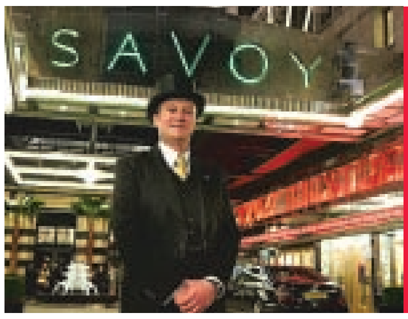

WEEKEND JOURNAL.

Julian Fellowes on a classic hotel reborn

PLUS: RECREATING A LANDMARK PICASSO EXHIBITION

THE WALL STREET JOURNAL.

VOL. XXVIII NO. 181 EUROPE Friday - Sunday, October 15 - 17, 2010

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Schwarzenegger praises 'true action heroes'

Getty Images

U.K. Prime Minister David Cameron, right, looks on as California Governor Arnold Schwarzenegger, the former screen tough guy, hails British troops as 'true action heroes' at Wellington Barracks in London on Thursday. Earlier, the two politicians discussed deficits and other issues.

Investors flee from dollar on stimulus fears

By Andrew J. Johnson

NEW YORK—The dollar fell sharply against a range of currencies Thursday as prospects for Asian economic growth contrasted with the likely need for more stimulus in the U.S.

A monetary-tightening move overnight by the Monetary Authority of Singapore accelerated the dollar's slide, knocking the greenback to long-term lows against rivals in Asia, Europe and North America before the dollar regained some poise in New York trading.

Investors viewed Singapore's decision to widen and raise the trading band for the Singapore dollar as an indication Asian economies now are strong enough to tolerate monetary tightening, while the dollar languishes under the likelihood of more easing by the Federal Reserve.

Thursday afternoon in New York, the euro was at $1.4054 from $1.3957 late Wednesday. The dollar was at 81.42 from 81.77 yen, while the euro was at 114.61 yen from 114.12 yen Wednesday. The pound was at $1.5991 from $1.5892. The dollar was at 0.9519 Swiss francs from 0.9594 francs.

"A broader emerging-market move against the dollar is starting to become more acceptable," said Steven Englander, a currency strategist at Citigroup. "Singapore may be at the leading edge of Asia, but what is of concern is that others may follow."

The Singapore news accelerated dollar selling that already had been stoked by concern over low U.S. interest rates, a run-up in Asian equities this week and large gains in commodities like gold and oil.

The combination drove the yen as well as higher-yielding currencies to notable levels overnight.

The dollar ground down to a fresh 15-year low of 80.88 yen. China's yuan surged to its highest point against the dollar since the Chinese currency began regular trading in 1994. The euro broke to $1.4123, its highest level since January. The Canadian dollar traded below parity for the first time since April, while the Australian dollar hit US$0.9993, its highest point since it was floated in 1983. The dollar dropped to an all-time low against the Swiss franc at 0.9464 francs.

In New York trading, the dollar recovered from its worst levels but remained sharply lower on the day.

With the dollar perilously close to its all-time low against the yen, investors are keenly attuned to any reaction from Japanese authorities.

Japanese Prime Minister Naoto Kan said Thursday that excess volatility in foreign-exchange rates is unfavorable, Kyodo News reported. The comment came after the dollar fell briefly to 80.88 yen for the first time since April 1995.

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■ Japan and South Korea tangle over currencies 4
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Wal-Mart pursues new environment effort

By Ann Zimmerman

Wal-Mart Stores Inc. pledged to dramatically boost the locally grown produce it purchases from small farmers in the U.S. and abroad over the next five years.

The move adds a new leg to the world's largest retailer efforts to improve its corporate image by reducing its environmental footprint. But some questions remain, including how much of the costs will be borne by its suppliers.

The giant retailer disclosed a wide-ranging set of goals related to its food supply chain Thursday, including doubling the amount of food bought from local farmers in the U.S. in the next five years. In emerging markets such as China and India it plans to sell $1 billion worth of food grown by a million small and medium farmers and train them to use water, pesticides and fertilizer more efficiently.

Food accounts for the largest share of Wal-Mart sales, which hit $405 billion in its fiscal year ended January 31. In the U.S., groceries accounted for more than half of its sales, but this is the first time in its five-year program to be more environmentally friendly that Wal-Mart has focused its efforts primarily on global agriculture.

Wal-Mart devised these goals with input from a host of non-profit environmental and social issues groups that work with the Bentonville, Ark., retailer.

"Wal-Mart can potentially use their scale to really move the needle on sustainable agriculture," said Michelle Harvey, at the Environmental Defense Fund's satellite office near Wal-Mart's Arkansas headquarters. The retailer has "the potential to have a significant impact on the best way to make food in a way that is the least harmful to the planet."

A panel of agricultural experts assembled by Wal-Mart warned that food production will have to expand exponentially in the next 35 years to adequately match expected population gains.

Wal-Mart will for the first time ask suppliers about the energy and fertilizer they use per unit of food produced in an effort to encourage efficiency and innovation in using resources, it said.

Experts say that two contributors to deforestation are beef ranching in South America and the production of Indonesian palm oil, a product used in cooking oils, cosmetics and soap.

In Brazil, where Wal-Mart is the third biggest retail chain, it says it only sells beef from ranches that have not despoiled the rainforest. Wal-Mart plans to expand that program globally in the next five years.

It is launching an initiative requiring palm oil used in its private label products to be sourced in a way that doesn't lead to rainforest destruction.

The Quirk

Halloween isn't the only reason for the spike in powdered-wig sales. Page 29

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Lifting the cap on British education. Page 12

Weber's tough talk goes down well but it could damage his ECB bid

[Agenda]

By Terence Roth

Still at the dawn of only its second decade, the European Central Bank has nurtured an experimental currency to prosperity, staved off a financial collapse and weathered Europe's worst recession in 60 years.

It has probably earned the right to throw a little more weight around. And so it is, demanding fiscal probity from its member states' governments, bullying euro-zone banks into lending and lecturing the U.S. and China on their currencies.

There will be more to come if the name of the ECB's next president is Axel Weber, which must be an unnerving prospect for weaker euro-zone members.

As the Federal Reserve and the Bank of Japan hint at extending existing monetary stimulus, Mr. Weber has departed from the ECB script of a gradual withdrawal of support for financial markets as read by Jean-Claude Trichet.

Instead, Mr. Weber says the ECB should stop adding to its pile of €63 billion ($88.5 billion) in bonds from the euro zone's weaker members, saying not only that it poses a threat of inflation, but also that it hasn't brought long-term interest rates down in the problem countries anyway.

Monetary conspiracists might suggest that Mr. Trichet and the ECB are tactically channeling a signal of a coming change through their arch-hawk.

This might not be farfetched. Bond purchases fell to €9 million last week—the lowest since the program started—although only a week before, the ECB had intervened heavily to stop a new rout in Ireland's bond market.

If Mr. Weber is heeding his drummer, he's exposing a rift inside a policy panel that prides itself on consensus.

When the German central banker isn't publicly contradicting his boss, he's demanding draconian conditions linked to future Greece-like bailouts under the euro-zone's European Financial Stability Facility. At some point, countries should just be allowed to restructure debt, a notion that restores the fears of default risk that pounded peripheral European bond markets earlier this year.

Reuters

Axel Weber, the president of Germany's Bundesbank, demands draconian conditions for EU strugglers.

The ECB has probably earned the right to throw more weight around. So it is demanding fiscal probity.

Mr. Weber's candidacy to succeed Mr. Trichet in late 2011 is an open secret as governments tactically maneuver for Europe's monetary crown.

The bank chief's tough talk plays well with his home audience in Germany, where taxpayers still seethe over having had to foot their share of Greece's €110 billion rescue plan. But governments in Dublin and Madrid couldn't be faulted for being alarmed.

Germany's roaring economic recovery is contrasting more starkly with the stagnation still plaguing Spain, where the jobless rate has just risen above the 20% mark.

If Mr. Weber's aim has been to rev up a policy profile to advance his candidacy, it's not a winner among governments who very much like the ECB's supportive role remaining intact for the duration.

Their votes would favor Mario Draghi, an ECB board member who has directed his attentions at building up capital reserves in banks to better absorb the shocks that almost brought down the house in 2008. The Italian, widely considered the other top candidate for the job, also has a natural contingency among neighboring countries whose needs could go unfavored by a central bank in German hands.

France, whose finance minister has openly disagreed with Mr. Weber's ideas of automatic sanctions against fiscal transgressors, would be a crucial vote for any ECB candidate. If Mr. Weber is, in fact, acting on orders from Mr. Trichet to put out advance notice of a policy tightening, he's doing a good job of it.

But it also could cost him the votes he needs next year.

Irish set up

Prime Minister Brian Cowen's call on Ireland's Labour Party to reach a cross-party consensus on deep budget cuts never had a chance of succeeding. Nor, really, did the government expect it to.

The Labour Party instead Thursday called for new elections, deriding the usefulness of a "phony consensus."

Score one for Mr. Cowen, whose frail administration had nothing to lose and everything to gain from the opposition rejecting a proffered hand in the national interests. Not that this much helps Ireland out of a budget deficit amounting to a third of the national economy.

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Real Time Brussels

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Matthew Dalton on European brewers consider options in a shrinking market

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Q: Do you agree with the Obama administration's decision to resume deep-water oil drilling?

Yes	**90%**
No	**10%**

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NEWS

India's Games fall shy of lofty goals

By Amol Sharma

Agence France-Presse/Getty Images

A military band performs Thursday at the closing ceremony of the XIX Commonwealth Games in New Delhi. India's image took a hit amid the chaotic preparations for the Games, though it had hoped they would showcase its economic progress.

NEW DELHI—India exceeded the world's low expectations for the Commonwealth Games after a chaotic run-up to the athletic event, but the organizers fell far short of their goals of showcasing the nation's economic progress and burnishing its global image.

The Games, which brought together 71 nations and territories including Britain and its former colonies, wrapped up Thursday evening with a closing ceremony that dazzled the capacity crowd of 60,000 at New Delhi's Jawaharlal Nehru Stadium. It featured big-name pop musicians, martial artists and thousands of dancers.

The show capped 11 days of relatively incident-free sporting action, a huge relief to the nation after India's tardy and lackluster preparations. The worst fears of foreign sports officials in the days leading up to the start—that venues wouldn't be fully ready for competitions or that countries would withdraw over concerns about hygiene and health—weren't realized. The Games went ahead, and there were great moments.

But they didn't come close to achieving the lofty ambitions India set when it won the rights to host them in 2003. The event was supposed to be a moment to show off the country's rising economic stature, share its vibrant culture with the world, and shatter the notion that India is a place where big-ticket infrastructure projects run way behind schedule. It was also an audition if India one day bids to host the Olympics.

Instead, the first impression India made on the world was dreadful. The country needed an 11th-hour push to finish major sporting venues and then clean up the filthy apartments some athletes and foreign officials found when they arrived late last month. Competitions proceeded on schedule, but there were logistical problems that could have easily been prevented with more time. A ticketing debacle led to a shortage of spectators in many venues even when they were officially listed as sold out.

Many big-name athletes who planned their tournament schedules months in advance chose not to come to New Delhi, reducing the level of competition in events ranging from track to tennis. The influx of foreign tourists that India expected to take in Delhi's sites and sounds never really materialized because of all the bad publicity ahead of the event.

"They got their act together at the last minute, but that's no good," said Abhimanyu Bhandari, an Indian lawyer who advises multinational companies on corporate transactions. "It's still caused deep embarrassment to the nation."

Mike Fennell, president of the U.K.-based Commonwealth Games Federation, which oversees host country arrangements, was a loud critic of India's poor preparations for the Games before they started, but struck a more positive note Thursday, saying New Delhi had done better than expected in some areas, especially security, even as foreign officials had complaints about housing and other issues.

"People have had to deal with issues, there's no denying that, but the end result has been good," Mr. Fennell said at a news conference.

After the Games' spectacular opening ceremony on Oct. 3, many Indians began rallying to support them, and rejoiced as they watched their countrymen win 38 gold medals, second only to Australia.

Some Delhi locals who attended events said they were happy the Games left behind new infrastructure in the city, including a metro train with many more stations than before, a new airport terminal, and several new sporting venues.

Still, many Indians are furious at the Games organizers, including Organizing Committee Chairman Suresh Kalmadi, for the hit India's image took globally, and want to see top officials held accountable. Mr. Kalmadi on Thursday maintained the same optimistic, even defiant, tone he has had for several weeks.

"We faced up to the challenges," he said. "My senior management delivered a great Games."

U.S., British courts spar over Liverpool

By Jonathan Clegg

LONDON—A British judge again cleared the way for a sale of Liverpool Football Club to **New England Sports Ventures** LLC, enjoining the team's American owners from using a U.S. court to stop the sale.

Owners Tom Hicks and George Gillett Jr. meanwhile continued their efforts in a Texas state court.

Thursday's events were the latest twist in what has become a trans-Atlantic legal battle over the future of debt-laden Liverpool, which until recently had been one of England's most successful soccer clubs.

U.K. High Court Judge Christopher Floyd on Wednesday ruled that the proposed £300 million sale ($477 million) to NESV, owner of the Boston Red Sox baseball team, could go forward over the objection of Messrs. Hicks and Gillett.

That decision seemed to end the legal contretemps over Liverpool's sale.

But late on Wednesday, Messrs. Hicks and Gillett won a temporary restraining order from a Texas state court halting the sale. The men called the proposed sale part of an "epic swindle," saying the NESV deal undervalues the franchise. The Dallas court said no sale could go forward until a hearing was held on the matter Oct. 25.

Royal Bank of Scotland Group PLC, the team's chief creditor, returned to the U.K. High Court on Thursday seeking to obviate the Texas court's order and force Messrs. Hicks and Gillett to accept the proposed sale to NESV.

"The owners from beyond the grave are seeking to exercise with their dead hand a grip on this company," said David Chivers, a lawyer for NESV.

The U.K. High Court ruled in favor of RBS and Liverpool's board, which had approved the NESV deal, calling the Texas action by Messrs. Hicks and Gillett, "unconscionable."

The High Court said Messrs. Hicks and Gillett have until 4 p.m. London time Friday to drop their Texas action. NESV said Messrs. Hicks and Gillett would have to comply with the U.K. court ruling by 3 p.m. if a deal is to be completed Friday.

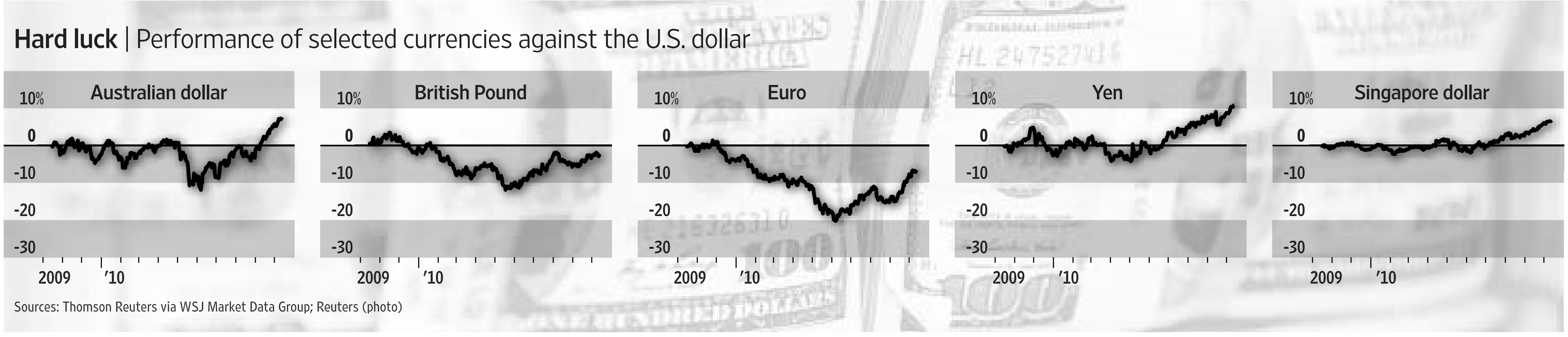
Messrs. Hicks and Gillett couldn't be reached for comment Thursday but filed a motion in Dallas asking that RBS, NESV and Liverpool's independent board be held in contempt. A hearing was scheduled for Thursday afternoon in Dallas.

RBS on Friday is due payment of £237 million in Liverpool debt. NESV has said it will cover the debt if the sale goes through.

If the debt isn't paid Friday, RBS could put Liverpool into administration, a form of bankruptcy protection.

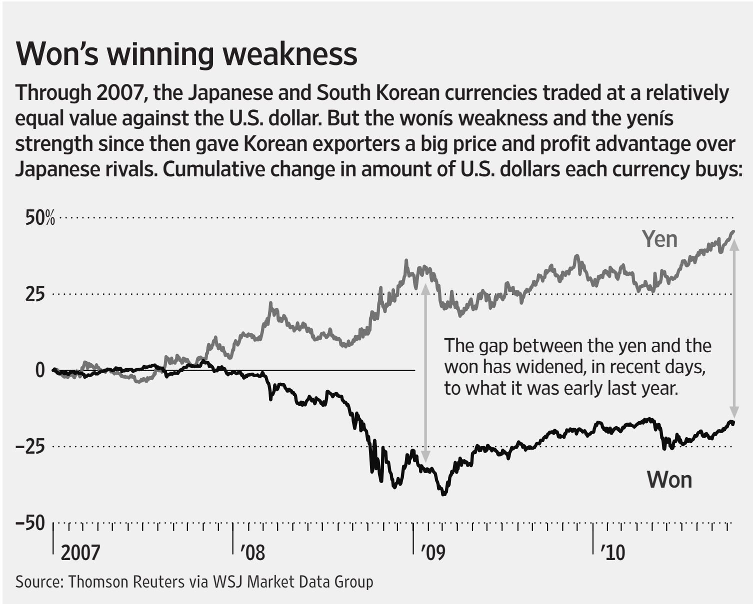
Meanwhile, Singapore businessman Peter Lim dropped his pursuit of the team. Mr. Lim said he won't proceed with his £320 million bid because the board is intent on selling to NESV "at the exclusion of all other parties."

CURRENCIES IN TURMOIL



Japan, Korea tussle over currencies

By Evan Ramstad



Japanese Prime Minister Naoto Kan raises his hand in parliament Wednesday. Mr. Kan blames South Korea for giving the won an unfair edge in exports.

SEOUL—Japan's decision to criticize South Korea for its currency interventions threw a spotlight on a little-noticed reason for South Korea's economic success this year—the Korean won's weakness compared with the Japanese yen.

Like the yen, the won has been rising against the U.S. dollar in recent months. But the lingering difference between the yen and the won helps South Korean companies maintain an edge in pricing and profit margins in the industries in which they compete with Japanese rivals, including automobiles, shipbuilding, steel and electronics.

The tussle between South Korea and Japan is part of the broader currency turmoil shaking up governments and businesses across the world.

The U.S. dollar has fallen 12.8% so far this year against the yen but is down only 4.8% against the won. The two traded nearly evenly against the U.S. dollar in 2007 but their performance diverged sharply in 2008 as investors worried about the global economy dove into currencies considered safe, like the yen, while moving out of currencies considered more speculative, like the won. The gap reached its widest point in January 2009, but is now almost as wide.

That makes Japanese products more expensive than Korean products when translated into other currencies. Because most companies choose to adjust prices to compete, the impact is usually seen on the bottom line.

Speaking at an event in Tokyo last month, **Sharp** Corp. President Mikio Katayama said the yen's strength and Japan's corporate-tax rate put the company at a disadvantage to Korean competitors. "It's unfair competition, like carrying dumbbells tied to your arms and legs," he said.

On Wednesday, Prime Minister Naoto Kan and Finance Minister Yoshihiko Noda for the first time blamed South Korea along with China for creating artificially low currency rates, citing the Bank of Korea's near-routine interventions in currency markets. "I want South Korea and China to take responsible actions within common rules," Mr. Kan said, though he cited Japan's own recent market intervention to bring down the yen.

In Seoul Thursday, the Bank of Korea and key economic agencies criticized Japanese leaders for making inappropriate remarks but declined to elaborate. In the past, Korean officials have said the central bank's currency interventions are intended to smooth the direction of the won's value, not change it.

Currency analysts expect both the won and yen to continue gaining strength against the U.S. dollar in the months ahead, though the gap in relative values may tighten and reduce some of the advantage Korean exporters hold.

The exchange-rate issue spilled into Thursday's decision by the BOK's monetary policy committee to leave interest rates unchanged. Many analysts speculated the bank's policy makers worried that higher interest rates would attract capital flows that would further drive up the won's value. BOK Governor Kim Choong-soo said the won's value was one of many factors influencing the decision to hold the rate steady.

In recent months, Korean firms and government officials have worried about the won's gains against the dollar, which have brought the currency nearly back to where it was in September 2008 ,before a global credit crunch and currency devaluation in many countries.

At the same time, the won's relative advantage against the yen has actually gotten better—helping Korean exporters along the way. That has meant, for instance, that South Korea's **Hyundai Motor** Corp. vehicles have a pricing advantage of 10% to 15% on Japanese manufacturers.

For **Sung Min Electronics** Co., which makes switches and lights for electronics products, the won's advantage against the yen has paid off in Germany, where sales are up 20% compared with last year, says Lim Hyuk, a sales manager.

Having a pricing edge against a main competitor is especially important to South Korea because exports account for 43% of its economy, the most of any developed nation, according to the Organization for Economic Cooperation and Development.

Australian dollar reaches a 28-year high

By Katie Martin

LONDON—The Australian dollar rallied to a 28-year high Thursday and came within a hair's breadth of one-to-one parity with the U.S. dollar, raising questions of when it might surpass that point—and whether it will surge still higher.

The Australian dollar rose as high as US$0.9993 in European trading hours Thursday, compared with US$0.9901 in U.S. trading Wednesday, amid a broad-based drubbing for the U.S. currency.

The Australian dollar's ascent toward parity against its U.S. counterpart has thrown it into the spotlight in recent days, but it has been a favorite of investors for months, surging by around 20% against the buck since June.

Its relatively high and rising interest rates, close economic links to Chinese growth and the related strength of Australia's crucial mineral exports have all fueled the increase.

Strong downward pressure on the U.S. dollar, based on concerns about further monetary easing by the Federal Reserve, also bolstered the move.

Speculation has now turned to whether the Australian dollar will pause if it breaks through the US$1 barrier. The currency could still face resistance because investors often place long-running sell orders when a notable benchmark approaches. But that resistance is generally fleeting, investors say.

"It's a psychological level, but that's it," said Thanos Papasavvas, a currency-fund manager at Investec Asset Management in London, which handles around $9 billion in dedicated currency funds.

"The Aussie is getting a little expensive now, but it's nothing significant," he said, adding that he started buying the Australian currency at around the US$0.90 area, and he is still "marginally overweight" on the currency despite having taken some profits on the trade.

While many monetary authorities in the Asia-Pacific region have fought back against the export-denting strength of their currencies, Australia is traditionally viewed as willing to let its currency climb as market forces dictate, which lures in funds looking to snag smooth profits.

Last week, the Australian dollar broke new ground as it burst above US$0.9851—a level that had previously marked its highest level against the buck since the Aussie became a freely floating currency in 1983. But it still hasn't reached parity.

In part, that reflects concerns among some currencies analysts that the rally has, for the short term at least, run a little too fast, after a chunky 4% climb in just the past eight trading days. "While fundamentals have continued to move in the Australian dollar's favor against the U.S. dollar, we think the rally is outsized," said analysts at Barclays Capital in a note to clients Thursday.

Barclays Capital's economic models suggest that the "high US$0.80s" represent a fair level for the Australian dollar for now, and that "levels around parity are not normal ... and will not last long."

Many funds, however, remain unfazed, and a move in the Aussie above the US$1 point would be unlikely to spark a rush to the exits. Monica Fan, a currencies portfolio manager at State Street Global Advisors, which manages $83 billion in currency-fund assets, said she thinks that the Aussie is heading to US$1.01 in the short term, and as high as US$1.05 in the first three months of next year, assuming that Chinese economic growth remains intact.

The biggest reason for this, Ms. Fan said, is that further monetary easing in the U.S.—a serious drag on the U.S. dollar—is inevitable.

Balraj Bassi, a managing partner at BlackTree Investment Partners in London, which runs a start-up currency fund driven by computer modeling, agreed that drags on the U.S. dollar are, for now, the biggest driver of Australian dollar gains. Some signs of soft global growth expectations suggest that the trade may be overdone, but crossing the US$1 mark wouldn't be enough for him to reverse his bets.

"It's a psychological number and it attracts headlines, but for us, it doesn't matter. We look at the fundamentals, which means everything—commodities, risk-aversion indicators and rates. We have been long of Aussie dollars for a while, and we're still positive on it," he said.

—Eva Szalay in London contributed to this article.

EUROPE NEWS

Strikes grip Athens to protest austerity

Riot police confront protesters at the Acropolis in Athens on Thursday.

BY NICK SKREKAS

ATHENS—Greek labor tensions heightened Thursday, as a railway strike caused travel chaos and police and workers clashed outside the country's most revered archeological treasure.

The protest in the Greek capital represented yet another wave of dissent as the government tries to drag the country out of an unprecedented debt crisis and recession. It only narrowly avoided bankruptcy in May after agreeing to impose painful measures in exchange for a €110 billion ($153.53 billion) bailout from the International Monetary Fund and the European Union.

The cash-strapped Mediterranean country has made sweeping cuts in public-sector wages and pensions, severely reducing new hires in the civil service and refusing to renew temporary contracts. It has also raised indirect taxes, deepening the current recession and resulting in higher unemployment.

July unemployment figures came in at 12%, up from 11.6% in June and 9.6% in the year-earlier month. Nikos Magginas, an economist at the National Bank of Greece, forecasts that unemployment will top 14% by December.

Unions predict there will be a million people out of work by year-end, corresponding to a 20% real jobless rate.

The temporary workers protesting at the Acropolis were angered by the coming dismissal of 320 employees whose contracts won't be renewed.

Just past noon, police clad in riot gear fired tear gas to dispel around 150 Culture Ministry workers and forced open a padlocked gate that had kept the Acropolis and the Parthenon inaccessible for the second straight day.

"I am only in Athens for two days and on both occasions I couldn't see the Parthenon," said 55-year-old Canadian tourist Tony Balwin, standing at the foot of the Acropolis. "After seeing the tear gas and heavily armed police, I am not sure sightseeing is always safe here. I don't think I will come again and I'll just have to show my happy snaps of clashes to my friends."

The temporary workers protesting at the Acropolis were angered by the coming dismissal of 320 employees whose contracts won't be renewed. The protesters also claim that about €5 million is owed to them in back pay for the last two years.

Meanwhile, railway workers walked off the job Thursday, causing widespread disruption for travelers that could spill over into Friday. The government has made state-controlled Hellenic Railways Organization, or OSE, which is €10.6 billion in debt and is slated for privatization, a focus of its plans to slash public spending.

"I was supposed to catch a train to Thessalonica to visit my grandkids because my wife and I can't afford airline tickets after our pensions were cut, so we booked and paid for our train tickets weeks ago. Now our plans are shot to pieces. I hope at least we get a refund," said pensioner Dimitris Ioannidis, outside the closed railway station in downtown Athens.

After sporadic work stoppages over the past two weeks, railway workers are timing their latest mobilization to coincide with a bill being submitted to Parliament to break up the monopoly, shed almost half its employees and seek out private investors to run a more streamlined operation. The government hopes the revamped OSE will produce marginal profits as early as next year so it can attract international bidders.

Meanwhile, Greece's largest union, GSEE, met Thursday to plan yet another wave of industrial action. The private-sector umbrella union of 800,000 members vowed to hold a 24-hour strike later this year.

"Our strike on Dec. 15 is a protest against continuing austerity measures as well as the spiraling unemployment that the policies are creating," GSEE spokesman Stathis Anestis said.

EUROPE NEWS

Reuters

The two sections of the NEAT Gotthard Base project are expected to meet Friday, creating the world's longest rail tunnel.

Tunnel breakthrough for Alpine train link

By Neil MacLucas

ZURICH—Miners drilling from southern and northern Switzerland are expected Friday to meet hundreds of meters below the Gotthard Alpine massif to create the world's longest railway tunnel as part of an ambitious long-term project to move goods and freight off European roads and onto railroads.

The 57-kilometer (36-mile) tunnel project, which will connect the Swiss towns of Erstfeld, north of the Alps, with Bodio, on the southern side, is designed to carry international 250-kilometer-per-hour high-speed trains. The price tag for the project is around 10 billion Swiss francs ($10.4 billion)

The trans-Alpine rail connection "is a key project for sustaining the long-term viability of both passenger and goods traffic," says Manfred Schellhammer, managing director of freight and logistics company **Kuehne & Nagel International** AG.

Some 2,500 miners, from all over Europe, as well as from countries with mining expertise like South Africa, have worked around the clock to move about 27 million tons of rock and rubble from the twin tunnels. About 13.3 million cubic meters of aggregate, enough to build the equivalent of five Giza pyramids, have been excavated since tunneling began. Eight miners have died.

The Swiss approved the project in a 1998 referendum in an effort to alleviate the environmental and logistical problems caused by a surge in heavy goods vehicles travelling through Switzerland from northern and southern Europe. When the twin tunnel is opened for traffic, probably in late 2017, it should cut the travel time between Zurich and Milan to 2½ hours from 3½ hours, and will provide the key north-south axis link between the ports of Rotterdam and Genoa.

Swiss Transport Minister Moritz Leuenberger and executives from the construction and drilling consortiums will be on hand to witness the breakthrough of the two tunneling teams Friday.

The tunnel will be longer than the Seikan tunnel, which links the Japanese islands of Hokkaido and Honshu, and is the third tunnel to be bored through the Gotthard Alpine range following the original rail tunnel, finished in 1880, and the 17-kilometer-long road tunnel completed 100 years later.

The project, dubbed NEAT, is managed by **AlpTransit Gotthard** AG, and some of the companies involved in the tunnel construction include Swiss cement maker **Holcim** Ltd., insulation materials specialist **Sika** AG, construction conglomerate **Implenia** AG and German mechanized tunneling technologists **Herrenknecht** AG.

The volume of road traffic using the Alpine transit routes is estimated to double every eight years, reaching around 14 million tons in 2009, according to data from the Swiss Federal Office for Transport, while the level of traffic using the Alpine rail network has seen little growth in recent years. The new Gotthard and existing Lötschberg railway nodes should increase the freight-carry capacity to 50 million tons per year by 2030 from 21 million tons at present.

The tunnel will provide the key north-south axis link between the ports of Rotterdam and Genoa.

"From 2017 it should be possible to shift a significant portion of the north-south European goods traffic from the road onto the railway, and the 57-kilometer long tunnel represents a milestone in the common European traffic system," says Kuehne & Nagel's Mr. Schellhammer.

Calculating the wider benefit to the Swiss economy of the investment in the tunnel isn't easy. "The benefits to the Swiss economy in general from this project are very difficult to quantify, although there are bound to be structural advantages in the future," says David Marmet, a senior economist at Zürcher Kantonalbank.

"The flat gradients in the Gotthard tunnel, and the already completed Lötschberg link, will offer us distinct business advantages in terms of cost and travel times, and in the freight and logistics market, that means money," says Joachim Schoepfer, head of sales and production at **BLS Cargo**, a Swiss rail operator that has around 40% of Switzerland's rail cargo transit market. BLS, which operates about 25,000 goods trains a year, will also benefit from the upgrading of capacities in German and Italy, where it has partnerships with **DB Schenker Rail Deutschland** AG and **IMT** AG, Mr Schoepfer says.

AlpTransit is bullish. "Depending on individual projects, we could have a 20,000 kilometer high-speed rail network in Europe by 2020," it says on its web site.

But making a European high-speed rail cargo network viable and efficient depends on Switzerland's neighbors and their willingness to match Swiss spending on the infrastructure improvements needed. And some Swiss observers have been skeptical that their neighbors are sufficiently willing. "The [rail] system first has to work efficiently and until then road transport will retain its advantages," ING transport analyst Axel Funhoff says.

The attraction of rail cargo is bound to improve over time, but the system needs to operate seamlessly from port to port, and country to country, and until then rail cargo is unlikely to improve on its 10% share of the European freight market, Brussels-based Mr. Funhoff says.

Deutsche Bahn is spending about €500 million to build a 9.4-kilometer twin-tunnel facility just across the Swiss border to link its network to that of the Swiss. But progress may be slow. For example, German efforts to upgrade and expand rail capacity between Karlsruhe and the Swiss city of Basel have attracted some 172,000 objections from private parties affected by the plans.

No euro-zone currency war, just tough choices on reform

[Brussels Beat]

By Stephen Fidler

As economic policy makers around the world fret about the outbreak of currency wars, in the euro zone that possibility has been abolished.

Economists at Dutch bank NIBC estimate that at least 18 countries around the world have intervened to depress their currencies over the past few weeks. In some of the countries that haven't, such as the U.S. and Britain, central banks are preparing to engage in another round of quantitative easing, or printing money—a move that would also depress currency values.

But there's no currency war here in the euro zone. Not only is the European Central Bank policy looking tougher than those of most of the world's other monetary authorities, but the common currency's high-deficit countries have given up the right to independently launch foreign-exchange wars of their own.

That may be no bad thing, but without the apparently easy option of devaluation for its weaker brethren, the euro zone faces the deep dilemma of how to reform itself. At a summit at the end of the month, European Union leaders will examine a report from a task force led by European Council President Herman Van Rompuy on how this should happen. Mr. Van Rompuy will have to walk a fine line between what probably should happen to make the euro zone sustainable—a significant pooling of political sovereignty—and the political practicalities within a currency bloc of 16 (and soon to be 17 as Estonia joins) nation states.

With member states' weaknesses exposed by the financial crisis, few disagree on the need for change—both in the way governments of the common currency coordinate economic policies and in the structures of many of its members' economies.

A research paper published this week by the International Monetary Fund underlines just how the advent of the common currency has exposed frailties in some of its members' economies.

Its main conclusion: Trade imbalances within the euro zone have widened considerably and have become more persistent since the introduction of the euro. For Italy, the paper points out, the trade deficit with Germany has risen fivefold within a decade, and now exceeds the country's overall deficit in external trade.

The paper from Helge Berger of the IMF and Volker Nitsch of the Darmstadt University of Technology doesn't represent IMF policy. But it draws its conclusions from bilateral trade patterns among the euro-zone economies and a few other economies in Europe, such as Switzerland. It adjusts the results for factors such as Germany's longstanding export success and for examples, such as Ireland, where there have been marked shifts over time in trading patterns with all trading partners.

The conclusion perhaps isn't a surprise. Nor are the reasons for the bigger and more persistent deficits: that countries cannot respond to the trade surpluses with Germany by devaluing their national currencies—in economists' jargon, they are unable to adjust their nominal exchange rates.

For the deficit countries in the euro zone, Mr. Berger says, "the absence of the adjustment to the exchange rate has made things more complicated."

Going a step further, the paper analyzes what influences the size of the trade deficits. Again the conclusions are not unexpected—but interesting because the results reflect what economists would have predicted.

The more rigid a country's markets in tradable products and services and the more inflexible its labor market, the slower will be the pace of adjustment to the trade deficit. "You need flexibility in your labor markets and in your product and services markets. If you don't have that, the adjustment will take longer," says Mr. Berger.

The economists also found another pronounced connection: higher external deficits are associated with high budget deficits. "Among euro area members, a one percentage point increase in the (relative) fiscal balance is associated with an improvement in the bilateral trade balance by about two percentage points," the paper concludes.

Tackling imbalances through unpopular reforms is not a route many politicians willingly take.

There's a message for surplus countries too. They could reduce their surpluses by cushioning the swings in the business cycle. Economic volatility, the authors argue, tends to increase trade surpluses because it increases the tendency to build up precautionary savings and therefore lowers the propensity to consume, including on imports.

"Our findings imply both bad and good news for policy makers. The bad news is that irrevocably fixed nominal exchange rates do come at the cost of larger and more permanent trade imbalances, just as [the economist Milton] Friedman claimed more than half a century ago. The good news is that these imbalances are not completely unavoidable," their paper says.

So imbalances aren't inevitable. But tackling them through unpopular and profound reforms, confronting powerful interests, changing working practices of lifetimes, challenging modes of living, and cutting popular public spending is not a route many politicians willingly take. For much of the rest of the world, currency devaluation looks like the easier option. For many in the euro zone, only hard choices.

European Pressphoto Agency

U.S. Secretary of State Hillary Clinton, left, with Catherine Ashton, the EU high representative, in Brussels on Thursday.

Clinton presses EU on Pakistan relief

By John W. Miller

BRUSSELS—U.S. Secretary of State Hillary Clinton suggested European Union leaders should follow the U.S. and withhold further flood-relief funding from Pakistan until Islamabad shows it is doing more to fight corruption and collect tax revenue from its wealthiest citizens.

After meeting with Catherine Ashton, the EU's high representative, Mrs. Clinton praised recent EU aid efforts but added, "the international community can only do so much." It is unacceptable, she said, "for those with means in Pakistan not to be doing their fair share to help their own people."

Mrs. Clinton's comments came a day before a conference of EU ministers in Brussels to address Pakistan's flood-relief needs.

The World Bank on Thursday tagged the estimated damage from the July floods at $9.7 billion. The torrential rains, which covered a fifth of the country and killed 2,000 people, knocked down bridges, destroyed homes and submerged farmland. Pakistan has received $1.5 billion in relief so far.

At this point, the EU has contributed around $500 million while the U.S. has given roughly $400 million. Additionally, the EU has waived duties for up to three years on 75 categories of imports, mainly textiles and clothing. The move has prompted criticism from European textile companies already under pressure from Chinese imports.

Mrs. Clinton's statements reflected a tougher stance on Pakistan. "Rhetoric in Washington on Pakistan has picked up across the board in the last few months," said Dhruva Jaishanker of the German Marshall Fund in Washington.

The U.S. has also said Pakistan isn't doing enough to battle militants along the Afghan border. Pakistan is engaged in an offensive against some groups, but has largely avoided fighters from the Afghan Taliban, al Qaeda and other groups that stage attacks on North Atlantic Treaty Organization forces in Afghanistan.

Mrs. Ashton's answer to Mrs. Clinton exposed a small difference in approach. Instead of bluntly stating conditions that Pakistan should fulfill, she said, "we look forward to learn more about Pakistan's strategy for a longer-term comprehensive approach to recovery."

On Friday, Mrs. Ashton will head a gathering of EU foreign ministers and Pakistani Foreign Minister Shah Mahmood Qureshi. He and other government officials have emphasized that their priority is rebuilding. "If you want to help us fight extremism and terrorism one way of doing that is making Pakistan economically stable," he said at the European Parliament.

Aid groups said they agreed with the U.S. stance in principle but insisted there should be no conditions. "People struggling from the floods shouldn't have to pay because of issues with the government," says Rebecca Barber, who works for Oxfam in Islamabad.

Oxfam on Thursday also criticized the West for not forgiving some of Pakistan's $55 billion international debt.

ECB hawks urge bold euro-zone rules

By Geoffrey T. Smith

FRANKFURT—Top officials from the European Central Bank called on politicians Thursday to show more courage as they finalize new rules for the governance of the euro zone.

The calls come as a task force under European Council President Herman van Rompuy enters the final stage of drawing up its recommendations on what new rules the euro zone needs to avoid lurching into a generalized debt crisis.

Mr. van Rompuy is due to present his recommendations to heads of government at the end of this month, but there are still strong differences of opinion within the European Union—and within the ECB itself—about what precisely is needed.

In a speech in Berlin, Bundesbank President Axel Weber repeated his call for the new rules to make it clear that countries that get into financial trouble should have their debts restructured rather than be rescued by other euro-zone members. If a country has to call on its partners for help, then that help should be attached to "strict and painful conditions," he said.

He also insisted there shouldn't be rules that penalize Germany for having a competitive export sector and a more flexible labor market than its partners.

Meanwhile in London, Luxembourg central-bank chief Yves Mersch argued for rules that would effectively break the traditional hold of national governments over wages and pensions in their own countries. The new rules "should take aim at national rigidities that are incompatible with a currency union, like automatic indexation mechanisms of wages and pensions," he said.

The European Commission already has proposed a mechanism under which countries that run excessive deficits would automatically incur sanctions unless an overwhelming majority of member states disagreed. For the ECB, those proposals don't go far enough. Chief Economist Jürgen Stark has argued for countries to be denied their voting rights and their access to EU budget funds if their budget policies are too loose.

Increasingly, though, officials have acknowledged that budgetary limits alone won't address the root of the euro zone's problems, which lie in the sharp divergences in developments in wages and productivity from one country to another.

Solar-powered lamp picked as 2010 object

By Javier Espinoza

LONDON—A humble solar-powered lamp became the star attraction of the British Museum on Thursday when it was revealed as the 100th and final subject of a radio series that has created a huge audience in the U.K. and beyond.

"A History of the World in 100 Objects" is a joint venture between the British Museum and the BBC, a series of 100 15-minute programs presented by the museum's director, Neil MacGregor. The series has generated about 10 million downloads, of which almost half have come from outside the U.K., Mr. MacGregor said.

Among the objects featured have been a colossal statue of Egyptian pharaoh Ramesses II, shadow puppets from Indonesia, a Tanzanian ax more than a million years old, and the Sutton Hoo helmet, hailed as a key Anglo Saxon discovery. The first program in the series was broadcast on Jan. 18, the last is scheduled for Oct. 22. Contributors have included Irish activist Bob Geldof, Nigerian writer Wole Soyinka, English artist Grayson Perry, Indian food writer Madhur Jaffrey and Irish poet Seamus Heaney.

Explaining the choice of the lamp, and its charger, which represent the year 2010, Mr. MacGregor said solar power has allowed millions of people to take control of their lives. "If exposed to eight hours of sunlight, the lamp gives 100 hours of light and heat [and] will allow everybody to access light, which has so far been a privilege of the urban elite."

More than 500 museums throughout the U.K. cooperated for the series of 15-minute programs, in which the significance of the various objects was explained by Mr. MacGregor and his guest contributors. Members of the public were also invited to contribute objects with a story to tell. Suggestions included a grain of genetically modified wheat, the cap of a BP oil well, a can of energy drink, an AK-47 rifle, and even an artificial Christmas tree and a CCTV camera.

The solar-powered lamp was chosen from a selection of five articles—the others were a Chelsea shirt worn by the footballer Didier Drogba, a mobile phone, Antarctic clothing and a pestle and mortar.

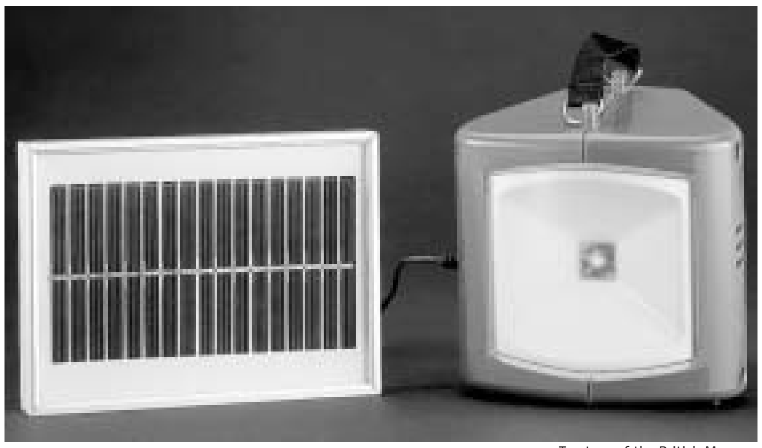
This project "has shown how important it is to look at the whole world together historically. I hope this has shown that collections like this one where the whole world's

The radio series on 100 objects, a joint venture between the British Museum and the BBC, has generated about 10 million downloads, almost half outside the U.K.

cultures are in one place can bring an understanding that nothing else can," Mr. MacGregor said.

Choosing the solar lamp, he added, had to do as well with the metaphorical power of light. "The idea of the series was about enlightenment, because when this technology develops to allow smartphone access from this kind of source of power, it will mean that everybody will be able to access the knowledge of the world," he said.

The British Museum and the BBC plan to work together on similar projects "looking at the connections of the world," the museum director said. "Our histories are never separate, national histories."



Trustees of the British Museum

Solar power has improved the lives of millions of people, the museum said.

Associated Press

Sen. Jim DeMint (R., S.C.) is a leader of the estate-tax repeal camp in the Senate.

Estate taxes heat up on campaign trail

By John D. McKinnon

A move to end the U.S. estate-tax is luring new adherents in the 2010 midterm campaign, turning permanent repeal into a negotiating stance for future congressional wrangling over taxes.

More than 250 current congressional candidates, mostly Republicans, have signed a pledge this year to support elimination of the tax, according to the advocacy group sponsoring the effort. The signers include 53 incumbents and more than half of Republicans running for House and Senate. During the 2008 elections, when the group first began seeking supporters, only 30 candidates signed up.

The estate tax has become a particularly hot issue in the West, including in Washington state's Senate contest, and some rural House districts where Democratic incumbents appear vulnerable. The tax tends to be a hotter issue in rural areas because it raises particular concerns among farmers and landowners.

During the Bush administration, Congress passed a law that lowered the tax gradually and repealed it entirely for 2010. It is set to spring back Jan. 1 to its 2001 level, absent congressional action, with a top rate of 55% and an exemption for the first $1 million of an estate's value.

For now, it appears unlikely the momentum behind repeal will prompt Congress to extend the repeal for 2011. Instead, the current Democratic-controlled Congress seems likely to consider a new version of the estate tax in a lame-duck session after the November election as part of a package of extensions of other expiring Bush-era tax breaks.

A strong showing for repeal in November, however, could raise pressure on lawmakers to lower rates and increase exemptions, Republican aides say. It could also lay the groundwork for reconsideration of the issue following the 2012 election.

President Barack Obama favors returning the estate tax to 2009 levels, which saw a 45% rate and $3.5 million exemption. Republican leaders in the Senate, a body key to any resolution on the tax issue, are lining up behind a plan drawn up by Sens. Jon Kyl (R., Ariz.) and Blanche Lincoln (D., Ark.) that would impose a 35% top rate and a $5 million exemption.

Of the 260 candidates for the Nov. 2 elections who have signed the pledge to eliminate the tax, 253 are Republicans, and two are Democrats, according the American Family Business Institute, the advocacy group behind it.

Sen. Jim DeMint (R., S.C.), a leader of the repeal camp in the Senate, said he hoped the 2010 elections would generate "the momentum to finally kill the death tax for good," using the conservative shorthand for the estate tax. Sen. Bernie Sanders (I., Vt.), who is leading a drive by congressional liberals for higher rates on large estates, called the repeal effort "morally obscene." But he said in an interview he was worried by its renewed momentum.

The repeal effort has been underway since the early 1990s. Former President George W. Bush promised in his 2000 campaign to abolish it.

Because of the loss of tax revenue, Congress chose to lower the rate gradually from 55% to 45% between 2001 and 2009, while increasing the exemption from $1 million to $3.5 million. Lawmakers limited outright repeal to 2010, the final year of Mr. Bush's tax-cut legislation.

In a 2009 poll by the nonprofit Tax Foundation, two-thirds of respondents said they favored estate-tax repeal, even though the tax was levied on only about 5,500 estates that year. The online survey of 2,002 adults aged 18 or older also showed that the estate tax is viewed as the most unfair federal tax, in part because the income being passed along has already been taxed by the federal government at least once.

Opponents of a full repeal argue it is largely a campaign by the richest Americans to safeguard their fortunes. They say the estate tax helps prevent the perpetuation of wealth.

Repeal proponents play down the role of the wealthy in their effort, saying such families often find ways to avoid the estate tax already. Instead, they say the tax mostly hits family-business owners and landowners.

Recession-hit areas can lag for years

By Sara Murray

Communities hit hardest during the recession could continue to fall behind the rest of the country for decades, research released by the Brookings Institution's Hamilton Project suggests.

In regions that suffered disproportionately in the recession of the early 1980s, for example, average earnings have risen at a quarter of the rate of the rest of the U.S. Employment grew more slowly, young people left the region, population growth slowed and, as a result, demand for housing weakened. A similar fate could be in store for areas of the country that faced the deepest housing and employment shocks in the latest downturn, the report warned. To avoid repeating the scenario that followed the 1980s downturn, papers commissioned by the Hamilton Project—formed by some Clinton administration Democrats to devise policies to improve the economy—recommended revitalization efforts targeting the worst-off communities.

White House, Chamber have a shot at reconciling

[Capital Journal]

By Gerald F. Seib

Perhaps, unlike Humphrey Bogart and Claude Rains in "Casablanca," the Obama White House and the U.S. Chamber of Commerce were never destined for a beautiful friendship.

But this? The White House implying the Chamber is illegally using foreign money to defeat Democrats in the midterm election? The Chamber accusing the White House of a smear campaign and intimidation? The nation's premier political institution and its most visible business institution sit about a block apart in Washington, but right now they are Mars and Venus.

It's easy to forget amid today's poisonous campaign atmosphere, but relations between the administration and the Chamber actually were reasonably cordial and productive at the outset. So how did things turn so sour? A long talk with Chamber Chief Executive Thomas Donohue sheds some light—and offers some hope for a rapprochement after Nov. 2.

First, Mr. Donohue underscores the notion that there was, at the outset, some mutually beneficial cooperation, starting with Chamber endorsement of President Barack Obama's big economic-stimulus legislation.

"Not only did we help with stimulus, but we did it when a good portion of the Chamber members were probably not happy about that," he says. "We did it because this institution fundamentally believed that America had a role to play in avoiding the globe from going into a global depression."

He also says he provided rhetorical support for the president's controversial rescue of General Motors, backed the cash-for-clunkers plan, and strongly supported Education Secretary Arne Duncan's education reforms.

But the conversation suggests three forces began to push the relationship off the tracks. First, while the business community—with the Chamber as its voice—had long called for a health-care overhaul, the health bill it saw wasn't what it bargained for.

Second, while the Chamber acknowledged the need for a new regulatory scheme for Wall Street, it decided the final version was too onerous—requiring, Mr. Donohue maintains, more than 500 new regulations. "My grandchildren will be working on that when they retire," he says.

Third, climate change really spoiled the climate. The Chamber went all out to defeat the kind of cap-and-trade approach embodied in a House bill, which the White House viewed positively. A few businesses quit the Chamber in protest over its climate-change stance—and Mr. Donohue asserts the White House encouraged others to follow.

But it's also clear a lot of the problem is atmospherics.

"You know what we did that really angered them?" Mr. Donohue says. "We started asking questions....We weren't having a war. We were having a debate in the legislative process."

The White House, in turn, cut back on communications with the Chamber, and courted individual CEOs as an alternative. Rhetoric on both sides got rough. "It got damn personal over here," Mr. Donohue says.

The White House view is different, of course. There, officials think the Chamber was happy to watch the administration finish bailing out big financial firms, and backed the stimulus package, but headed for the hills when the political winds shifted on those initiatives. They argue the Chamber has never appreciated how, in the fevered atmosphere of the deep recession, the White House held the line against far more drastic solutions some were advocating, including nationalizing banks and car companies.

Administration officials also think a lot of the tension simply boils down to taxes: The Chamber and its members want lower rates, personal and corporate, than the administration favors.

All those tensions were carried into an already-tense election season. But what about after Nov. 2? Mr. Donohue insists he has no desire to extend the arguing: "I would say the Hatfields and the McCoys are not feuding. I would say that we have established our bona fides on helping do what's good for this country and the business community." He adds: "My members don't want me in great big fights. What the hell good is that for them?"

The Chamber's CEO notes that a lot of tensions aren't with the White House but with Democrats in a Congress that is about to undergo a makeover.

He also notes that a lot of tensions aren't with the White House but with Democrats in a Congress that is about to undergo a makeover.

Mr. Donohue mourns the departure of White House Chief of Staff Rahm Emanuel, a "moderating guy," but also calls his replacement, Pete Rouse, "a moderate and thoughtful guy." If the "right people" call, serious conversations will resume.

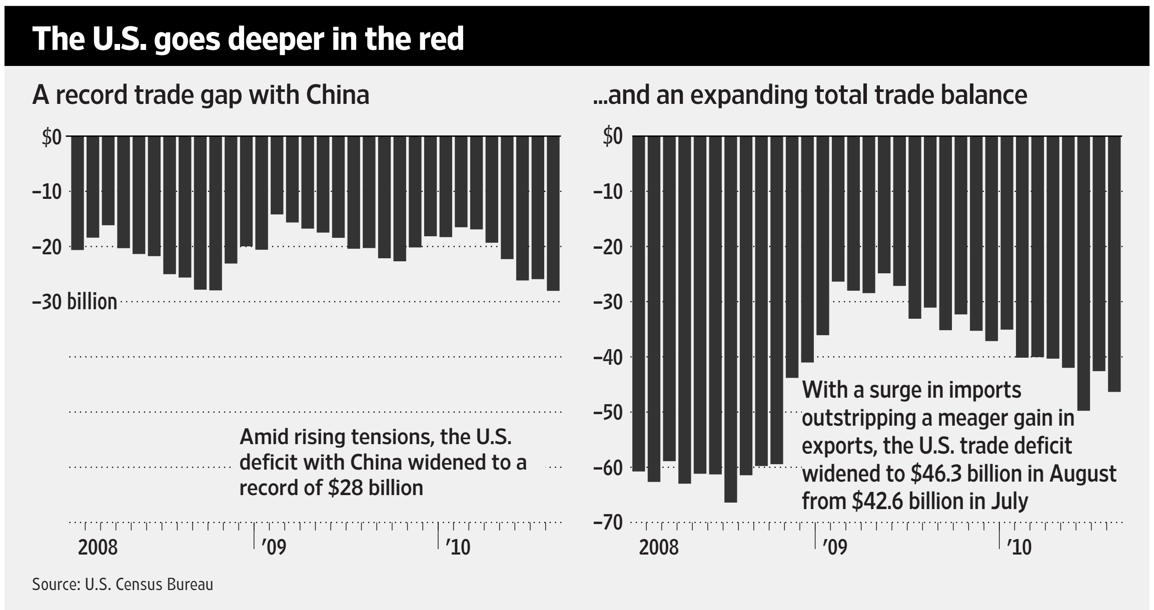
That would be a good thing. Above all, America's leaders will need to set out right after the election figuring out how to tackle a dangerous long-term budget deficit. That will require all big players—Democrat and Republican, business and labor—to be at the table, each willing to agree on things that will make some of their constituents unhappy.

At that point, better if the White House and the Chamber are watching each other's backs, not stabbing them.

U.S. NEWS

Trade deficit grows as imports surge

By Justin Lahart
And Bob Davis



A jump in the U.S. trade deficit in August—the result of soaring imports, particularly from China—adds fuel to the debate over China's trade practices.

The U.S. deficit hit $46.3 billion in August, up from $42.6 billion the month before.

The jump came from a $4.1 billion increase in imports which far exceeded the $239 million increase in U.S. exports during the month. A wider trade deficit is a drag on domestic growth, because it means more of what the nation is consuming is coming from overseas rather than from production at home.

The trade report highlights "how growth in the third quarter might not be as strong as it looked like it might be," said Capital Economics economist Paul Dales.

Many economists trimmed estimates for the third quarter growth, based on the trade numbers. Zach Pandl, an economist at Nomura Securities, cut his estimate to a 1.5% annual rate, down from 2.2%. Mr. Pandl said he thought the surge in the trade deficit in the second quarter was a temporary phenomenon, but the August figures suggest that it wasn't.

Morgan Stanley economists dropped their GDP growth estimate to 1.8% from 2.1%, while St. Louis-based economic consulting firm Macroeconomic Advisers lowered its estimate to 1.2% from 1.6%. Nomura Securities cut to 1.5% from 2.2%.

The U.S.'s trade shortfall with the euro-area, which continues to suffer from anemic growth and a sovereign debt crisis, fell 20.8% to $6.46 billion from $8.16 billion.

The deficit with China widened to a record $28 billion in August from $25.9 billion in July. With many Americans becoming increasingly hostile toward trade with China, the growing gap is bound to redouble U.S. efforts to pressure Beijing to raise the value of its currency. The currency battles will be on center stage next week at a finance ministers' meeting of the Group of 20 industrialized and developing nations taking place in South Korea. The ministers are meeting to prepare a G-20 leaders' summit in November.

U.S. Treasury Secretary Timothy Geithner recently called for China to boost the yuan at a "gradual but still significant rate." He also has made clear that he is looking for China to match the 20% appreciation it managed between 2006 and 2008.

At the annual meeting of the International Monetary Fund this past weekend, Yi Gang, deputy governor of China's central bank, made clear that Beijing wasn't interested in a 20% increase.

On Friday, the Treasury is due to announce whether China is "manipulating" its currency, in a semi-annual report required by U.S. trade law. The Treasury is likely to delay the release, portraying the delay as a way to give China further time to work out policy changes. Mr. Geithner has said the manipulation designation can be counterproductive. It simply requires the U.S. to negotiate with Beijing on currency, which it already is, and raises the risk of Chinese retaliation against U.S. firms doing business in China.

Even if China does boost the yuan's value, many industries that have left the U.S. say they are unlikely to bring those jobs back to America. Stockton, Calif.-based **California Pencil Products** Co. makes thin pieces of wood, called slats, for pencil production. It used to make them in the U.S. but shifted production to Tianjin, China, earlier this decade. It was either that or be forced out of business by global competitors, said company president Charles Berolzheimer.

But lower wages aren't the only reason to be in China now—it is also where the customers are. "The reality is there's not a lot of U.S.-based production these days," Mr. Berolzheimer said.

Meanwhile, separate reports showed initial claims for jobless benefits increased in the latest week, while wholesale inflation accelerated in September on the back of a jump in volatile food prices.

Initial U.S. unemployment claims rose by 13,000 to 462,000 in the week ended Oct. 9, the Labor Department said in its weekly report Thursday. New claims for the previous week, ended Oct. 2, were revised upward to 449,000 from 445,000.

The tough labor market is likely to be a key issue in Nov. 2 elections as Democrats try to maintain their majority in Congress. That is also the first day of the Federal Reserve's two-day Federal Open Market Committee meeting, where Fed officials are likely to take additional action to help spur more economic growth.

—Luca Di Leo and Sarah N. Lynch contributed to this article.

Spotting the likely voters holds key to predictions

[Poll Watch]

Peter A. Brown

When Gallup questioned potential voters recently, it found the U.S. could either be headed for a Republican landslide or for just a normal off-year election loss for the party controlling the White House—the Democrats.

The difference depended on who the polling firm decided was likely to go to the polls. In one scenario, Gallup saw the GOP with a three-point lead nationally; in another, the margin was 17 percentage points.

How Gallup and other pollsters make that determination dictates forecasts for November and explains much, if not most, of the fog surrounding the size of expected Republican victories.

Firms carry out polls of registered voters long before Election Day, but as they get closer to voting time, most begin to screen just for those likely to vote.

In off-year elections especially, when turnout is generally lower than in presidential years, the accuracy of a pollster's determination of who is a likely voter is the key to being right or wrong. Simply put, the electorate in normal off-year elections is whiter and older than the one that votes in presidential elections.

And this year, an unusually large dose of Republican intensity is changing the face of the likely electorate even more than normal.

Party allegiance often changes over time. In 2006 and 2008 that meant a Democratic edge; this year it goes the other way. In Florida in 2008, the exit polls found the electorate was 37% Democratic, 34% Republican and 28% independent.

This month, a Quinnipiac University poll found the likely electorate 36% Republican, 31% Democratic and 28% independent.

Gallup, which doesn't carry out state-by-state polls, is finding much the same thing on a national scale. In its most recent survey of 2,747 registered voters, among whom there were 1,953 likely voters, it found the enormous divergence in the views of the two groups.

Registered voters said by 47%-44% that they would vote Republican for Congress. But among likely voters, the GOP margin is either 13 or 17 points, depending on whether there is a low turnout or high turnout.

In either case, a double-digit lead in the "generic ballot"—whether a respondent says he or she will vote for a Republican or a Democrat for Congress—would almost certainly mean a GOP landslide. And that's why the difference between registered and likely voters is so important.

Peter A. Brown is assistant director of the Quinnipiac University Polling Institute.

WORLD NEWS

Ahmadinejad caps Lebanon visit with praise for Hezbollah

Agence France-Presse/Getty Images

Iranian President Mahmoud Ahmadinejad, flanked by bodyguards, is surrounded by supporters trying to shake his hand Thursday in the southern Lebanese village of Qana. Lebanon's Shiite Muslim population, concentrated in sections of Beirut and in southern Lebanon, has given a hero's welcome to the Iranian president.

China takes old path in quest for new self: the 5-year plan

By Andrew Batson

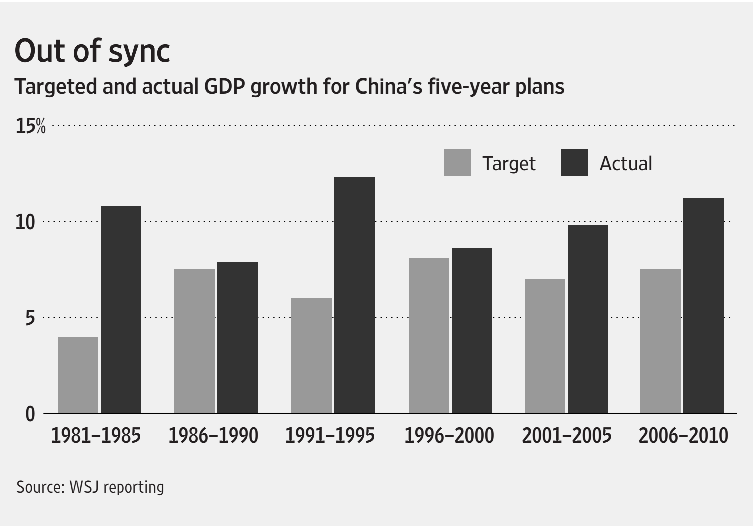
BEIJING—China's leadership is aiming to use a sweeping twice-a-decade economic and social plan to set the country on a more equitable and sustainable path, but there are questions whether the old-style five-year plan can get it there.

The Communist Party leadership will discuss and approve an outline of the massive blueprint, which sets the nation's priorities for the years 2011 to 2015, at a major meeting that starts Friday, before the final plan is published next year.

The broad outlines of the next five-year plan are known even if the precise contents are still secret: In recent speeches, President Hu Jintao and Premier Wen Jiabao—who are set to hand over power to a new generation of leaders two to three years from now—have made clear their ambition to steer China away from a focus on growth and toward a society more befitting the world's second-largest economy.

Mr. Wen has said the government will "reverse the trend of widening income gap as quickly as possible" while Mr. Hu has said the government will "institute a social safety net that covers all." Economists expect the coming five-year plan to give government officials new targets to meet in terms of boosting consumption and incomes, expanding public services and preventing climate change.

China's five-year plans have come a long way since the first was launched in 1953 with a call for self-sufficiency in industry. But their lofty goals don't always translate well into concrete action: Ensuring that directives from Beijing are actually carried out in the nation's hundreds of cities and thousands of villages is a monumental challenge.



"While the Beijing leadership can reach consensus on policy, it doesn't have the capacity to implement those policies effectively because of the divergent interests of localities," said Huang Jing, a political scientist at the Lee Kuan Yew School of Public Policy in Singapore. "Whatever policy is made by Beijing, it will be distorted in the implementation by local governments."

Some targets in past five-year plans—like economic growth—are routinely exceeded by large margins, while performance lags on other indicators like boosting research and the service sector.

Particularly problematic has been the current plan's signature target: a reduction in energy intensity—the amount of energy used to produce each dollar of economic output—by 20% from 2006 to 2010. That goal is key to the current administration's push to reduce China's pollution and reliance on imported resources.

While China's energy intensity had dropped 15.6% by the end of 2009, it actually rose in the first quarter of the year amid a stimulus-driven construction boom. The government now says efficiency improvements have resumed and the target is on track to be met. But the episode highlighted the challenges the current administration faces as it tries to use the old five-year plan system for a new agenda of structural change to China's economy. Some economists argue, for instance, that liberalizing state-set prices for energy would work better than imposing administrative targets for efficiency.

With economic performance the key to advancement, local officials tend to compete to deliver higher growth and treat other directives as secondary. The end result: Growth has averaged over 11% since 2006.

So some economists have argued for setting a lower growth target of 7% in the next five-year plan, to take account of the weaker global economy and de-emphasize the pursuit of growth above all else.

"The key is getting local governments to change from pursuing GDP growth to pursuing targets like increasing public services and higher average incomes," said Hu Angang, an economist at Tsinghua University who has worked on the last three five-year plans. He hopes to see that transition completed by the end of the next plan in 2015.

"We need to pursue appropriate and high-quality growth in the future, not just fast growth," he said.

Outlook for output stays flat for OPEC

VIENNA—The Organization of Petroleum Exporting Countries decided to keep its production policy unchanged, amid strong oil prices and concerns about the health of economic recovery and the weak U.S. dollar that is undercutting the purchasing power of many OPEC states.

*By **Spencer Swartz, Benoit Faucon** and **Summer Said***

The decision was confirmed by OPEC President Wilson Pastor following a ministerial meeting Thursday afternoon. "It's officially a no change," an OPEC delegate said.

The group's 12 ministers, meeting for the first time since March, decided to keep their production quotas at the level they have been since December 2008. The move follows similar decisions by OPEC in 2009 and in March 2010 to maintain the current quota system.

The cartel's decision, widely expected, comes as oil producers continue to enjoy strong and consistent prices. At the same time, the decision came flagged with concern about the uncertainty over the health of recovery and the weak U.S. dollar that is undercutting the purchasing power of many OPEC states.

The move reflected most members' relative contentment with prices. OPEC, whose crude accounts for four out of every 10 barrels burned globally daily, has been in a comfortable position for months, benefiting from rising oil prices while producing a lot more crude than its output quotas technically permit.

Some OPEC states are hankering for even higher oil prices in the months ahead. "I think $100 is a perfect price for next year," Shokri Ghanem, the head of the **Libyan National Oil** Co., told journalists here at the group's headquarters.

But that sentiment jarred OPEC's most important member, Saudi Arabia. The kingdom, the world's largest crude exporter, said it prefers an oil price between $70 and $80, a level widely seen among many oil-producing and consuming nations as adequate to support oil-drilling investments without financially hammering consumers.

Saudi oil minister Ali Naimi said the kingdom was "very happy with how things are in the market" and played down calls from some hawkish ministers—under pressure at home from fragile economies—for higher prices to compensate for a weaker U.S. dollar against the euro and other currencies. "Everybody has their own opinion. We [in the kingdom] are happy with the way the market is," Mr. Naimi said.

Mr. Naimi's comments carry weight because Saudi Arabia sits on roughly 4.5 million barrels a day of spare oil pumping capacity that can be tapped to keep oil inventory—which OPEC watches closely to influence prices—at healthy levels and, thus, to put a lid on runaway prices. Mr. Naimi said the kingdom was producing about 8.1 million barrels a day and said it would satisfy all customer demand for more oil, if requested.