to be working, and *if* the Irish continue to remain on their couches and in their pubs rather than take to the streets, the flow of red ink might abate before the nation's debt level becomes unmanageable. And *if* British voters put a deficit-cutting government in place on Thursday, the nation might avoid losing its triple-A rating.

Greece's finance minister outlines the rescue package in Athens on Sunday.

It is difficult to tell just how effective the Greece bailout will be in stemming the contagion.

Even if all of these *if*s come to pass, the world will not return to any semblance of its pre-crisis condition. The days of national fiscal-policy determination are over in Europe. EU President Herman Van Rompuy is calling for the creation of an "economic government" run from Brussels, and European Commission chief José Barroso claims the Lisbon Treaty gives him the power of "economic management." National sovereignty takes another hit, courtesy of the Greece crisis and the ever-ready eurocracy.

Also changed forever is the standard by which sovereign debt will be judged. The rating agencies are under pressure to be less generous in rating debt instruments, and not only those issued by euroland governments. In the U.S., these agencies gave their coveted triple-A rating to the securities that **Goldman Sachs** is accused of unethically, or perhaps illegally, flogging to knowledgeable investors. In Europe, the agencies are accused of delaying too long in reconsidering their ratings of the bonds of euroland's periphery countries, and ignoring the effect on sounder economies of their link to shakier ones.

The rating agencies now know that the Greek bailout means euro-area nations are indeed their brothers' keepers, which in practice means that every country's debt is on every other country's balance sheet. Germany and France can no longer argue that the relevant fact is that their own finances are sound, now that they are assuming responsibility for the debts of Greece and other countries, and will have to bail out their own banks if loans made to Greek, Portugal, Spain and perhaps others are not repaid in full. British voters, their nation brought to its knees by excessive government spending, might temper their harsh judgment of Gordon Brown by recalling that as chancellor he prevented Tony Blair and Peter Mandelson from consigning sterling to the fate of the deutsche mark by adopting the euro.

The more skinflinty rating agencies will also have to take into account the condition of private-sector institutions or government agencies that might look to the government if trouble strikes. A troubled bank that can turn to the government should have its woes reflected on that government's balance sheet, as should U.S. states that Washington won't allow to go broke. In the private sector, the day when off-balance sheet obligations were ignored are over, or almost so.

With this new, consolidated approach to the appraisal of credit-worthiness comes greater knowledge by investors of the real risks, and with greater knowledge will come a demand for higher interest rates.

Time to dust off those forecasting models and plug in those higher rates when guessing at future growth.

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

What's News

■ **Warren Buffett offered** a vigorous defense of Goldman Sachs at the Berkshire Hathaway annual shareholders meeting. Separately, Berkshire recorded a first-quarter profit of $3.6 billion. **17**

■ **Norway's Norsk Hydro** agreed to buy an aluminum mine and operations in Brazil from Vale in a deal the firms valued at $4.9 billion. **19**

■ **Government-bond yields** are likely to keep rising for all but the healthiest borrowers, even if the deal to bail out Greece keeps its financial troubles from spreading. **17**

■ **The Conservative Party** extended its lead in opinion polls ahead of Thursday's U.K. vote, but the Tories still face a fight to win a clear parliamentary majority. **4**

■ **A failed car bomb** smoked, popped and shut down New York's Times Square, causing panic, evacuations and confusion Saturday evening. Most streets reopened Sunday. **8**

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Andy Murray bristles at criticism of his defensive game. **28**

ONLINE TODAY

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5. Latin America Frets Over Spain

Iain Martin on Politics

blogs.wsj.com/iainmartin

"Whichever person ends up in power, just try and leave the place better than you found it."

Iain Martin on the lessons that can be drawn from Labour's 13 years in power

Continuing coverage

See complete coverage of Greece's bailout, including analysis, charts and video, at **wsj.com/greekdebt**

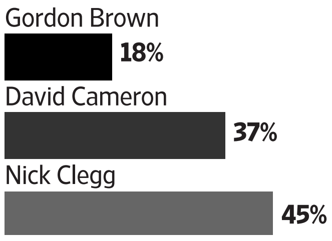
Question of the day

Vote and discuss: Do you expect Goldman shares to fare worse next month?

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

Previous results

Q: Who won the final U.K. party leaders debate?



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NEWS

A subdued Obama still gets laughs

By John D. McKinnon

Reuters

U.S. President Barack Obama's standup routine got big laughs at the Correspondents' Association dinner on Saturday.

WASHINGTON—After a year of tough political sledding, President Barack Obama struck a more subdued tone in his standup comedy routine at Saturday's White House Correspondents' Association dinner.

It was still funny.

"It's been quite a year since I've spoken here last," he began. There have been "lots of ups lots of downs—except for my approval ratings, which have just gone down."

Still, he insisted the dropoff doesn't bother him, because his ratings remain "very high in the country of my birth"—a teasing dig at so-called birthers who still question whether he was born in the U.S.

At another point, Mr. Obama conceded that "obviously I've learned this year [that] politics can be a tough business."

Mr. Obama tried to balance the humor of the occasion with the seriousness of real-world events. He went to Louisiana Sunday to examine the extent of the huge Gulf Coast oil spill, and he said he was "mindful" of Americans serving in the continuing conflicts in Iraq and Afghanistan. He ended with a frustrated dig at the political process, saying he wanted to present the gathered journalists with a bipartisan resolution honoring their work, "but unfortunately I couldn't break the filibuster." Still, he added that "there are times when you can't help but laugh."

As Obama did at the 2009 dinner, he took aim at some of his favorite targets with sharply honed sarcasm. Tops among them this year was his blunt-speaking vice president, Joe Biden, who drew ridicule for whispering to Mr. Obama that the health-care bill the president was about to sign was a "big f—deal." The White House Correspondents' annual dinner, Mr. Biden told him, was "a big f— meal," the president said.

Recalling a congressman's account of being accosted by a naked Rahm Emanuel, White House chief of staff, in a shower at the gym, Mr. Obama said: "Welcome to my world! ... It's a tense moment."

Mr. Obama also spoofed senior White House adviser David Axelrod, not renowned for his devotion to physical fitness. Mr. Obama suggested that Mr. Axelrod recently did a "salacious" nude photo spread for a Krispy Kreme catalog.

The president added a few new targets this year, including **Goldman Sachs Group** Inc., under scrutiny for its practices in the runup to the financial crisis. "All of the jokes tonight are brought to you by our friends at Goldman Sachs," Obama said. "They make money whether you laugh or not."

As for Jay Leno, who followed Mr. Obama as the headliner, the president said he was glad he wasn't speaking after Mr. Leno. "We've seen what happens when someone takes the time slot after Leno's," Mr. Obama said.

He had a not-too-subtle warning for tween heartthrobs the Jonas Brothers. While first daughters Sasha and Malia are big fans, Mr. Obama said: "Boys, don't get any ideas...I have two words for you, `predator drones.' You will never see it coming."

Mr. Obama, who won the Nobel Peace Prize this year, also took a few digs at himself, suggesting he was disappointed that he hadn't won a Nobel for physics.

As for his sweeping health-care legislation—which appeared to cost him significantly in polls—he suggested there were "like, hundreds" of secret provisions. One would provide coverage for his potential 2012 rival, Mitt Romney, for temporary lapses in memory about his record on Massachusetts health-care legislation, Mr. Obama said.

The president also took his accustomed digs at the media, including favorite target Fox News. This time he added a shot at more liberal cable channel MSNBC. At one point he suggested MSNBC had hailed him for pitching a no-hitter when he threw out the first pitch at the Washington National's first game. Fox, by contrast, accused him of pandering to the extreme left wing of the batter's box. News Corp. owns both Fox and The Wall Street Journal.

Oil spill threatens coast

Continued from first page

rack Obama arrived in Louisiana for a first-hand look at the damage.

The National Oceanic and Atmospheric Administration is closing commercial and recreational fishing from Louisiana to parts of the Florida Panhandle because of the oil spill, the Associated Press reported. In a news release sent Sunday afternoon, NOAA says the closure begins immediately and will last for at least 10 days.

NOAA Administrator Jane Lubchenco says government scientists are taking samples from the waters near the spill to determine whether there is any danger.

The fishing ban extends between Louisiana state waters at the mouth of the Mississippi River to waters off Florida's Pensacola Bay.

Officials are considering an increasing variety of techniques to deal with the gusher of oil flowing up from the sea floor a mile below the surface. Adm. Allen said officials were looking into the possibility of adjusting dams to increase the flow from rivers draining into the Alabama's Mobile Bay and then into the Gulf. The hope would be, he said, that the currents would keep the oil slick at bay.

Industry experts on Friday said that based on satellite images and standard measuring indexes, the spill rate was an estimated 20,000 to 25,000 barrels a day.

Asked on ABC News's "This Week" if the 25,000 barrel a day figure was accurate, Lamar McKay, head of BP America, said he didn't know the actual volume. "Estimates of how much oil is coming out are very difficult because you can't measure in any way accurately."

Mr. Salazar said he believed BP could stop the leak, but he feared that it could take 90 days to do so. BP is placing a new rig over the leak and will soon attempt to use drilling tools to close it.

If the 25,000 barrel-a-day estimate is accurate and the leak lasts for 90 days, that would total 2.25 million barrels, or 94.5 million gallons.

Ms. Napolitano on Sunday dismissed suggestions that the U.S. had relied too much on BP's assessment of the oil-leak potential. She said the Coast Guard and other government agencies had moved quickly in the wake of the explosion, and were already deploying vessels and booms for a possible cleanup as they carried out the initial search and rescue mission for missing workers.

The fact that the oil is gushing out of a well 5,000 feet underwater makes it monumentally difficult to clean up. The amount of oil pouring into the water far surpasses what was originally estimated. And because the crude is spilling from an oilfield, rather than from a tanker's hull, the gusher is, for practical purposes, potentially endless. It won't stop flowing until the underwater leak is capped.

To top it all off, the weather won't cut the cleanup effort a break. Harsh winds and high waves have been impeding the effectiveness of the more than 200,000 feet of harder booms that have been laid along parts of the coastline in hopes of keeping the oil from washing into the fragile marshes and inlets that form the coastline.

—Ann Zimmerman, Angel Gonzales, Guy Chazan and Jonathan Weisman contributed to this article.

Reuters

Conservative Party leader David Cameron, center, talks to staff at a Tesco supermarket in North Wales on Sunday.

Tories broaden lead

Polling reflects possibility of hung Parliament after Thursday vote

LONDON—The U.K.'s Conservative Party extended its lead in opinion polls ahead of Thursday's hotly contested general election, benefiting from a strong debate performance by party leader David Cameron

*By **Laurence Norman, Alistair MacDonald** and **Paul Hannon***

and a memorable gaffe by Labour Prime Minister Gordon Brown. But even with those advantages, the Tories face a fight to convert their lead into a clear parliamentary majority.

Several weekend polls showed the Conservatives with a solid lead over both the ruling Labour Party, which has been in power for 13 years, and the Liberal Democrats, riding a populist surge ignited by leader Nick Clegg.

The Tory lead in some polls grew from previous surveys, but not by much—perhaps surprising given the uproar that ensued last week when Mr. Brown, on the campaign trail, was forced to backpedal furiously after a live microphone recorded him saying a voter he had just met was "bigoted."

A poll by ICM for the Sunday Telegraph put the Conservatives at 36%, with Labour at 29% and the Liberal Democrats at 27%; a YouGov poll for the Sunday Times put the Conservatives seven points ahead of both other parties at 35%.

A ComRes poll, taken April 30 and May 1 for the Sunday Mirror and Independent on Sunday, gave the Conservatives 38%, Labour 28% and the Liberal Democrats 25%.

Most political observers say a popular vote in that range on Thursday would probably leave the Tories short of a majority of seats, resulting in a so-called hung Parliament.

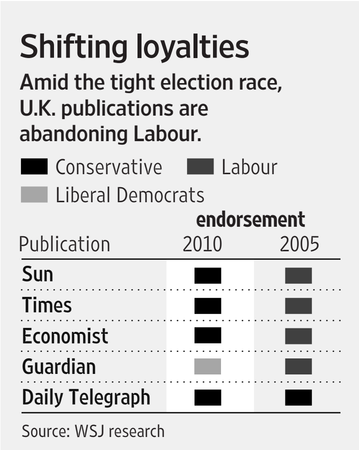
So over the weekend, the candidates began their final sprint to the finish, with the Tories and Liberal Democrats attacking each other and the embattled Mr. Brown facing hecklers and a growing sense of Labour's demise on a campaign swing to the northeast.

Mr. Cameron—who many saw as the winner of the U.K.'s final election debate on Thursday—headed to the southwest on Sunday, a crucial region where the Conservatives are fighting to win seats from the Liberal Democrats.

Speaking in Newquay, he urged still-undecided voters to embrace a clear change.

Mr. Clegg, meanwhile, appeared to make a pitch for disaffected Labour voters.

Mr. Brown campaigned in northeast England, a traditional Labour stronghold—underscoring the fact that Labour, which could face its worst electoral showing in decades, is working to hang on to its base.



Debt concerns reach the U.K.

By Neil Shah
And David Crawford

Sovereign-debt concerns rippling through the euro-zone have started to reach across the English Channel.

In the wake of Greece's fiscal nightmare, ratings agencies moved last week to downgrade ratings on Portugal and Spain. That, in turn, has prompted analysts to re-examine the durability of the U.K.'s top-notch AAA rating.

The U.K.'s budget deficit, at nearly 12% of gross domestic product, rivals Greece's. Its national debt load, at 70% of GDP, is rising.

By most market measures, however, investors appear unconcerned. Long-term government-bond yields remain historically low. Costs of credit-default insurance, a measure of investors' confidence in a country's ability to meet its debt obligations, are close to where they started the year.

Ratings agencies have warned that Britain could lose its AAA rating if a new government doesn't quickly come up with a tough, credible program for cutting the budget deficit. With a tight national election set for late this week, the scope of the U.K.'s fiscal problems will start to get more attention.

Labour Party Prime Minister Gordon Brown, Conservative leader David Cameron and Liberal Democratic leader Nick Clegg have all acknowledged the need to tackle the fiscal problems. But U.K. commentators say details have remained scant. Mr. Cameron has pledged to move more quickly on deficit reduction than Mr. Brown, but none of the three leaders have said much about how they would get control over the fiscal situation.

Analysts at Goldman Sachs Group last week compared the U.K.'s fiscal challenges with those of Spain, emphasizing that the British fiscal issues will receive more scrutiny after the election.

Tories walk line on banking rules

By David Enrich
And Alistair MacDonald

The U.K.'s Conservatives are bashing banks in public. Behind the scenes, though, they are striking a more conciliatory tone with London's financial community.

George Osborne, the Conservatives' candidate to become Chancellor of the Exchequer, has been reaching out to top U.K. bankers to assure them that, despite the party's populist rhetoric, a Conservative government won't declare war on banks, according to people who have heard his pitch.

All three major parties have had to walk a fine line with the U.K.'s powerful financial community during this intensely tight campaign, which culminates in national elections on Thursday.

While the Labour party has decried excessive banker bonuses, it also had to oversee such payouts for employees of state-owned **Royal Bank of Scotland Group** PLC. Moreover, Labour has long enjoyed a chummy relationship with the City of London and championed the now derided "light-touch" regulatory approach.

The Liberal Democrats, perhaps the most vocal critic of London's financial community, have at least three "shadow ministers" who worked in the banking industry and the party received funding from the heads of large London hedge funds.

But the Tories have historically had a tighter relationship with the City of London than the other major parties, and that is seen as a potential vulnerability in an election where bankers have become the bad guys.

Thus, the Conservatives have sought to establish their populist bona fides with strong words. In Thursday's televised debate, Tory leader David Cameron assailed "appalling bonuses" and blasted Labour for being too cozy with the financial industry. "They did very much hitch the whole fortunes of the economy to the City of London," Mr. Cameron said.

Given the potency of the rhetoric, Mr. Osborne lately has tried to mend fences with bankers after lambasting them in public, according to people familiar with the matter. In a televised debate last month, for example, Mr. Osborne lashed out at **Barclays** PLC President Bob Diamond.

"It really beggars belief that two years after we all bailed them out, we get the Barclays Bank chief paying himself £63 million [$96.2 million]," Mr. Osborne said.

When Barclays officials called Mr. Osborne's office to complain that the £63 million figure was inaccurate, Mr. Osborne relayed an apology to Barclays, according to people familiar with the matter.

A person familiar with Tory thinking said Mr. Osborne is being consistent with his public and private remarks.

All the same, people in the City say Mr. Osborne's quiet outreach efforts have been frequent. For instance, in phone conversations and private meetings, senior banking executives say Mr. Osborne has tried to allay their concerns that a Tory government would try to force giant banks to shed their investment banking and trading divisions.

Banking on new rules

Where the U.K.'s three major parties stand on banking policy

Labour

- push for global consensus on bank tax
- advocate tougher international capital and liquidity rules

Conservatives

- move bank supervision to Bank of England from FSA
- push for global rules restricting risky activities by retail banks
- impose tax on bank liabilities

Liberal Democrats

- require separation of investment banks from deposit-taking retail banks
- impose tax on bank profits
- set new lending requirements for partly nationalized banks

Mr. Osborne's assurances come even as the Conservatives publicly back international rules that would restrict risky banking activities. Mr. Cameron reiterated Thursday that retail banks "should not be behaving like casinos" and endorsed the Obama administration's proposal to separate proprietary trading from traditional banks. Such rules could force major U.K. banks to rein in or divest their investment-banking divisions.

Last October, the Bank of England's governor, Mervyn King, delivered a speech in which he advocated separating high-risk activities from retail banking. Mr. Osborne applauded the remarks as "powerful and persuasive."

Further aligning the Conservatives with Mr. King, the party's platform calls for the Bank of England to gain control over supervising the U.K. banking industry, a duty now held by the Financial Services Authority.

The Conservatives' tough talk has alienated some traditional supporters. Last year, for example, Jon Moulton, a private equity fund manager and former Conservative donor, said that while a degree of "banker bashing" was justified, the Tory attack is "merely opportunistic" and could damage the City's long-term prospects.

When bankers have phoned Mr. Osborne to seek clarification about his views on splitting banks' retail and trading businesses, people familiar with the matter say he has tried to ease their concerns and said the Conservatives have no intention of breaking up giant banks.

"They've said, 'We've got an election to win. Things will be said in the heat of an election. We believe it's a good thing for the economy that we have strong, profitable banks','' said a person who has heard Mr. Osborne's remarks.

The person familiar with the Tories' thinking stressed that the Tories have never advocated a wholesale breakup of big banks.

Mr. Osborne also has sought to quell concerns that Mr. King's support for forcing banks to shrink would become official Bank of England policy, according to people familiar with the matter.

EUROPE NEWS

Merkel's regional dilemma

German chancellor's coalition appears headed for defeat in North Rhine-Westphalia vote

By Marcus Walker
And Patrick McGroarty

BERLIN—German Chancellor Angela Merkel has managed so far to limit the political backlash in Germany against the Greek bailout. The bad news for Ms. Merkel: Her coalition is nonetheless heading for defeat in crucial regional elections.

The chancellor's center-right alliance is likely to lose power in Germany's most populous state, North Rhine-Westphalia, in elections on May 9, opinion polls show. Defeat would cost her conservative-led government its majority in Germany's upper house of parliament, which represents the country's 16 states, making it harder for Ms. Merkel to push through reforms.

Fear of a voter backlash had been one factor in Ms. Merkel's reluctance to offer financial assistance to Greece, until financial-market panic forced Germany's hand, according to critics, including some other EU governments, which wanted earlier action on Greece. (Ms. Merkel's aides deny any connection between Greece and the regional election.)

Although a majority of Germans oppose aid for Athens, according to opinion polls, analysts say the Greek crisis isn't playing a significant role in the North Rhine-Westphalian election. The region's nearly 18 million residents care more about local issues such as education and jobs, surveys show.

"It is not yet evident that Greece is an important topic for voters" in the region, says Manfred Güllner, head of opinion-polling institute Forsa. That may be partly because Ms. Merkel's tough stand on aid for Greece has left opposition parties with little way to exploit the issue, other analysts say.

North Rhine-Westphalia is home to Germany's industrial heartland, the Ruhr valley area, and has traditionally been a bastion of the left-leaning Social Democrats. The state's conquest in 2005 by Ms. Merkel's conservative Christian Democratic Union was a coup for the party and was soon followed by her election as national leader.

For many voters today, however, the state election is a referendum on the patchy overall performance of Ms. Merkel's federal government, composed of Christian Democrats and the pro-business Free Democratic Party, which together won national elections last October.

"I think voters' greatest dissatisfaction is that the government doesn't work clearly and definitively," says Nils Diederich, a political scientist at Berlin's Free University. "That will certainly carry over to North Rhine-Westphalia."

The stakes are high. The current CDU-FDP administration in North Rhine-Westphalia mirrors Ms. Merkel's own in Berlin. If the coalition loses the state as opinion polls indicate, Ms. Merkel's ability to push through major policies including tax cuts and a health-insurance overhaul would be curtailed.

A Forsa opinion poll released April 28 puts the CDU's support at 39% and the FDP's at 7% in North Rhine-Westphalia, leaving the two allies behind a potential coalition of left-leaning parties.

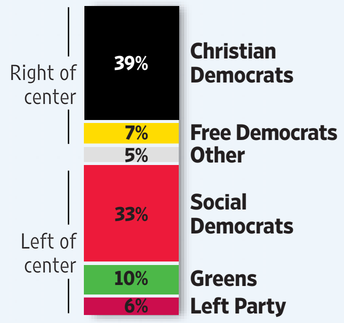
If the two center-right parties fall short of a majority in the state legislature, the CDU might hold on to power by teaming up with the left-leaning Greens or Social Democrats. In such an ideologically diverse coalition, the CDU would have to compromise on many issues, including tax cuts. As a result, Ms. Merkel wouldn't be able to count on the state government to support her national policies, analysts say.

The latest blow to the center-right is a campaign-finance scandal. A CDU official acknowledged over the weekend that the party may have broken party-funding rules in the state's last election in 2005, when the CDU, according to allegations in German media, financed a supposedly independent grass-roots campaign group. The extent of the rule-breaking remains unclear, but the affair could embarrass state Premier Jürgen Rüttgers of the CDU just as he tries to save his administration.

Education has been the election's central issue, with the left-leaning parties calling for an overhaul of Germany's school system, which critics say puts students from poor and immigrant backgrounds at a disadvantage. Other leading issues in the campaign include the parlous state of municipal finances and how long to operate the region's nuclear power plants. Greece, in contrast, hardly got a mention when Mr. Rüttgers and Hannelore Kraft, the Social Democrats' regional head, clashed in a TV debate last week.

Right behind

Germany's center-right trails left-leaning parties ahead of May 9 elections in North Rhine-Westphalia



Note: 1,004 people were surveyed from April 19-23. Average margin of error: 2.5%
Source: Forsa/Stern

Pope to overhaul key order

Legion of Christ revamp comes in wake of investigation into cover-ups of sexual abuse

By Stacey Meichtry
And José De Córdoba

VATICAN CITY—Pope Benedict XVI will overhaul the Legion of Christ, one of the most powerful orders in Roman Catholicism, in the wake of a Vatican investigation into decades of cover-ups inside the order that allowed its founder to sexually abuse seminarians and father at least one child.

In a statement Saturday, the Vatican announced plans for Benedict XVI to appoint a special envoy and set up a commission to restructure the Legion.

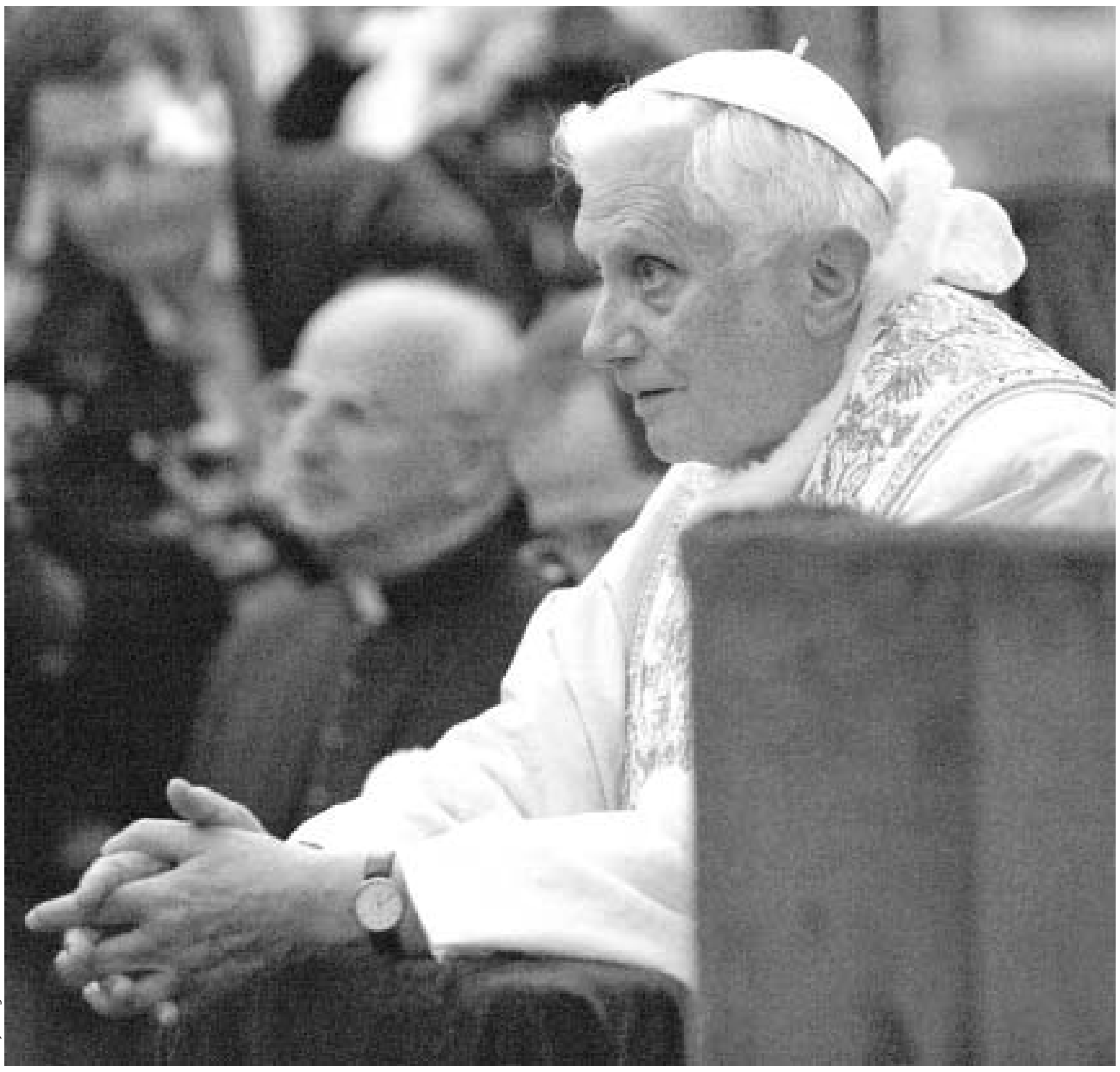
The commission, the Vatican said, will rewrite the order's statutes and redefine the military-like culture, which led its members to maintain a code of secrecy in the face of sexual abuse committed by its late founder Rev. Marcial Maciel Degollado.

"The conduct of Father Marcial Maciel Degollado had consequences in the life and the structure of the Legion that are so serious as to require a journey of profound revision," the Vatican said.

Father Maciel, who died in 2008, had always denied the allegations of sexual abuse. The Legion, which defended the founder for years, repudiated Father Maciel last month and apologized to his victims. "The Legionaries thank the Holy Father and embrace his provisions with faith and obedience," the Legion said in a statement posted on its Web site Saturday.

In an email responding to an interview request, Luis Garza, the Legion's No. 2 official, said: "For the moment, we will have to wait a bit to have the context and full knowledge of everything."

The overhaul of the Legion comes as Benedict XVI is under intense pressure to show his willingness to crack down on sexual abuse in the highest ranks of Catholicism.



Getty Images

Pope Benedict XVI in Turin on Sunday, visiting the famous shroud believed to be Christ's burial cloth.

Over the years, Benedict XVI has stripped many sexually abusive priests of their ministry and met with victims in the U.S., Australia and Malta.

Benedict XVI, who visited the Shroud of Turin Sunday, will meet with bishops from Belgium this week to discuss their response to the sex-abuse crisis, the Associated Press reported.

The Legion has some 800 priests and 2,500 seminarians operating universities and schools in more than 20 countries from Brazil to Chile and Spain.

Greece reaches agreement on bailout

Continued from first page

of searing measures to cut Greece's budget gap. The government will slash public-sector wages, raise sin taxes, increase value-added taxes, impose a new levy on businesses, cut pension payments and raise retirement ages for some public-sector workers.

The IMF's portion of the Greek program represents the largest financial commitment the IMF has ever made to a single country and returns the fund to the days when it imposed not only sharp austerity measures but steep changes in the structure of a country's economy.

"It's an unprecedented program in terms of the adjustment" required of a recipient country, said Poul Thomsen, the IMF's mission chief for Greece.

IMF Managing Director Dominique Strauss-Kahn said the three-year program aims to "correct Greece's grave fiscal imbalances, make the economy more competitive and—over time—restore growth and jobs." He said the plan's requirements, "along with the government's firm commitment to implement them, will get the economy back on track and restore market confidence."

Mr. Thomsen said there is a sense from government and opposition leaders "that this is a defining moment for Greece....There's a clear understanding in the political elite that one should be careful not to play politics with this issue," he said.

Whether that will turn out to be the case once the pain of the cuts hits Greek society is far from clear. In the past, the IMF has often played the role of political whipping boy, turning itself into a symbol of austerity that politicians and opposition leaders can attack—while making the required adjustments.

The new, more drastic measures have whipped up an already angry populace. In Athens on Saturday, tens of thousands joined a giant May Day protest in anticipation of the aid deal. Rioters threw Molotov cocktails at police, and marchers chanted "get out to the IMF and the European junta." Union leaders said on Sunday they will renew protests this week, and a widespread general strike is set for Wednesday.

Still, the weekend deal puts a giant check within Greece's grasp. Approval by the 16 euro-zone leaders is needed, but their finance ministers have signed off, so it is all but a formality. That is expected to be accomplished at an emergency meeting on Friday.

Several countries, most notably Germany, which will take on the largest part of the EU loans, must now put the bailout measure through their parliaments. German Chancellor Angela Merkel has put the legislation on a fast track to approval by the end of the week. Parliamentary approval isn't likely to be a serious obstacle.

Greece's profligacy and the reaction of the capital markets that financed its deficit spending forced the EU's hand. The push to ink a bailout deal comes after a turbulent week in the markets that included a downgrade of Greece's debt—all but forcing Greece to move fast on a bailout and swallow the deep fiscal cuts that will come with it.

Atop European leaders' list of worries is the effect of Greece's crisis on other fiscally precarious EU countries. Last week, investors shunned the debt of Portugal and Spain, in a dangerous sign that the credit spigot could tighten for others with debt and deficit problems—and potentially vastly raise the bailout tab for Europe's healthier nations. Downgrades last week of the Iberian countries' credit ratings heightened those concerns.

The bailout has been percolating since February, when euro-zone leaders said, vaguely, that they would come to Greece's aid if needed. It has taken form drip-by-drip over the past months in the EU's glacial, decentralized decision-making process.

The aid deal has been a political struggle in Europe. A bailout is distinctly against the spirit of the euro zone, which was designed to be a common currency union with purely national fiscal management. The bloc set rules to enforce spending discipline but has been unable to make them stick.

Grim milestone is set in Spain as jobless rate exceeds 20%

By Jonathan House

MADRID—Spain's unemployment rate breached 20% in the first quarter as the country's ailing economy, reeling from the collapse of a decadelong construction boom, continued to shed jobs, Spain's National Statistics Institute said.

The INE said first-quarter unemployment rose to 20.05% from 18.83% in last year's fourth quarter, confirming leaked data published by a Spanish newspaper last week.

Spain's first-quarter unemployment rate is the highest in the developed world. It is Spain's highest since 1997 and it surpasses government predictions, which had forecast a 19% unemployment rate at the end of this year.

Since the onset of the global financial crisis in 2007 precipitated the collapse of its credit-driven economic-growth model, Spain's economy has been shedding jobs as rapidly as it created them in the previous boom years. Euro membership in 1999 ushered in an era of historically cheap credit for Spain and spawned a massive building boom.

The INE said 4.6 million people were unemployed in Spain in the first quarter, while 1.3 million households had no working members. The agency said nearly 700,000 jobs had been lost over the past year.

Raj Badiani, economist at IHS Global Insight, said he expects the economy to keep shedding jobs throughout this year as housing investment remains depressed and industrial and service companies attempt to contain costs "in the context of still-squeezed margins [and] the prospect of a labored recovery in domestic demand."

The Spanish economy has contracted for six consecutive quarters. The first-quarter unemployment report adds pressure to a government reeling from a debt-rating downgrade last week from Standard & Poor's and a sharp rise in financing costs for euro-zone sovereign debt from countries with large budget deficits and low growth prospects.

The government has promised an overhaul of labor rules that would reduce Spain's costs for hiring and firing, one of the key factors behind the country's historically high unemployment rate, economists say. Spain has also been an outspoken advocate of a quick agreement on a support package for Greece, which it hopes will contain the euro-zone debt crisis.

Across the euro zone, the unemployment rate hovered at an 11.5-year high, logging in at 10% in March, figures from the European Union's Eurostat agency showed.

The number of unemployed people posted its biggest monthly increase for six months in a sign that companies remain under pressure. Some 101,000 people joined unemployment queues in March, the largest monthly increase since September, Eurostat said.

The sharp increase suggests companies across the bloc are suffering after recovery stalled in the fourth quarter. With so many out of work, the data also suggest that retail sales won't bounce back quickly, leaving the recovery dependent on foreign demand for exports.

Wildlife threats often linger for years

Researchers say hydrocarbons evaporate in air, but intertidal zones, sediment are at risk; 'long-term consequences'

By Robert Lee Hotz

Driven deep into Gulf Coast waterways by wind and seasonally high tides, the spreading oil slick from the Deepwater Horizon accident could cause serious ecological and wildlife-health consequences long after signs of surface damage have been erased.

Independent studies of several major oil spills, including the 1989 Exxon Valdez accident, show that oil often reaches farther into tidal estuaries than previously thought and can soak into shoreline sediment where it can continue to affect fish and wildlife for 10 or 20 years.

To some extent, the Gulf of Mexico is naturally awash with oil seeping from seafloor sediment.

In the aftermath of offshore oil spills in Alaska, Massachusetts and Spain, researchers discovered long-term effects on shellfish, crabs, seabirds, whales and sea otters years after the accidents. The problems ranged from altered blood chemistry and higher levels of stress hormones to erratic behavior, contaminated eggs and long-term population declines.

"Everyone assumes all the bad stuff happens immediately after a spill and that things get progressively better," said wildlife biologist Dan Esler at Simon Fraser University in British Columbia. "There are long-term consequences."

Since the Exxon Valdez spill—one of the most intensively studied marine oil incidents in history, Dr. Esler has tracked the long-term effects of the spill among wildlife in Alaska's Prince William Sound. Last month, he reported genetic evidence showing that the harlequin ducks there are still exposed to oil.

He cautioned that exposure didn't by itself prove any adverse effect. "We can safely say that oil is not good for you, but how bad it is at the levels they are encountering, we can't say," he said.

Other follow-up studies have shown that, a decade after the spill, fish in the original spill zone still were being exposed to hydrocarbons, while 17 seabird species had yet to recover.

The National Marine Fisheries Service still lists seven species of oysters, clams, ducks and killer whales as recovering from the oil spill. Two species of herring and salmon have shown no signs of recovery even after 20 years.

As long as the underwater well in the Gulf of Mexico continues to spew oil, oil will wash into estuaries on every tidal cycle, building up successive layers of silt and oil along the shoreline. The salt marshes and beaches are home to thousands of nesting waterfowl and a rest stop for millions of migrating birds.

Emergency workers continued Friday to set up protective barriers around the most vulnerable coastal regions, but the area's salt marshes and other wildlife refuges are difficult to sequester. And researchers said mangrove swamps, seagrass shallows and marshes are so fragile that any effort to clean them up would do additional damage.

To some extent, the Gulf of Mexico is naturally awash with oil seeping from seafloor sediment.

In the early 1990s, researchers discovered more than 600 areas where oil naturally leaks into the Gulf from undersea reservoirs. Based on satellite and radar surveys, the researchers estimated that this natural leakage amounted every year to twice the amount of the Exxon Valdez spill, which was about 260,000 barrels.

Last year, researchers at Woods Hole Oceanographic Institution in Massachusetts and the University of California calculated that natural oil seeps off Santa Barbara, Calif., had leaked 20 tons to 25 tons of oil every day for thousands of years. Almost all of it had been naturally contained in seafloor sediment.

Associated Press

Dr. Erica Miller treats a Northern Gannet covered in oil from the spill at a facility in Fort Jackson, La., Friday.

But the concentrated spillage from the Deepwater Horizon well overwhelms the natural background levels, researchers said, and the oil will be carried into more vulnerable intertidal zones. "The oil will come in on the tide and penetrate as far as the tide penetrates," said marine ecologist Charles Peterson at the University of North Carolina in Chapel Hill.

Exposed to the air, the lighter hydrocarbons in crude oil, such as benzene, toluene, xylene and ethylene, evaporate quickly, researchers said. But the heavier carbon compounds, called polycyclic aromatic hydrocarbons, can persist at toxic levels in sediment for years, isolated from the sunlight and bacteria that ordinarily would break these chemicals down. The oil traces can contaminate fish and animals' food, impair their ability to breed successfully and even alter their natural behavior. Fiddler crabs, for example, in oil-soaked areas stagger and "act like drunken sailors," Dr. Peterson said.

"These are areas where the oil can come to rest and retrain its toxicity and cause longer-term chronic effects," Dr. Peterson said, "not killing wildlife outright in some spasm of agony—but affecting their fitness, health and growth."

Investment by U.S. companies is robust

By Mark Whitehouse

U.S. companies from industrial giant **Caterpillar** Inc. to apparel maker **Guess** Inc. are plowing money back into their businesses at a rate that demonstrates growing confidence in the economy's recovery, but still leaves questions about its strength.

The Commerce Department reported Friday that private investment in equipment and software, everything from machine tools to word-processing programs, rose at a robust annualized rate of 13.4% in the first quarter of 2010, adjusted for inflation.

That was the third straight quarter of growth since the economy hit bottom in mid-2009, but slower than the 19% pace of the previous quarter.

Business investment overall, including money spent on warehouses and office buildings, grew at an inflation-adjusted annualized rate of 4.1%, dragged down by the persistent slump in commercial real estate.

Among the bright spots: Building of mining structures such as natural-gas rigs rose 43.8%.

The increased spending on equipment and software encouraged hopes that businesses will help lead the economic recovery, generating enough investment and jobs to sustain a recent resurgence in consumer spending.

So far, though, it is falling well short of the pace needed to drive the kind of sharp, "V-shaped" recovery that has followed deep recessions in the past.

Together with rising exports, the business investment "is enough to generate a sustainable recovery, but not enough to generate a V," said Nigel Gault, chief U.S. economist at consultancy IHS Global Insight.

In the first four quarters after the harsh recession of 1981-82, inflation-adjusted investment in equipment and software rocketed back at an average annualized rate of 21%, helping to drive nearly 8% growth in the broader economy.

On average, economists expect the U.S. to grow at an inflation-adjusted rate of 3.1% in 2010.

Most business surveys show optimism rising and many companies planning to boost capital expenditures further in coming months.

But disparities remain.

On average, economists expect the U.S. to grow at an inflation-adjusted rate of 3.1% in 2010. Most business surveys show optimism rising.

Large companies that export to growing Asian economies, for example, tend to be in better shape than smaller firms, many of which still face lackluster sales and problems getting the credit they need to expand.

At Caterpillar, strong revenue growth in emerging markets is driving an investment revival.

Chief Executive Officer Jim Owens said the company expects to make $1.6 billion of capital expenditures this year, up from $1.35 billion last year, partly to expand its capacity to build mining trucks in Decatur, Ill., for the global market.

The company also aims to add about 9,000 jobs this year, about a third of them in the U.S.

Given the amount of excess capacity in manufacturing, though, Mr. Owens thinks other manufacturers, such as Caterpillar's suppliers, will have to see some more quarters of growth before they follow suit.

"It's going to take a little while before they become believers," he said.

In the retail world, rising sales have added to confidence at apparel maker Guess Inc. Chief Financial Officer Dennis Secor said the company plans to more than double capital expenditures this year, mainly to open 52 new stores in the U.S. and Canada. That's up from only 18 openings last year.

"This is definitely a year of investing for us," Mr. Secor said.

Business investment still has a long way to go to reach normal levels.

In the first quarter of 2010, net private investment—including capital spending on everything from houses to assembly lines, minus depreciation—stood at 1.6% of economic output, well below the 20-year average of 5.4%.Meanwhile, the smaller firms that tend to account for an outsize share of job growth are facing serious obstacles. Rochelle Balch, CEO of Phoenix-based information-technology consultancy RB Balch & Associates, said her bank closed her $150,000 credit line earlier this year, just as her company was recovering from the recession.

The lack of credit, she said, is hampering her plans to add two or three employees this year to the nine she already has—despite the fact that business is up as her small-business customers look to make purchases of new servers and other equipment they had been putting off.

The banks are "gun shy," she said. "They don't want to loan to us little guys."

U.S. NEWS

Bomb attempt closes Times Square

Failed car bomb made of propane, gasoline and fireworks started smoking, prompting panic and evacuations

A failed car bomb smoked, popped and shut down Times Square, causing panic, evacuations and confusion Saturday on one of the tourist spot's busiest nights.

By *Joel Stonington, R.M. Schneiderman, Sean Gardiner* and *Ellen Gamerman*

Getty Images

Police guard the perimeter of New York's Times Square on Sunday after the car bomb was disabled.

Most of the streets in the area were reopened Sunday morning, though a heavy police presence remained in the area.

Authorities said a Nissan Pathfinder at West 45th Street and Seventh Avenue was left Saturday night loaded with a bomb made from two clocks, three propane gas tanks, two additional one-gallon gas canisters and fireworks.

"It appeared that [the bomb] was in the process of detonating and malfunctioned," said police spokesman Paul Browne.

A street vendor alerted a policeman on mounted patrol—Wayne Rhatigan, 47 years old, a 19-year-veteran of the force. In an interview, Mr. Rhatigan said he smelled gunpowder coming from the vehicle and went toward it, thinking it could explode at any second. He grabbed two other officers to help move people away from the smoking Pathfinder as he called for backup at 6:34 p.m.

Police blocked the area from West 43rd to 47th streets along Broadway and Seventh Avenue with metal railings. Parts of West 48th Street were also closed. Most of the streets were reopened Sunday morning after police removed the Pathfinder.

Police later said the Pathfinder was spotted on security video at 6:28 p.m. The video wasn't clear enough to identify the driver and no videos have been found showing the suspect in the attack, police said.

"We have no idea who did this or why," said Mayor Michael Bloomberg, alongside Police Commissioner Ray Kelly at a Times Square news conference early Sunday morning.

The mayor called the bomb "amateurish." He added that investigators believed the car's actual owner had nothing to do with the bomb and that the vehicle's Connecticut license plates didn't match the make of the car.

Homeland Security chief Janet Napolitano echoed Mr. Bloomberg's comments, saying Sunday on Fox News that the bomb appeared to be an "amateurish" terrorism attempt.

Ms. Napolitano said the Federal Bureau of Investigation, the Department of Homeland Security and the city of New York were investigating the incident, including examining the car, tracing fingerprints and looking at video from the area around the bomb.

"There are a lot of cameras in that area," she said, adding that there's "a lot of activities in terms of investigation."

Ms. Napolitano said there was no information to suggest that any other sites had been targeted in Saturday's car bomb attempt. Evidence so far suggested this was a "one-off attempt," she said.

Mr. Bloomberg earlier said that no other hazards were found and that "there's no more danger here than in any other city." Further, no credible threats were made by organized groups with regards to the attack, police said.

President Barack Obama had been briefed on the bomb. In a statement, the administration said that the president, who attended an annual dinner for White House news correspondents Saturday night, praised the response by the New York Police Department. The president has also directed his homeland security and counterterrorism adviser, John Brennan, to advise New York officials that the federal government is prepared to provide support, the Associated Press reported.

Street vendor Larry Franklin, 56, said a friend reported a man to police who put keys in the black SUV and walked away. His friend told him smoke began coming out of the back and police rushed to the scene.

"I looked back and boom," said Matthew Fox, 44, a street vendor. "Everyone started running and women started screaming." He said he was "10 blocks away from 9/11 when it happened," but that "this wasn't anything like that."

Nineteen-year-old Ivan Morrison, who was in town from Vermont to see "The Addams Family," said "it sounded like a deeper gun shot."

Police said the bomb parts and an additional locked metal box would be removed to the NYPD Rodman's Neck firing range in the Bronx.

Subway service on many lines also was suspended or delayed. On Broadway, "God of Carnage" and "A Behanding in Spokane" each began 30 minutes late, show officials said. The evening performance of "The Lion King" was performed as scheduled. Early reports erroneously said that the show had been canceled.

Talk-show host Oprah Winfrey attended the musical "Fela!" at the Eugene O'Neill Theatre on West 49th Street, and the production began on time and wasn't interrupted, according to a show spokesman.

At around 8 p.m., Lucy Liu, one of the stars of "God of Carnage," walked toward the police barricade on the corner of 45th Street and Eighth Avenue to ask police officers what had happened.

Hundreds of others did the same. Telecharge and Ticketmaster said they would offer theater-goers tickets for shows midweek, but that didn't appease some tourists.

"I've only got tonight and tomorrow in New York. It's very disappointing," said Annie Monks, 50, visiting from Australia. She was there to see "God of Carnage" but couldn't get in.

Around 9:15, police began letting ticket holders along 46th Street walk toward the theaters. Hotel guests were initially not permitted to enter or leave.

At the Hotel Grace on 45th Street, a clerk said that just before midnight, police began letting guests standing in line outside enter in groups of 10. Enrique Sarasola, 45, the owner of the hotel said guests are permitted to leave, but if they do, they will not be allowed to return until 7 a.m.

Adrienne Smith, 25, of Park Slope, Brooklyn was attending the "Straight for Equality Gala" at the New York Marriott Marquis in Times Square where Liza Minnelli performed.

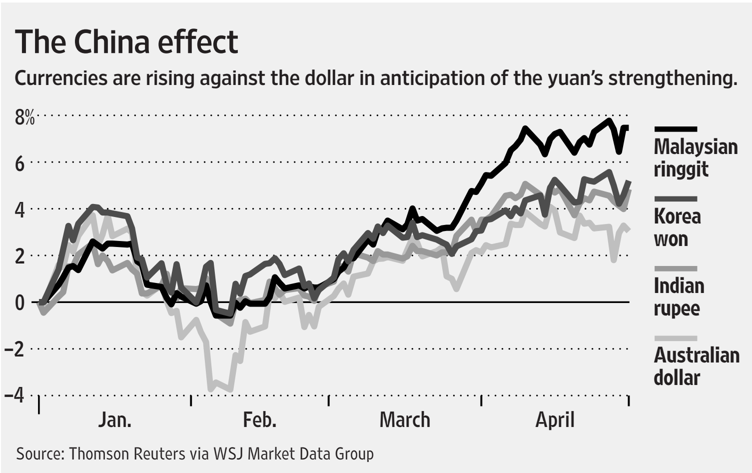
After Ms. Minnelli sang, Ms. Smith and other partygoers gathered at bar on the hotel's ninth floor where they looked out on to the deserted streets of Times Square, which by then had been evacuated. "We were looking at the TKTS booth, and it was completely empty," Ms. Smith said.

By 10:15 pm, the gala organizers alerted the crowd that the police weren't allowing guests to leave with their cars, and Ms. Smith left the hotel shortly after.

By 11 p.m., a clerk at the Paramount Hotel on 46th between 7th and 8th said guests were not allowed to come in or out. Police said guests at the south tower of the Marriott Marquis on 46th and Broadway were moved to the auditorium of the hotel. Repeated calls to the Marriott weren't answered.

—Ian Talley and Joseph De Avila contributed to this article

WORLD NEWS



China's yuan gains in world-wide clout

Traders expect currency to rise against dollar

BY ALEX FRANGOS

A new heavyweight is flexing its muscles in the $3 trillion-a-day market for currency trading: China.

It is an unusual sort of influence given that the Chinese currency, the yuan, doesn't readily trade in foreign-exchange markets and its value is fixed against the dollar.

THE OUTLOOK

Yet China's economy, and speculation that the yuan's value vis-a-vis the dollar will soon be allowed to rise, is moving currencies around the world.

This is especially true in Asia, where the U.S. dollar has long reigned as the most consequential currency. It's also making waves in countries that are major raw-materials suppliers to China such as Australia, Canada and Brazil.

"The U.S. dollar used to be the center of the earth," says David Bloom, currency strategist for HSBC in London. "Now China is becoming a very powerful influence on the way currencies are working."

Speculators, for instance, bet that other Asian currencies, especially those that are more freely traded, will rise relative to the dollar when the yuan is also allowed to.

Investors believe expectations of yuan appreciation give central banks in these countries the leeway to let currencies strengthen without fear of losing export competitiveness. So far this year, the Malaysian ringgit is up 7.5% against the dollar and the Korean won and Indian rupee are both up around 5%.

"We've reached a junction where the dollar and yuan are equally important in Asia," says Hai Xin, head of Asia for Overlay Asset Management, a unit of BNP Paribas Group that hedges currency risk for large investors.

To be sure, the U.S. dollar is still the top dog. It's the most heavily traded currency in the world and still the denomination that investors flee to in tough times.

Some say talk of the yuan's prominence is overblown. "This is a country that has never had a real floating exchange rate and has no experience responding to markets," says Fraser Howie, of CLSA Asia-Pacific markets and a longtime critic of China's financial system.

Even so, China's growing currency clout is showing up indirectly. For instance, derivatives that investors use to bet on the yuan's direction have become popular. And these yuan bets are starting to move other currencies, too.

Deutsche Bank currency strategist Mirza Baig says that on days when trading is especially volatile, the Singapore dollar moves in tandem with the yuan bets. The Malaysian ringgit, Taiwanese dollar and Korean won are also high on the list of currencies affected by the yuan.

The so-called dollar bloc—Australia, Canada and New Zealand, whose currencies have long been considered tied to the value of the U.S. dollar—are more sensitive to China these days as well. A large part of that is China's demand for commodities from those countries.

In theory, the strength of currencies broadly reflects the relative growth rates of underlying economies. China is leading the global recovery, part of the reason many economists, especially in the U.S., think the yuan is undervalued at its current level of 6.83 to the dollar, where it's been since August 2008.

China is by far the largest economy whose currency doesn't float. That's despite China being set to overtake Japan this year as the world's second-largest economy after the U.S.

China's economic output will be more than $5 trillion, or around 9% of the world's economy, according to the International Monetary Fund. The U.S. is a quarter of the world's economy. The euro zone is 20% and Japan is 9%.

The yuan is also becoming a more important currency to the world's central bankers. The lack of movement in the yuan has put pressure on central banks in countries that compete with China for world trade.

As economies recover in Asia and Latin America, some policy makers are reluctant to raise interest rates to fight inflation, for fear the higher rates will also mean stronger local currencies. Strong currencies make their exports more expensive compared with China's

Central banks are key players in currency markets, as they allocate their massive reserves. The dollar is still dominant, making up 62% of the world's central-bank reserves, according to the IMF.

The yuan, which is almost impossible to trade, is many policy changes away from being the kind of currency that risk-averse central bankers want to hold.

But central banks or sovereign wealth funds from Malaysia, Norway and Singapore have received special quotas from the Chinese government to allow them to gain a bit of exposure to China's currency. The bet is that holding yuan-denominated assets is an important feature of a diversified national reserve.

Israel joins Arab League in supporting Mideast talks

Associated Press

JERUSALEM—Israel's prime minister on Sunday welcomed the Arab League's endorsement of indirect, U.S.-brokered peace talks with the Palestinians.

Benjamin Netanyahu's office said the prime minister still awaited a formal Palestinian statement on the resumption of peace talks, but renewed his willingness to restart peace talks "at any time and at any place" while insisting the talks begin "without preconditions."

The Palestinians' executive committee was expected to meet next week to officially announce a resumption of talks. U.S. Secretary of State Hillary Clinton has said the talks will start this week, and U.S. Mideast envoy George Mitchell was expected back in the region.

The previous round of Israeli-Palestinian peace talks broke down in late 2008, reportedly while on the verge of an agreement.

The Palestinians have since refused to sit down with Israel until it agrees to freeze all construction in the West Bank and East Jerusalem—two areas that the Palestinians want for an independent state along with the Gaza Strip.

The indirect talks, with Mr. Mitchell shuttling between the two sides, are seen as a compromise.

Militants seize Somali pirate town

BY ABDINASIR MOHAMED

MOGADISHU, Somalia—Islamic fighters have seized a pirate haven in central Somalia, said residents of the town, in what could be a bid for a slice of the lucrative business of hijacking ships on the high seas.

On Sunday, members of the group Hizbul Islam, driving pickups mounted with heavy guns, moved into the town of Haradheere. As the militants arrived, the pirates fled, piling into Toyota Camrys and Land Cruisers to escape potential clashes.

"We have to leave this town—those who behead people meaninglessly have arrived," said Farah Ganey, a Haradheere pirate, in a telephone interview.

Hizbul Islam and al Shabaab, a separate militant group aligned with al Qaeda, have vowed to cooperate to overthrow Somalia's weak transitional government in Mogadishu, the capital. But the militants also fight with each other over land and resources. Hizbul Islam's takeover of the pirate town could lure retaliatory attacks by al Shabaab fighters.

A spokesman for Hizbul Islam said the groups wanted to capture several more towns in the region, but he declined to comment on plans for the piracy business.

The takeover on the coast reflects a scramble among militants for strategic position and access to capital ahead of a planned government offensive. Though the government, backed by African Union peacekeeping troops, is surrounded by militants, it has been planning a broad counterattack to reclaim parts of Mogadishu.

On Saturday, explosions at a mosque in Mogadishu's crowded Bakara market killed about 35 people and injured nearly 100 more. No one immediately claimed responsibility for the attack.

The capture of Haradheere is expected to put a dent in the pirates' operation. Piracy has become a major threat to ships sailing in East African waters, and it has largely flourished independently of the militant groups that control much of south and central Somalia.

Pirates cluster in towns along the coast, from where they launch skiffs to capture cargo ships for ransom. Some say they pay about 15% of their takings to militants to allow them to operate in peace, but most have no interest in aligning themselves further with the fighters.

Al Shabaab overran a nearby town last week, unnerving the pirates. The Haradheere pirates had long paid taxes on their ransoms to al Shabaab to keep the group at bay. But last week, pirates in Haradheere said they would no longer pay those taxes, prompting a standoff between the two groups.

—Sarah Childress in Nairobi, Kenya, contributed to this article.

INTERVIEW

How to pitch Italian bonds amid euro-zone contagion

Italy, With Total Public Debt of €1.7 Trillion Is Seven Times That of Greece, Has So Far Avoided the Storm

[Maria Cannata]

By Christopher Emsden

ROME—Maria Cannata's job description sounds daunting: manage a €1.5 trillion portfolio comprised entirely of peripheral euro-zone government debt.

As the director-general of public debt at the Italian Treasury she has to sell Italian sovereign debt, which for years has vied with Greece's for the weakest credit rating on the continent. Greek bonds are close to untradable and the yields on the debt of fellow heavily indebted southern European countries Portuguese and Spanish are rising.

But Italy—whose total public debt of €1.7 trillion ($2.3 trillion) amounts to seven times that of Greece and an equal share of gross domestic product as Greece's—has so far avoided the storm.

Despite a tremor last week when demand for a bond seemed unusually weak, this year should be "smooth sailing" and next year mostly similar as new issues are sequenced to track redemptions, she says. Yields on Italian government bonds are lower than a year ago all along the maturity spectrum. Italy, rated single-A, offers yields that are a bit lower than Spain's, especially at shorter maturities, despite the fact that Spain has an AA rating, even after Standard & Poor's downgrade April 28.

Part of Italy's resilience lies in low private-sector debt levels as well as Finance Minister Giulio Tremonti's refusal to embark on any fiscal stimulus despite the worst recession since World War II.

But it also reflects some technical strategies developed by Ms. Cannata, who lines her office with bond certificates from Italy's past, ranging from a 500-lire issue to fund train tracks in 1880 to documentation for a recent bond worth 3 trillion in Japanese yen. Given fears that some southern European countries may have too much public debt, her sales pitch to the markets is unflashy: Italy sells its bonds according to an obstinately regular schedule to emphasize transparency and predictability. Some other countries, by contrast, sometimes sell issues privately with no announcement at all.

Italian Treasury

Maria Cannata has to sell Italian sovereign debt, which for years has vied with Greece's for the weakest credit rating on the continent.

That is helped by MTS, the Italian bond-trading platform that traders hail for the quality of its real-time (and binding) price quotes.

That platform, launched in 1988 and regularly modernized since, means thinner margins for primary dealer banks that make markets for Italian bonds. But Ms. Cannata cajoled them to comply by offering those that do the best—using the Treasury's sophisticated method in monitoring their performance—special consideration when assigning syndicated deals that involve specialist fees.

The mix of a highly efficient trading infrastructure and the large amount of Italian debt means the Italian bond market doesn't suffer from liquidity problems, which boosts their appeal in times of turmoil. "For better or worse, you can always get a price on Italian bonds," she said.

Ms. Cannata acknowledged she was also making virtue out of necessity with her rigid timetable of debt issuance, given the public debt load is almost 120% of GDP.

"The size of our debt means we can't afford to be opportunistic," she said. An example arose on April 27, when demand at an auction for €9.5 billion in six-month debt was surprisingly weak. The cover ratio, the amount of demand versus the supply, was 1.03, down a worrying 50% from a similar auction in March.

Ms. Cannata said primary dealers warned her the size of the issue was simply too large for the market to swallow at a time of uncertainty. But she stuck to her guns, saying it would have been worse to signal alarm.

Strong demand at auctions two days later vindicated her, and Italy looks set to "continue benefiting" from its better economic, fiscal and rating outlook compared with its peripheral euro-zone peers, said Chiara Cremonesi, a fixed-interest strategist at UniCredit in Milan.

Ms. Cannata said only an "extraordinary event" would push her to alter her published plans.

Her strategy has a downside. She has pushed the average maturity of Italy's government bonds to 7.1 years from 5.0 in 1998, when Italy qualified to join the single-currency union. Longer maturities carry higher yields, meaning Italy's public accounts didn't benefit as much as they could from the lower interest rates ushered in by the euro.

That average maturity compares with only 4.6 years for the U.S.—which intends to raise that figure to 6 in short order—and with 5.8 years for Germany, where short-term interest rates are particularly low because of the country's status as a safe haven.

But that schedule means Ms. Cannata doesn't have to refinance as often as other governments, which means Italy is spared the nerve-wracking experience of having constantly to roll over all of its debt. Back in 1980, when she joined the Treasury, the average maturity for Italian bonds was just one year.

Indeed, Italy actually cut its gross issuance of bonds in the first quarter, while Germany raised its by €27 billion and France by €21 billion, according to UniCredit.

Italy's tight fiscal policy last year has also allowed Ms. Cannata to put "hay in the barn," which can help her cope with any potential fiscal bond-market freeze. The Treasury will have at least €25 billion in a cash account this year, almost three times the usual target level.

That money, Ms. Cannata said, means Italy can instantly fund its share of a Greek rescue package without issuing new debt, and has also allowed it to skip any issuance at all so far this year of three-month Treasury bills or commercial paper.

During the crisis many rich countries rushed to short-term debt markets to fund their responses to the global economic crisis: propping up banks and fund fiscal stimulus plans. That money has to be rolled over constantly—a big risk if market interest rates rise from their current record lows—or moved into longer maturities.

As it happens, that's what Italy has already done. At the end of March, Italy has €151 billion in Buoni Ordinari del Tesoro—bonds with maturities of 12 months or less—outstanding, or 10% of total tradable public debt, down from 12% a year earlier. That compares to €206 billion of short-term French T-bills now in circulation, which is 18% of all French government bonds.

Investors shouldn't expect Italy to be next in the rating agencies' firing line, Ms. Cannata says.