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Debt markets on the ropes in euro zone

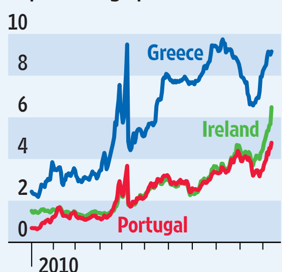
By Neil Shah

LONDON—Irish and Portuguese bonds came under increased pressure as the dimming fortunes of the euro zone's weaker economies stirred fears that other countries besides Greece may need bailouts from the European Union and International Monetary Fund.

The selloffs showed that investors increasingly doubt that crisis-hit countries in Europe can pull off big reductions in their budget deficits in the face of stagnating economies without defaulting or being rescued.

Fear that Ireland can't repair its finances without help pushed the difference in yield between Irish 10-year government bonds and safer German debt to more than six percentage points for the first time on Wednesday. Ireland's chief central banker conceded that his country's debt is now trading at "crisis levels."

Widening
Spread between 10-year government bonds and comparable German bonds, in percentage points



Source: Thomson Reuters

Portugal had to pay a record-high yield of 6.85% to attract investors for an offering of 10-year bonds, adding to the challenges Lisbon faces as it tries to repair its public finances.

The euro sank to its lowest level in one month against the U.S. dollar, dipping below $1.37 before recovering a little. European stocks fell 0.7%.

Investors have refocused on the euro-zone's debt troubles in the past week following news of a Franco-German initiative that could end up forcing bondholders to bear part of the pain in any future bailout of a European country.

German Chancellor Angela Merkel and French President Nicolas Sarkozy are pushing for the debt-restructuring provision to be included in the EU's arrangements for dealing with future debt crises. The European Financial Stability Facility, part of a €750 billion ($1.033 trillion) EU-IMF package to support euro-zone members, is expected to expire in 2013.

The yield on Ireland's 10-year bond, which moves inversely to its price, jumped to nearly 9% from 8.16% on Tuesday, a record premium of

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■ Greek revenue lag hits budget deficit 5

U.K. students protest jump in tuition fees

Reuters

Demonstrators break windows of the Conservative Party headquarters building in central London. Tens of thousands of students marched through the city Wednesday to protest government plans to triple university tuition fees to £9,000 ($14,000) a year. **Article on page 3**

The Quirk

It's all about structure in rapping architect's musical presentation. Page 33

World Watch

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Editorial & Opinion

Three finance ministers on what needs to happen at the G-20. Page 14

Obama asks G-20 leaders for unity to foster growth

SEOUL—U.S. President Barack Obama urged members of the Group of 20 to stand firm against protectionism and called for a joint commitment to growth, part of a concerted effort by U.S. officials to ameliorate global discord on economic policy.

By Damian Paletta, Jonathan Weisman and Kanga Kong

His letter came amid finger-pointing that has threatened to overwhelm the meeting of world leaders. Mr. Obama arrived in Seoul on Wednesday night for a series of critical meetings Thursday, including with German Chancellor Angela Merkel, whose government has led the criticism of U.S. dollar policy, and Chinese Premier Hu Jintao, who has resisted the U.S. president's push on China's currency.

A draft G-20 communiqué illustrated the divisions. Prepared Wednesday for G-20 leaders, it said the group will increasingly let markets determine currency rates. But officials remained undecided about how to discuss currency interventions. The Wednesday draft says the G-20 will "refrain from competitive devaluation," the same language as from a meeting of finance ministers several weeks ago. The draft has the alternative "competitive undervaluation" in brackets, an apparent reference to China, suggesting officials are divided.

Officials also indicated leaders would fudge the key issue of how to reduce global economic imbalances, with Germany and China opposing a move by U.S. Treasury Secretary Timothy Geithner to focus on trade as an indicator. Mr. Geithner said over the weekend that the Seoul summit likely wouldn't agree on specific targets.

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A matter too big for G-20 to decide?

[Agenda]

By Patience Wheatcroft

When world leaders prepare to leave Seoul at the end of this weekend's G-20 gathering, they will issue the obligatory communiqué talking of the momentous decisions made and steps taken to protect the global economy. Read it with some skepticism. While there may be a unity of purpose among the group, agreement over the best route toward achieving it is far from assured. In particular, the search for a definitive recipe for dealing with the problem of financial institutions deemed "too big to fail" is likely to have been inconclusive.

There is no longer the perceived sense of urgency over this issue that there was when it first hit the agenda, as governments were being forced to shovel huge amounts of taxpayers' money into banks to prevent total financial meltdown. Nevertheless, the importance of creating a structure that would ensure the orderly wind-down of a failed financial institution without any catastrophic knock-on effects remains vital. The G-20 has its list of the institutions it judges "systemically important" and they each have the capacity to wreak havoc in their home countries and, in some cases, on a much wider scale.

The International Centre for Financial Regulation, which has just staged its own summit in Amsterdam ahead of the Seoul gathering, concluded that agreeing to a system of crisis resolution for systemically important financial institutions was "the single most important issue in preparing to mitigate the impact of the next crisis." But it could not offer a blueprint to the G-20, believing that more work had still to be done on the practicalities of bail-ins, "living wills" and the various other ideas that have been mooted.

Agence-France-Presse/Getty Images

Oxfam activists wearing masks depicting G-20 leaders in Seoul on Wednesday.

While such an important move does demand careful examination, if the G-20 deliberates for too long, it could find that the next crisis has arrived before its avoidance strategy is in place.

The markets are sounding ever-shriller warnings over the prospect of a sovereign-debt default in Europe. Although the EU now has its temporary bailout fund in place, with €440 billion ($605 billion) signed up to pump into ailing euro-zone economies, that expires in 2013. German Chancellor Angela Merkel has steamrollered through the European Council her plan to have the temporary facility replaced by a permanent one, but the details of this still have to be worked out.

> **Crises have a habit of arriving unexpectedly, which is why the G-20 needs to press on.**

One key element, however, is the incorporation of Ms. Merkel's demands that, should the fund have to ride to the rescue of an EU government, then the private sector, in the shape of bond-holders, should take some of the pain. Quite what level of haircut should be imposed has still to be thrashed out but the prospect should be enough to frighten many banks' risk directors.

Irish and Greek bonds have been hammered in recent days but the wonder is that there should be any market in them at all.

Yet while the problems of those two countries cannot be overestimated, and there is an inevitability about their having at some stage to restructure their debt, the next crisis may land from a totally different source. Crises have a habit of arriving unexpectedly, which is why the G-20 needs to press on with its preparations.

At the culmination of its June meeting in Toronto, the group acknowledged that: "While growth is returning, the recovery is uneven and fragile, unemployment in many countries remains at unacceptable levels, and the social impact of the crisis is still widely felt." Little on the economic front has changed for the better since then.

There have been advances on the financial side, with Basel III laying down some tougher rules on capital ratios, although with a relatively undemanding timetable. But the Financial Stability Board and the Basel Committee had indicated when the new rules were announced that systemically important financial institutions would be required to have even greater loss-absorbing capacity. The details were to be announced in Seoul but now there are doubts as to whether the G-20 will be ready to pronounce on this either.

At the end of the Toronto meeting, the G-20 was clear about the need to minimize the risks posed by the biggest financial institutions. Bringing 20 countries to an accord on how to do it is much tougher but the need remains pressing. If they leave Seoul without genuine progress on this issue, the world's leaders will have a massive gap in their final communiqué.

Accounting for Europe

This week sees the final chapter in the haggling over the EU budget for next year. The European Parliament, oblivious to the climate of austerity in its constituent countries, is demanding an increase of 6.2% while the Council is pushing for a limit of 2.91%.

In the circumstances, it seems worth pointing out, as lobby group Open Europe has, that the EU's auditing body, the European Court of Auditors, has, for the 16th year running, refused to give the EU's accounts unqualified approval. It says that in all but two areas, "payments from the budget continue to be materially affected by error."

The EU spent €118 billion in 2009 and the taxpayers that funded that bill might like to feel the money was at least being properly accounted for, even if they would not all agree it was being well spent. (Open Europe has some fine examples of where it certainly does not appear to be well spent, in particular a €411,000 grant for a project to "improve the lifestyle and living standard of dogs.")

The auditors say that the accounting is improving but they are still sufficiently concerned about the errors that they cannot sign off the accounts. On that basis, the EU's right to demand any more cash looks questionable.

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What's News

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NEWS

Police caught off guard by tuition protest

A Wall Street Journal Roundup

LONDON—Police battled with protesters to regain control of the headquarters of the governing Conservative Party in London on Wednesday as students took to the streets against plans to triple university tuition fees.

Organizers said 50,000 students, lecturers and supporters demonstrated against plans to raise the cost of studying at a university to £9,000 ($14,000) a year—three times the current rate—in the largest street protest yet against the government's sweeping austerity measures.

As the protesters—who marched down Whitehall and by Downing Street and Parliament—passed a high-rise building that houses Conservative headquarters, some protesters smashed windows as others lit a bonfire of placards outside the building.

Several dozen demonstrators managed to get into the lobby, scattering furniture, smashing CCTV cameras, spraying graffiti and chanting "Tories Out," while outside police faced off against a crowd that occasionally hurled food, soda cans and placards.

The violence caught police off guard. Sir Paul Stephenson, the Metropolitan Police commissioner, said the police could have been better prepared.

He said: "It's not acceptable, it's an embarrassment for London and for us and we have to do something about that. ... This level of violence was totally unexpected. We have to ask ourselves why it was unexpected; should we have anticipated it better and what lessons can we learn for the future."

The police said 32 arrests were made and 14 people were taken to hospitals, seven of them police officers, after suffering minor injuries.

The violence appeared to be carried out by a small group as hundreds of others stood and watched. Anarchist symbols and the slogans were spray-painted around the building, and black and red flags flew from atop an office block beside the 29-story Millbank Tower.

"There is a real groundswell of anger among the student community, this is only just the beginning really," said Sol Gamsu, who is studying European Social and Political Science at University College London.

"People will disagree with the violence but essentially it is an expression of a lot of hopelessness and anger that people feel. Who do we go to? In terms of tuition fees there is no political party now who supports an end to the free education the people of Parliament enjoyed."

While British tuition is modest compared with tuition at some U.S. colleges, opponents of the tuition increase have pointed out that Prime Minister David Cameron and other members of the government attended elite universities such as Oxford and Cambridge at a time when university education was free.

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G-20 SUMMIT

Leaders to back U.S. on banks

By Damian Paletta

SEOUL—World leaders are expected to pledge support on Friday for central planks of the new U.S. law governing financial regulation, but officials remain far apart over how to adopt these rules globally to prevent financial crises and taxpayer bailouts in the future.

The divide shows how much work regulators and bankers say still has to be done more than two years after the height of the financial crisis, with banks regaining their footing but economic growth remaining strained.

"There are areas which are still undefined," Stephen Green, chairman of **HSBC Group**, one of the world's largest banks, told reporters after he met with other executives in South Korea. "There is still work to be done, but nevertheless, the direction is right."

Officials at a meeting of the Group of 20 leading nations plan to ratify rules to limit risk at the world's largest banks by requiring companies to hold capital reserves that are at least double what was mandated in the past.

The move would force some of the world's biggest lenders, such as **Deutsche Bank** and **Bank of America** Corp., to operate under new rules aimed at making banking more conservative and less prone to crises. But efforts to reach a compromise in other areas, such as what to do the next time a crisis occurs, have faltered for nearly a decade because of their complexity and the unknown impact on economic growth. Critics say this uncertainty has made it easier for bank lobbyists to play countries off one another and stall a global accord.

"The governments want to be able to advertise that they've done something that will be effective and that they claim will avoid any kind of repeat, but, in fact, the institutions are becoming more powerful than ever," said Ed Kane, a finance professor at Boston College.

Agence France-Presse/Getty Images

Anti-G20 protesters wearing masks take part in a candlelight vigil Wednesday in Seoul on the eve of the summit.

The speed with which officials brokered the bank capital agreement surprised many, in part because a previous effort to create rules in this area took almost a decade. Large, internationally active banks will have to hold capital levels equivalent to 7% of their assets, and governments made it harder for banks to find loopholes around the rules by moving assets off their balance sheets.

U.S. President Barack Obama, in a letter to other world leaders on Wednesday, praised the swift resolution of the capital rules but said more work must be done. "The market will not wait for us to finish," Mr. Obama wrote. "They will test us every day. We need to press on and complete our reform agenda, with new steps to ensure no financial institution is too big to fail.

Attention now shifts to areas where officials have been further apart, such as how to ensure that banks have enough short-term funding to stay solvent during a crisis, and how to break apart globally active banks that become insolvent.

Officials plan to issue jointly a communiqué that pledges support for the Dodd-Frank law passed by the U.S. in July, someone familiar with the matter said. Specifically, leaders will praise key parts of the law, such as tighter regulation over financial instruments called derivatives and new consumer lending-rules.

Officials also are expected to back the notion that governments should have the power to break up and liquidate a failing financial company to prevent a repeat of the chaotic 2008 bankruptcy of Lehman Brothers or the government bailout of **American International Group** Inc. But they haven't reached an agreement on how these powers should work. For example, if a U.S.-based concern that operates across Europe and Asia were to fail, officials don't have a joint plan for how to liquidate the company.

Nations try to restrict 'hot money'

By John Lyons

SÃO PAULO, Brazil—Emerging nations from Brazil to Taiwan are racing to erect protective berms around their economies as a torrent of capital pours in from rich countries such as the U.S., threatening to derail growth by sending currencies soaring, squeezing exporters and injecting volatility into local markets.

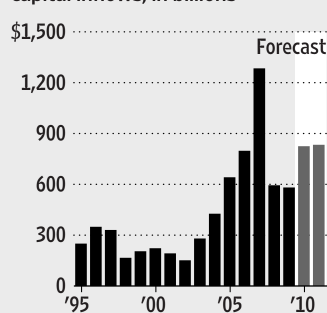
This week, Taiwan imposed limits on bond holdings by foreigners. In October, both Brazil and Thailand raised taxes on foreign investment in local bonds. In June, South Korea restricted derivatives trading, while Indonesia limited investors from selling some short-term bonds. Meantime, central banks from Israel to South Africa are buying dollars to keep their currencies from rising.

As currencies surge across emerging markets, officials are reaching for once-taboo policy prescriptions broadly defined as capital controls in a bid to head off asset bubbles and the other economic downsides of excessive capital flows. The moves, which often carry unwanted side effects, are the latest example of how economic imbalances between rich and developing economies in the wake of the global financial crisis are creating economic headaches for policy makers in the emerging world.

With economies in the U.S., Japan and Europe feeble and interest rates there very low, faster-growing nations like Brazil are attracting a frenzy of investment. Much of it is speculative "hot money" attracted by the higher yields in emerging markets and the prospect of rising currencies, relative to those of richer nations. The trend isn't likely to ease soon. Last week, the U.S. Federal Reserve said it will buy $600 billion of government bonds to stimulate the U.S. economy. Some of the stimulus will slosh to higher-yielding emerging markets.

"There is a tsunami of dollars that is difficult to contain," said Mauricio Cárdenas, a Latin America scholar at the Brookings Institution in Washington. "Countries are doing what they can."

The currency tension between the rich and developing worlds has touched off protests by emerging economy leaders, most prominently Brazil, seeking to push the issue into the center of debate at the Group of 20 summit in Seoul this week. With its won rising, South Korea is considering new capital controls, including taxes on capital flows and foreign bond holdings to add to limits on derivatives trades.



"It doesn't help things to be throwing dollars from a helicopter," Brazil's outspoken Finance Minister Guido Mantega said Nov. 4 about the U.S. Fed's bond buying program. "The only result it has is to devalue the dollar."

U.S. officials have defended the move on the grounds that the global economy will be better off if the U.S. economy recovers faster.

What's more, some economists say the true culprits are countries such as China that maintain artificially weak currencies as a matter of course. China raised reserve requirements at banks this week, also a move to slow foreign investment.

The patchwork of currency policies has sparked concern that global cooperation in the wake of the financial crisis has been replaced by economic self-interest.

"Urgent action is needed to arrest the disturbing trend towards unilateral moves on macroeconomic, trade and currency issues," Charles H. Dallara, managing director of the International Institute of Finance, an association of big international banks, said in a recent statement.

In normal times, rising investment and strong currencies are considered good things. And emerging-market countries still rely on foreign investment for growth.

But what's changed is the flow of speculative cash has reached levels that are bigger than the mostly smaller emerging economies can digest.

The Institute for International Finance estimates private capital flows to emerging economies will be $825 billion in 2010, compared with $581 billion last year.

—Tom Murphy in São Paulo and Evan Ramstad in Seoul contributed to this article.

Obama asks for unity, commitment to growth

Continued from first page

Instead, the G-20 may leave it to the International Monetary Fund to sort out, said Canadian Finance Minister Jim Flaherty. The IMF would report to G-20 finance ministers at their next meeting in February to "define what the options are" on the planned "indicative guidelines," which would measure whether trade surpluses or deficits—which reflect and underlie exchange rates—are in a danger category.

As originally conceived, at least by the U.S., this G-20 gathering was a chance to push China to allow its currency to appreciate more quickly. U.S. officials want countries with trade surpluses, such as China, to consume more domestically and export less, which will help America save more domestically and export more.

But countries have turned the tables on the U.S. in recent days. Several, including Germany, accused the Federal Reserve of driving down the value of the dollar, particularly through a controversial new program to buy $600 billion of U.S. government bonds and other assets. American officials, including the president, have denied the central bank is manipulating the dollar and have said U.S. growth should be in every country's interest.

The Federal Reserve policy looks unlikely to be mentioned formally by the G-20 leaders. Although China has led the criticism of the Fed, it isn't pushing to have the Seoul communiqué single out the central bank, a Chinese official said Wednesday.

U.S. officials believe the depth of the disagreement is being overstated in the pressure-filled last few days before the summit. Given opposition to the trade guidelines, the U.S. isn't likely to press for trade targets in Seoul. U.S. officials hope emotions will ease if leaders endorse what their ministers previously agreed to.

The squabbling among finance ministers "overstates the level of disagreement about the challenges we have ahead," said Mr. Geithner. "We think everyone is going to have an interest in lowering the temperature and defusing some of the tension by agreeing on a multilateral process for helping to resolve these pressures" on the financial system.

Mr. Geithner and his counterparts in Singapore and Australia in an editorial called on world leaders to embrace a four-point plan targeting growth, currencies, capital flows and protectionism. "The deep economic challenges left by the crisis in the established economies and the prospect of rapid expansion in emerging economies necessitate a new agenda for international economic cooperation," they wrote in Thursday's Wall Street Journal. (See page 14.)

At a meeting of business and political leaders several miles from Seoul's Coex Center, several executives expressed frustration that the currency and trade-imbalance issue had disrupted plans to improve economic growth.

—Bob Davis and Andrew Monahan contributed to this article.

EUROPE NEWS

Greek revenue lag hits budget deficit

By Charles Forelle

BRUSSELS—Anemic government revenue has pushed Greece behind its targets for reducing the state's treacherous budget deficit, fresh data from monthly reports of the Greek finance ministry show.

The ministry reported that Greece's central-government deficit narrowed 30% in the first 10 months of this year compared with a targeted narrowing of 32%.

Greece's poor fiscal health sparked Europe's sovereign-debt crisis this spring. When the country ran out of money to repay its creditors, the other euro-zone countries and the International Monetary Fund stepped in with a €110 billion bailout.

The country has little room for fiscal maneuver, and missing the deficit target would leave Greece with unpleasant options if it wants to avoid a debt default: more tough budget cuts imposed on a restive population, or more bailout money.

It remains effectively shut out of private debt markets by the giant premiums that investors are demanding on Greek bonds.

The encore of Greek woe comes as Ireland faces rapidly rising borrowing costs that are pushing it, too, closer to needing a bailout.

The finance ministry data show that Greece's central government took in €41.0 billion ($56.5 billion) in revenue in the first 10 months of 2010, just 3.7% more than it did in the same period of 2009.

Revenue has fallen short in part because budget austerity has helped squeeze a weak economy. GDP is expected to contract 4% this year, weighing heavily on income and sales taxes.

The Greek deficit-reduction plan hammered out with the EU and the IMF in May calls for 13.7% growth in those revenues for all of 2010. That means that to meet the target, Greece must take in €14.1 billion in November and December, an extremely tall order. So far in 2010, Greece has only once had monthly revenue above €5 billion, in January.

The country has had better luck cutting spending, and over the summer it put forward a revised plan that foresees lower revenue but compensates with deeper spending cuts.

But even meeting the lowered target of €52.7 billion would require a 30% jump over last year's revenue for the last two months of the year.

George Zanias, the president of the finance ministry's council of economic advisers, said that Greece's efforts to collect more taxes will bear fruit and that spending cuts are offsetting revenue shortfalls. On revenue, "we are behind; however compliance is increasing," he said in an interview, "and this has not affected deficit targets because we have cut expenditures."

Still, Greece appears very far from the deficit of 7.8% of gross domestic product that it said in September it would achieve this year.

Revenue has fallen short in part because budget austerity has helped squeeze a weak economy. GDP is expected to contract 4% this year, weighing heavily on income and sales taxes. Cuts to public-sector paychecks that went into affect this summer, for instance, contributed to a fall of about 10% in retail sales in August and September.

Austerity will be the order of the day for several more years, and the future looks bleak. "As long as you do not have solid economic recovery, it will be difficult to generate sufficient tax revenues," Jürgen Michels of Citigroup said in an interview.

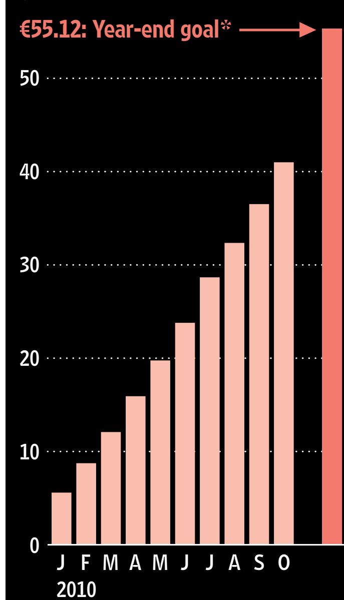
In a report last month, Mr. Michels and his colleagues said Greece is likely to need an extension of its three-year bailout in 2013.

The Greek debt crisis spurred the European Union and the IMF to create a €750 billion backstop for troubled euro-zone countries.

But the largest part of that package, the €440 billion European Financial Stability Facility, will expire in 2013 and European leaders haven't agreed on a permanent replacement.

Off the mark

Greece's cumulative central-government revenue, in billions



*Goal set after EU and IMF bailout in May
Source: Greek Finance Ministry

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Russia prison probe stalls

By Gregory L. White

MOSCOW—Just days before the one-year anniversary of the death of investment-fund lawyer Sergei Magnitsky in a Moscow jail, Russia's Interior Ministry issued decorations to several of the officials responsible for putting him there.

Lawyers and activists say the awards are the latest evidence that the full investigation into Mr. Magnitsky's death that President Dmitry Medvedev ordered nearly a year ago is effectively stalled.

Mr. Magnitsky died suddenly on Nov. 16, 2009, in Moscow's Matrosskaya Tishina jail, where he was being held before trial on tax-evasion charges. His lawyers allege he was denied medical care and moved to steadily worse conditions in an effort to force him to withdraw allegations of massive fraud he had made against police investigators. Police deny that.

The case shocked Moscow's legal and business community and led to a Kremlin push to make it harder for police to jail people suspected of white-collar crimes. Several top prison officials were fired or reassigned. But probes by prosecutors into Mr. Magnitsky's death remain open. No charges have been filed.

"Over this year everything has been checked—the investigators were checked, the judges were checked—and they didn't find anything," said Irina Dudukina, spokeswoman for the Interior Ministry's Investigative Committee, which charged Mr. Magnitsky and his client, U.S.-born fund manager William Browder, with tax evasion. Mr. Browder, now living in London, denies the charges.

The men accused the committee of fraud. They alleged Interior Ministry officials used material seized in the tax-evasion case involving Mr. Magnitsky to fraudulently get $230 million in tax refunds from the Russian government. The committee denied the allegations.

Ms. Dudukina was among those who got awards this week, along with Oleg Silchenko, who led Mr. Magnitsky's case and was granted the "Best Investigator" badge. Ms. Dudukina said Mr. Silchenko's award wasn't related to work on Mr. Magnitsky's case, which was closed after he died.

Robert Zinoviev, a top official at the Moscow Bar Association, said he was "amazed" at Mr. Silchenko's award. "They've taken the position that they won't give up their own," he said.

—Olga Padorina contributed to this article.

RIA Novosti/Agence France-Presse

A woman at a rally for police reform holds images of Magnitsky and jailed former Yukos executive Aleksei Pichugin.

EU to invest €1 trillion in energy network

By Carolyn Henson

BRUSSELS—The European Union's energy chief, Günther Oettinger, set out a plan for a single European energy network to mirror the EU's flourishing cross-border market in goods and services as means to achieve energy security and efficiency.

The project requires €1 trillion ($1.378 trillion) of funding over the next 10 years, Mr. Oettinger said, to upgrade aging pipelines and construct cross-border infrastructure to build a fully integrated network, where energy can flow both east-west and west-east across the European continent.

"Looking at our networks for gas, oil and electricity, we are still stuck within the borders of 19th-century principalities," he told a news conference. "We don't have the quality or the capacity compared to goods and services."

Mr. Oettinger said the planned infrastructure would form a backbone through fragmented national markets, many of which remain dominated by former monopolies, and would allow EU members to form better links with neighboring countries.

The commission will come up with proposals for the plan in the next 18 months and an energy summit of EU heads of state and government will be held from Feb. 4 to seek backing from member states.

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EU debt markets take hits

Continued from first page

6.49 percentage points over the borrowing rate of Europe's safest sovereign borrower, Germany. This premium, which stood at 5.74 percentage points on Tuesday, has jumped for 12 straight days.

"We are getting to the point where people are panicking," says Huw Worthington, an analyst at Barclays Capital in London. "The market is anticipating some sort of [Irish debt] restructuring now," he says. However, he adds that the chance of an imminent Irish default is "zero."

Ireland's jumping bond yields quickly hit bond markets in Portugal, Greece and, to a lesser extent, Spain.

In Greece's latest financial setback, the country appears to be slipping further in its goal of trimming a treacherously high budget deficit. Monthly budget figures released Wednesday by Greece's finance ministry show that central-government revenue rose just 3.7% in the first 10 months of this year, compared with the same period of 2009. Greece's deficit-reduction plan, hammered out in May, calls for a 13.7% increase for the full year.

George Zanias, the chairman of the Finance Ministry's council of economic advisors, says that Greece's efforts to collect more taxes will bear fruit and that spending cuts are offsetting revenue shortfalls.

Investor sentiment on Ireland took another blow on Wednesday when European securities-clearing firm LCH.Clearnet said it is effectively raising the cost of trading Irish government bonds due to heightened risk of an Irish debt default.

Clearing firms stand between buyers and sellers of bonds to ensure that transactions go through even if one party collapses.

Irish bonds were also hit by rumors that the increasingly indebted country, struggling with a banking crisis whose cost to taxpayers could hit €50 billion, has already asked the IMF for aid. However, Irish Finance Minister Brian Lenihan told the country's Parliament on Wednesday that "there has been absolutely no application by Ireland to the IMF and/or the EFSF," the European Financial Stability Facility.

Investors are worried about the stability of Irish Prime Minister Brian Cowen's fragile coalition government, which must pass a crucial austerity package next month. Its majority in Parliament is razor thin.

Portugal also faces strong political and financial headwinds, raising concerns about its ability to stick to its deficit-cutting plans.

While Portugal's minority government and its opposition have come to the table lately, Parliament must still approve the budget at the end of the month.

Some investors also now fear that aggressive austerity programs in Ireland and Portugal could actually crimp economic growth, short-circuiting any deficit-cutting by reducing tax revenue.

Still, there has been some good news in recent days. Chinese officials have offered to help Portugal, possibly by buying government bonds, repeating similar moves towards Spain and Greece. And Ireland's manufacturing sector continued to push ahead, according to data released Wednesday.

—Charles Forelle in Brussels contributed to this article.

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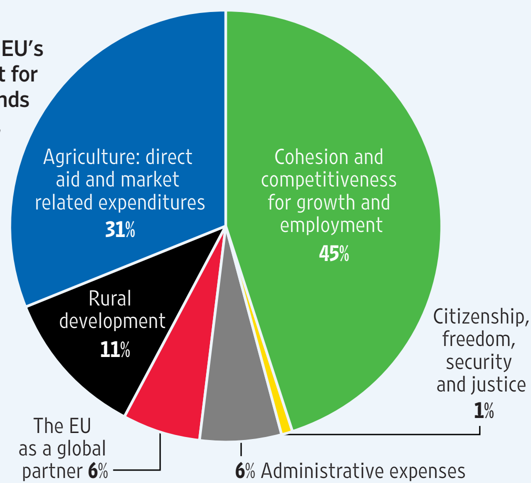
EUROPE NEWS

On the table

A breakdown of the EU's €142.6 billion budget for commitments, or funds allotted for projects, for 2011.



Source: European Commission

Officials seek agreement on next year's EU budget

By Frances Robinson

BRUSSELS—European budget ministers will meet representatives from the European Parliament in Brussels on Thursday to try to reach an agreement on next year's European Union budget.

The council, which comprises budget ministers from the bloc's 27 member states or their representatives, wants the budget for payments—the actual cash spent over the year—to increase by no more than 2.91% from this year's level of €122.9 billion ($169.33 billion), while the European Parliament is pushing for a 6.2% rise.

"At a time when many national governments around Europe are taking tough steps to clamp down on dangerous deficits, it's completely unacceptable to be talking about large increases for the European budget," a British diplomat said. "Others are continuing to argue for a budget above acceptable levels. Our objective over the next 24 hours is to nail down 2.91%."

The EU budget is funded primarily through the contributions of member states and the overall budget for this year is equivalent to 1.04% of the EU's gross domestic product, according to the European Commission, the bloc's executive arm. The commission's draft budget for commitments—the money allotted for projects—is €142.6 billion for 2011.

Thirteen EU member states signed a letter when heads of government met here last month saying the budget increase should be no more than 2.91%, but the parliament says a larger increase is necessary to achieve its goals.

"The European Parliament is accused of extravagance," Sidonia Jedrzejewska, a Polish member of Parliament who is responsible for negotiations, said in a statement. "But we have to keep in mind that the increase of the 2011 EU budget was already decided in 2006 under, somewhat ironically, the British EU Presidency, which negotiated the current financial perspective."

As well as establishing how much money the bloc will have for projects, the negotiations themselves will set a precedent as it is the first time the decision has taken place under the Lisbon Treaty, the latest set of rules to govern the EU institutions. The group known as the Conciliation Committee brings together the parliament and council to try to reconcile their positions, as they are now on an equal footing in the process.

Failure to agree on a joint text by Nov. 15 means the process will stall and next year will see the equivalent of this year's budget, adjusted for inflation,divided up into 12 monthly parcels—effectively, a cash freeze.

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Group calls for overhaul of U.K. tax rules

By Paul Hannon

LONDON—The U.K.'s tax system is overly complex, inequitable, costly to administer and in need of a radical overhaul, according to a report commissioned by the Institute for Fiscal Studies.

The report recommends that income tax and a separate charge known as national-insurance contributions should be merged, while the number of goods and services on which the sales tax is levied should be made more comprehensive.

"The U.K. system falls short of the ideal in costly and inequitable ways," said James Mirlees, the report's chief author and winner of the 1996 Nobel Prize for Economics. "It discourages saving and investment, and distorts the form they take. It favors corporate debt over equity finance. The revenue it raises, and the redistribution it does, could be achieved in less costly ways." The government said it will consider the report's findings.

Cargo bomb was timed to explode over U.S.

By Alistair MacDonald

A device found in the U.K. on a **United Parcel Service** Inc. plane last month was primed to go off over the Eastern seaboard of the U.S., British police said.

A forensic examination showed the device was set to explode at 10:30 a.m. British Summer Time, or 5:30 a.m. Eastern Daylight Time, on Oct. 29, when the aircraft carrying it would have been somewhere over the Eastern U.S., police said.

After a tip from Saudi intelligence, British police intercepted the device at East Midlands Airport at 3:28 a.m. Oct. 29 on a cargo plane bound for Chicago via Philadelphia. The plane left East Midlands at 4:20 a.m., after the suspect package had been removed. Explosives experts didn't disable the device, which was hidden in a printer cartridge, until around 7:40 a.m., police said.

The delay in disrupting the device—which would have put it within about three hours of detonating—will add to criticism that the U.K.'s response to the incident was slow.

A White House spokesman said the British findings "underscore the serious nature of the attempted AQAP attack and the challenge we all face in trying to prevent or disrupt such attacks."

A similar device was found at around the same time aboard a cargo plane in Dubai that had come from San'a, Yemen, via Qatar. The thwarted bombs heightened concern in the U.K. and U.S. over al Qaeda in the Arabian Peninsula, the Yemen-based group suspected of being behind the plot. AQAP is also thought by U.S. officials to have been behind the alleged attempt of a Nigerian man to bomb a flight over Detroit on Christmas Day last year.

A British police spokeswoman said it is hard to be more precise in stating where the device would have exploded, because tail winds, air-traffic control and the fact that cargo planes often reschedule routes make it hard to pinpoint a location at a specific time.

For those reasons, the bomb makers probably expected to bring down a cargo jetliner without full control of where the device would detonate, investigators in the U.S. have said.

The U.K.'s conclusion about the timing of the explosion contradicts a statement made by French Interior Minister Brice Hortefeux last week, when he told French television the device was 17 minutes from exploding when the British intercepted it.

Both the U.K. and Dubai devices appeared to be wired with cellphone motherboards. However, the phone components didn't include SIM cards, suggesting they might have been built to be triggered by the phones' timers and not by outside phone signals, according to people familiar with the matter.

Police also said Wednesday that a man had been arrested in England's Midlands region for allegedly encouraging an act of terrorism in connection with the posting on a U.S.-based website of a list of U.K. lawmakers who voted for the Iraq war.

U.K. crackdown on welfare fraud

By Laurence Norman

SEOUL—U.K. Prime Minister David Cameron's government is planning legislation that could strip jobless-benefit claimants of the allowance for as long as three years, in tough new rules aimed to squeeze benefit cheats.

The move, which is due to be announced Thursday as part of a broader shake-up of the benefits system, stems from the government's efforts to slash welfare costs and reshape the system by maximizing incentives for people to work. The government has said welfare cuts must play a key role in paring back the budget deficit, which total about 11% of gross domestic product in the last financial year.

The move could prove highly controversial. While there will be a right of appeal, the plans could vest significant power in the hands of local job-center officials, who would decide when the penalties apply. The measure also comes at a time when jobless numbers remain high and the economy is in a fragile recovery.

Under the plans, which the government says will take effect before 2013, people claiming job-seekers allowance would lose the benefit for three months if they refuse a job, fail to send in a recommended job application, or don't turn up for mandatory community work.

The benefit of £64 ($102) a week will be held back for six months after a second offense and for three years if the claimant breaks the rule a third time, Mr. Cameron said during a trip to Asia. "The message is clear," Mr. Cameron said. "If you can work, then a life on benefits will no longer be an option."

A person familiar with the matter suggested the allowance could be withheld from "thousands" as the new rules take effect. The person said penalties wouldn't be "100% automatic" but that people would need an "incredibly good excuse" for them not to be applied. However, the person said that since claimants have three months to find a job in their field under the present program, the measure wouldn't lead to skilled workers being forced to take menial jobs.

For those in tough circumstances, the government would make available a hardship fund that would pay out between 60% and 70% of what the job-seekers allowance pays, the person said. However access to the fund would be tightly restricted.

Under the present rules, which applied under the previous Labour government, the maximum penalty for abusing the system was to be denied the allowance for half a year. However, maximum penalties were rarely applied.

The proposal is the latest tough measure the government has put forward as it seeks to contain a total welfare bill that is expected to reach £194 billion this year.

The government has proposed a cap on housing benefits, a reduction in housing allowance if a person is jobless for a year, and a streamlining of disabilities allowance aimed at cutting the number of claimants. The government is also considering forcing the unemployed to do 30 hours a week of mandatory unpaid work.

While the government says these measures will encourage work and are fair for those who struggle in low-paid jobs, others worry the measures will be draconian for some already-struggling families. The opposition Labour Party is fighting the housing benefit cap but has said it will accept some welfare reforms.

Within the coalition government, lawmakers from the junior Liberal Democrat coalition party have also voiced opposition to some of the proposed welfare cuts.

Thursday's allowance announcement comes as the Department for Work and Pensions details its plans to launch a universal benefit, which will wrap the current myriad of allowances into one benefit.

The government has set aside £2.1 billion to pay for the universal credit, which it pitches as the most radical shake-up of welfare since World War II.

The government says the universal credit will make 2.5 million of the poorest people better off and reduce workless households by 300,000 by giving people incentives to work and withdrawing the universal credit only gradually when someone takes on work.

Reuters

The government of U.K. Prime Minister David Cameron, here speaking at the Great Wall during a trip to China on Wednesday, plans to announce rules that could strip benefit cheats of their allowance for as long as three years.

Cameron walks rights tightrope in China

By Jeremy Page And Laurence Norman

BEIJING—British Prime Minister David Cameron faced a conundrum on his first official visit to China aimed at drumming up trade and investment for his flagging economy: how to raise the issue of human rights without sabotaging his business agenda.

It is a dilemma increasingly common to Western leaders who face renewed domestic demands to speak out forcefully on human rights with a Chinese government more confident of its economic power and less tolerant of dissent.

The big question hanging over Mr. Cameron's two-day visit, which ended Wednesday, was whether he would broach the case of Liu Xiaobo, the jailed Chinese dissident who won the Nobel Peace Prize last month. China has denounced Mr. Liu's prize as part of a Western conspiracy and warned Britain and other foreign governments they will have to "bear the consequences" if they attend the Nobel awards ceremony in Oslo next month.

Mr. Cameron was the first Western leader to come to China since Mr. Liu's award, which thrust human rights back on the agenda after a decade in which Britain, the U.S. and most other Western governments have focused on developing commercial ties.

Other Western governments, as well as human-rights activists and business leaders were watching closely to see if and how he would talk about the potentially explosive issue, and what reaction that would elicit from his Chinese hosts.

In the end, Mr Cameron did "raise the issue" of Mr. Liu in a broader discussion about freedom of speech with Chinese Premier Wen Jiabao at a banquet Tuesday as part of a broader discussion on the rule of law, according to a person familiar with the situation. But it was unclear whether Mr. Cameron explicitly called for the release of Mr. Liu, who is serving an 11-year prison sentence for state subversion.

During a speech to Chinese students at Peking University on Wednesday, Mr. Cameron called for "political opening," extolling the virtues of British democracy and expressing the British public's concern about human rights in China. Several other Western leaders have made similar speeches at the same venue, however, and he chose his words carefully to avoid overtly criticizing China, and even, at times, to reflect recent calls for political reform from Premier Wen himself.

"The rise in economic freedom in China in recent years has been hugely beneficial to China and to the world," Mr. Cameron said. "I hope that in time this will lead to a greater political opening because I am convinced that the best guarantor of prosperity and stability is for economic and political progress to go in step together. In some respects it already has."

There was no immediate response from China's leaders, but diplomats said the content of the speech was likely to have been discussed in general terms in advance and was unlikely to have caused offense as it was well within the boundaries of what Western leaders have said before in China.

The reactions from human-rights activists, meanwhile, were mixed.

Some praised Mr. Cameron for going further than President Nicolas Sarkozy of France, who they say glossed over human rights and failed to discuss Mr. Liu during a visit by his Chinese counterpart, Hu Jintao, to France last week.

They have also criticized U.N. Secretary-General Ban Ki-moon for failing to call for Mr. Liu's release, or to express sufficient concern about other human-rights issues, in a visit to China earlier this month.

But some rights activists accused Mr. Cameron of playing to a domestic audience with a publicity stunt that would have no real impact.

"It was positive that [Mr. Cameron] raised the issues at all," said Corinna-Barbara Francis, a China researcher at Amnesty International. "But I think he should have been stronger."

The trip has seen a string of business deals by U.K. firms, the largest of which was a $1.2 billion order from **China Eastern Airlines** for engines from **Rolls-Royce Group** PLC. Still, Mr. Cameron may be disappointed that more deals weren't reached. There had been reports of agreements in the works involving **BP** PLC and Chinese oil firm **CNOOC** Ltd., which didn't materialize.

Separately, an official in Mr. Cameron's office said Chinese officials told their U.K. counterparts that wearing a poppy on their jackets—as Brits do to commemorate soldiers killed in war—could be seen as a reference to the Anglo-Chinese opium wars of the 19th century.

"We informed them that they mean a great deal to us and we would be wearing them all the same," the official said.

Strategic choices lie ahead for four leaders

[Capital]

By David Wessel

Four men now face strategic decisions that will shape the political economy of the U.S. for the next couple of years: President Barack Obama, Republican congressional leaders John Boehner and Mitch McConnell, and Federal Reserve Chairman Ben Bernanke.

For Mr. Bernanke, the question is what would prompt the Fed to buy even more U.S. Treasury bonds than now planned. Unable to cut short-term interest rates further, Mr. Bernanke figures that printing $600 billion more to buy bonds will push down long-term interest rates (to spur a bit more borrowing), boost stock prices (to make people wealthier so they spend more) and depress the dollar (to give U.S. exports a lift).

Justifying last week's move, the Fed pointed to inflation below its 2% target and unemployment well above its "maximum sustainable employment" mandate. In part because key officials don't agree, the Fed didn't spell out under what circumstances it would keep buying beyond next June.

If inflation remains too low and unemployment too high, does the Fed buy more? Or does it only keep buying if its economic forecast worsens? What if it succeeds in getting everyone to anticipate 2% inflation, but unemployment remains high, does it buy more? If not, how does it explain that to American workers?

What if the medicine proves stronger than anticipated, sending stock or corporate bonds into bubble territory? Does it curtail bond buying or rely on its new untested "macroprudential" regulatory tools? How much should it worry about side effects in emerging markets?

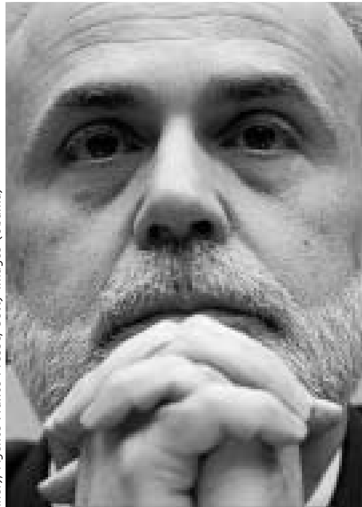
The calls aren't easy; this really is an experiment. Fans of bond-buying outside the Fed say it'll take a lot more than $600 billion to do the job. Complicating Mr. Bernanke's decision: Making what he sees as the right call for the economy in the face of increasingly public internal dissent, most recently from his usual ally, Fed governor Kevin Warsh.

For President Obama, the question is whether to move left or move to the center.

One camp says: Look, you've lost your base, the ones who elected you. Young people didn't turn out last week; you can't win re-election without them. Franklin D. Roosevelt showed the upside of lambasting big business; Harry Truman the upside of attacking a "do-nothing Congress." Republicans didn't take your outstretched hand when they were weak; why expect them to take it now? Stand for something.

The other says: Ronald Reagan and Bill Clinton showed that when your side takes "a shellacking," you can be re-elected if you reclaim the center. It wasn't only a bad economy that hurt Democrats, voters rejected your policies. If you don't show people you heard them, you'll be a one-term Jimmy Carter president. There aren't enough liberals left in Congress to get your old agenda through. Your only hope is compromise—and you'll be better off trying and failing, than not trying at all.

The president's moves on spending cuts and taxes in the next few weeks, on which if any of the proliferating proposals to tame the deficit he embraces, and on how hard he presses Congress to ratify free-trade pacts will be early signs of his leanings. One challenge for him: Staying on message. Rhetoric, whether about business or Republicans, has to match the policy, or this doesn't work.



Reuters (Bernanke); European Pressphoto Agency (McConnell); Associated Press (Boehner); Agence France-Presse/Getty Images (Obama)

Clockwise from top left: Federal Reserve Chairman Ben Bernanke, Republican Sen. Mitch McConnell, President Barack Obama and GOP Rep. John Boehner.

For the Republican leaders, Mr. Boehner in the House and Mr. McConnell in the Senate, the question is whether to continue to "just say no."

The early talk remains combative. Listen to Mr. McConnell on The Wall Street Journal's The Big Interview: "Just because we have differences on whether it was a good idea to try to turn America into France in two years doesn't mean that the president can't take a new path and address some of the issues he indicated in the past he may share our view on."

One approach is to aim everything at 2012: Attack every Obama initiative, look for confrontation, expect gridlock and hope to retake the White House and govern from the right. The other approach reasons that voters gave Republicans a much bigger role in the government and expect them to get something done. The only way to win in 2012 is to show that. This camp calls for avoiding confidence-shaking confrontations over shutting the government or the debt ceiling, and seek issues—trade, perhaps, or business tax cuts—where Mr. Obama is ready to deal.

Like Mr. Bernanke, though, Mr. Boehner and Mr. McConnell have internal unrest. There's already an internecine squabble over earmarks among Senate Republicans, and newly elected Republicans may not follow if their leaders decide to compromise with the White House.

None of these decisions are independent. Mr. Bernanke is buying bonds now because he doubts Congress will provide the near-term fiscal stimulus or long-term deficit reduction that's needed. He can't keeping buying if world markets lose confidence in the ability of elected politicians to manage U.S. finances.

And, of course, neither the president nor the Republican leaders can meet in the middle unless the other side shows up.

Cigarette labels get tough

By Jennifer Corbett Dooren

Graphic images depicting dead bodies and diseased lungs were unveiled by U.S. health officials Wednesday as part of a move to require bolder health warnings on cigarettes and advertising.

A 2009 law requires larger and more graphic health warnings on cigarettes as part of an effort to discourage people from starting to smoke and to lower current smoking rates. Currently, 20.6% adults and 19.5% of high-school students smoke cigarettes, according to government figures.

The Food and Drug Administration has developed 36 images and will be accepting public comment on them until January before it narrows the selection to nine.

The warnings will be required to cover 50% of the front and back panels of a cigarette pack.

The warnings will be required to be placed on all cigarette packages and advertisements no later than Oct. 22, 2012. The pictures and warnings such as "smoking can kill you" will be required to be placed on the top half of cigarette packages with the brand name on the lower portion of the packages. The warnings will be required to cover 50% of the front and back panels of a cigarette pack as well as the top 20% of a cigarette advertisement.

Associated Press

Three of the 36 images proposed by the U.S. FDA for cigarette packaging.

"It will drastically change the look and message on a pack of cigarettes," Health and Human Services Secretary Kathleen Sebelius said at a news conference announcing the new warnings.

The changes will affect all tobacco companies including **Altria Group** Inc., the parent company of Philip Morris USA; **Reynolds American** Inc.; and **Lorillard** Inc.

Earlier this year a federal district-court judge in Kentucky upheld many of the provisions of a 2009 law that gave the FDA the authority to regulate tobacco including a requirement that companies place large, graphic health warnings on cigarette packs.

However, the judge ruled that it can't block companies from using color or graphics in their advertisements, meaning the FDA can't require black-and-white only packaging or advertising.

Reynolds American and Lorillard filed a lawsuit last year against the U.S. government challenging some provisions of the 2009 tobacco law.

Deficit advisers back $200 billion in cuts

By Corey Boles
And Martin Vaughan

WASHINGTON—The co-chairmen of a deficit commission established by the White House would seek to limit federal spending on health care, gradually raise the retirement age and lower the corporate tax rate to 26%, according to a draft set of proposals released Wednesday.

The sweeping plan is likely to provoke a political firestorm. It touches many of the third rails of politics, including defense spending, Social Security and middle-class tax breaks long seen as inviolate.

It isn't a final document. The co-chairs—Erskine Bowles, a chief of staff in the Clinton White House, and former Republican Sen. Alan Simpson of Wyoming—presented the draft plan to members of the 18-strong committee earlier Wednesday. It was presented as a series of options that could be taken together or considered individually as a way to bring down federal spending.

Members of the panel said they thought the proposals were "provocative," but they failed to endorse them outright.

The plan identifies $200 billion in discretionary-spending cuts by 2015, with half the savings from reductions to Pentagon spending. It would remove deductions of interest on second homes, home-equity loans and mortgages worth more than $500,000.

The plan would lower the corporate tax rate but remove a number of deductions. The federal gasoline-tax rate would start to rise from 2013, increasing by 15 cents a gallon at that stage. Federal subsidies to agribusinesses would begin to be slashed by $3 billion a year.

On Social Security, it would gradually increase the retirement age when people can start receiving benefits to 68 at around 2050 and to 69 by 2075. It would combine a cut in benefits with an increase in taxes on wealthier seniors' benefits.

The savings would be phased in over time and include a freeze on salaries paid to federal employees for three years. The plan would propose cutting the federal work force by 10%. It would seek to rein in federal spending on health care, both by introducing changes and by seeking to slow Medicare growth.