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Agence France-Presse/Getty Images

A woman walks past a share-price board in the window of a securities firm in Tokyo. Japanese shares rebounded sharply on Wednesday, after the government intervened in the foreign-exchange markets in an attempt to drive the value of the yen lower

Japan spends big to arrest surge in yen

A wave of foreign-exchange market intervention by Japan estimated at roughly $20 billion sent the dollar sharply higher against the yen Wednesday, a successful beginning to what appears to be a campaign by Tokyo to stop a soaring yen that threatens to cripple its fragile economy.

*By **Takashi Nakamichi** and **Takashi Mochizuki** in Tokyo and **Tom Lauricella** in New York*

Although Japanese officials have for weeks signaled their unhappiness with the yen's 14% rise in since early May, the currency markets were surprised by the exact timing of the operation and impressed by its size. Traders say that if their estimate for the size of the intervention is accurate, it would likely mark the biggest one-day effort on record by the Bank of Japan to cap the yen.

The initial barrage of yen-selling orders hit the market early in the Asian day as the dollar hit to a new 15-year low below 83 yen, apparently a trigger point for authorities.

The effect of the intervention was swift. The dollar jumped to 84.50 yen and then pushed higher as the Japanese authorities continued selling yen and buying dollars through European and New York trading hours. By late Wednesday, the yen had retreated nearly 3% and the dollar stood at 85.57 yen.

Bank of Japan Gov. Masaaki Shirakawa said in a statement he "strongly expects" the action "will contribute to a stable foreign-exchange rate formation."

Many in the currency market say that while the intervention had a big short-term impact, on its own the long-term effectiveness is questionable. But for now, "it seems there are very few people who are willing to take the other side and fight it," says Douglas Borthwick, a managing director at Faros Trading in Stamford, Conn.

In recent weeks, investors have grown concerned about the impact of the yen's strength on Japan's export-dependent economy. As a result, Japanese stocks surged in the wake of the intervention. The Nikkei Stock Average posted its biggest gain in over five weeks, rising 2.3% to 9516.56 led by exporters such as Toyota Motor Corp. and Sony Corp.

"It's positive as a first move," Okasan Securities

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Yen intervention

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Would you like flies with that? Discerning foodies in U.S. try out insect fare.
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BOE's King tries to sell unions on austerity, saying anger apt

BY NATASHA BRERETON

MANCHESTER, England—Bank of England Gov. Mervyn King sought to win labor unions' understanding of the need for painful fiscal austerity, stressing radical action is vital to reassure investors and to achieve sustainable economic growth.

In a speech Wednesday to the Trades Union Congress—the first by a BOE governor in more than a decade—Mr. King said the public is entitled to be angry about the crisis, adding there is "nothing fair" about it, with its roots in the financial sector and banks being bailed out while the economy suffered.

But he underscored that the U.K.'s large budget deficit needs to be tackled. In the short run, monetary policy is the best tool to manage the recovery, he said, reiterating that the central bank stands ready to add further stimulus if output expands more slowly than expected.

Mr. King's appearance at the congress received a mixed reaction. While Rail, Maritime and Transport union leader Bob Crow's promise to boycott the speech grabbed headlines ahead of the event, delegates listened intently and clapped politely—some of them holding placards reading "Condemn cuts."

In a rare question-and-answer session after his speech, Mr. King drew warm applause when he expressed "enormous sympathy" with public concern over banker bonuses.

"My experience has been ... that most people in this country don't object to people earning more than they do, even a lot more, provided they understand why and can see the contribution that people have made," Mr. King said.

"But when large bonuses are paid to people in organizations that only two years earlier were bailed out by the taxpayer, it becomes somewhat harder to understand."

The answer to this, he said, isn't to focus on the "symptoms" of the problem by trying to reduce banker remuneration with direct controls or an arbitrary ratio, because banks could work around them. The important

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Two years more is hardly a lifetime

[Agenda]

By Patience Wheatcroft

So loud are the howls of protest from his socialist opponents, one might think that President Nicolas Sarkozy of France is about to put the nation's elderly to work in coal mines or turn them into an army of street sweepers. In fact, he is proposing merely to increase the retirement age from 60 to 62 by 2018 and also to increase by two years the age of full pension entitlement. This relatively modest change has provoked thousands of protesters into angry demonstrations and union leaders to threaten a series of strikes. Nevertheless, the National Assembly voted Wednesday to push through the changes. They still need to win the support of the upper house but it seems that the majority in the French parliament is accepting that dealing with the deficit is going to require a degree of sacrifice.

But just how much of a sacrifice dare governments ask of voters? Mr. Sarkozy faced pressure to tackle the pension issue because of a deficit of €10.7 billion ($14.6 billion) in the state pension fund which, without changes, could double by 2030. He is also pledged to reduce the national deficit from its current 8% level. Asking the country to accept a modest cut in its relatively generous retirement provision might seem, to a politician who enjoys his job, a not unreasonable request.

Had the deficit been more than 11%, and rising, how much tougher might Mr. Sarkozy feel obliged to be? In the U.K., Prime Minister David Cameron is wrestling with just such a massive problem and his plans for cutting public spending are meeting with equally vociferous protests to those from across the Channel. This week the U.K.'s major trade union conference, the Trades Union Congress, has been the scene for repeated attacks on the government's strategy and threats to fight them at every stage. The leader of the transport workers union, Bob Crow, even called for a campaign of civil disobedience.

Reuters

President Nicolas Sarkozy speaks with construction workers in Paris Tuesday.

Less hot-headed speakers focused on the belief that the extent and speed of the cuts being advocated by the U.K.'s coalition government risk tipping the country back into recession, a view not restricted to trade unionists but shared by plenty of economists.

> **Some are beginning to question whether the U.K. government will maintain its resolve.**

Addressing the TUC, one economist, Mervyn King, the Governor of the Bank of England, conceded Wednesday that, "There is a perfectly reasonable debate about the precise speed at which to reduce the deficit." But he was adamant that a start had to be made. And he pointed out that the government's current plan, causing such angst among the unions, is "a more gradual fiscal tightening than in some other countries."

Despite that, there are some who are beginning to question whether the government will maintain its resolve to push through the budget cuts, due to be laid out in next month's Comprehensive Spending Review. Only last month a junior minister who suggested that the practice of providing free school milk for children under five might be ended prompted an almost instant retort from the prime minister that this would not happen.

How steadfast will the government's conviction be when special interest groups such as the arts lobby decry any cuts that might be levelled in their direction? Mr. Cameron and his Chancellor, George Osborne, are going to have to be prepared to be some of the most unpopular people in the country for a while.

Mr. King suggested that the trade unions should engage with government in debating what the balance between tax rises and spending cuts should be in the hunt for deficit reduction. That would likely be a fruitless discussion, since most of those gathered at the TUC would happily see income taxes take even more from the rich than the current 50% rate. That this level is already driving talent out of the country and raises little revenue is irrelevant to their conviction.

There is scope, however, for government to listen to the unions on any constructive suggestions that they might have for encouraging business. The latest employment data for the U.K. is mixed, showing a rise in those claiming unemployment benefit while the number of unemployed is marginally down, although that is largely due to people taking part-time jobs.

The unions want to see more people in employment, and paying union subscriptions. Instead of threatening strikes, they could play a constructive part in helping the government figure out how to produce the growth in the economy that is essential if the painful but necessary cuts are not to push the country into a downturn again.

Learning how to govern

Politicians and those who work in government tend to learn on the job. Given the importance of their actions, this should be a cause of some concern.

Next week Oxford University will reveal more of its plans to open a School of Government which will aim to build on, and better, the achievements of institutions such as the Kennedy school at Harvard.

Russian businessman Leonard Blavatnik has pledged at least £75 million ($117 million) to endow the project, which has high-level political endorsement from around the world. Although the numbers of students will be relatively small, the aim is that they will create a global network of people interested in public policy and able to share ideas and learn from others' experiences.

Governments often have to move at speed and under pressure and perhaps do not have the opportunity, or maybe the desire, to examine what has been done elsewhere.

In looking at health policy, for instance, a new minister might pay a quick visit to Sweden or have a look at how the French insurance system works but it is unlikely that he would look at the Thai system, where costs were slashed and outcomes hugely improved. If Oxford can find a way to broaden the focus of policy makers, it will do us all a service.

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Iain Martin on Politics

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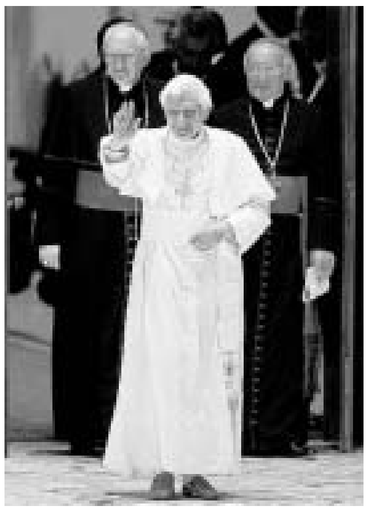
'He bounced into the Commons for PMQs and proceeded to show how much he loves his new job.'

Iain Martin on Cameron's confident display at Prime Minister's Questions

Continuing coverage



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Question of the day

Vote and discuss: Do you agree with France's decision to ban burqas?

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

Previous results

Q: Do you think Nokia's new CEO, Stephen Elop, can rejuvenate the handset giant?

Yes	54%
No	46%

What's News

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NEWS

BP chief faults complacency in Gulf spill

By Guy Chazan

LONDON—In what is likely to be his last public appearance as chief executive of **BP** PLC, Tony Hayward defended his track record before a British parliamentary committee and said the Gulf of Mexico oil spill from a BP well reflected complacency in the industry rather than problems specific to the company.

At a hearing to investigate implications of the April 20 explosion on the Deepwater Horizon rig, which killed 11 workers and triggered the massive spill, Mr. Hayward said oil companies believed they had mitigated the risk of such a deep-sea blowout. "It was a very bad assumption, as it turned out," he said.

Members of parliament quizzed Mr. Hayward on BP's safety record and asked whether the company had cut corners to save money while drilling its Gulf well.

Tim Yeo, chairman of the House of Commons' Committee on Energy and Climate Change, quoted Mr. Hayward as saying he would focus on safety when he became CEO three years ago. And yet on his watch, Mr. Yeo said, "We've had the biggest-ever oil spill in U.S. waters."

Others sought to draw parallels between the Gulf disaster and other incidents in BP's past, such as the explosion and fire at its Texas City, Texas oil refinery in 2005 that killed 15 people, suggesting BP had systemic safety issues—a claim Mr. Hayward dismissed.

But the treatment meted out to him was kid-glove compared with the grilling Mr. Hayward got in the U.S. Congress last June. During his appearance Wednesday, he largely escaped the tongue-lashing that he was subjected to in Washington, and was even asked whether he felt he had been treated poorly in the U.S. Mr. Hayward responded that the emotion and anger in the U.S. was "understandable."

Just over a month after his congressional appearance, Mr. Hayward said he was stepping down as CEO, to be replaced Oct. 1 by Robert Dudley, an American currently in charge of BP's Gulf cleanup operation.

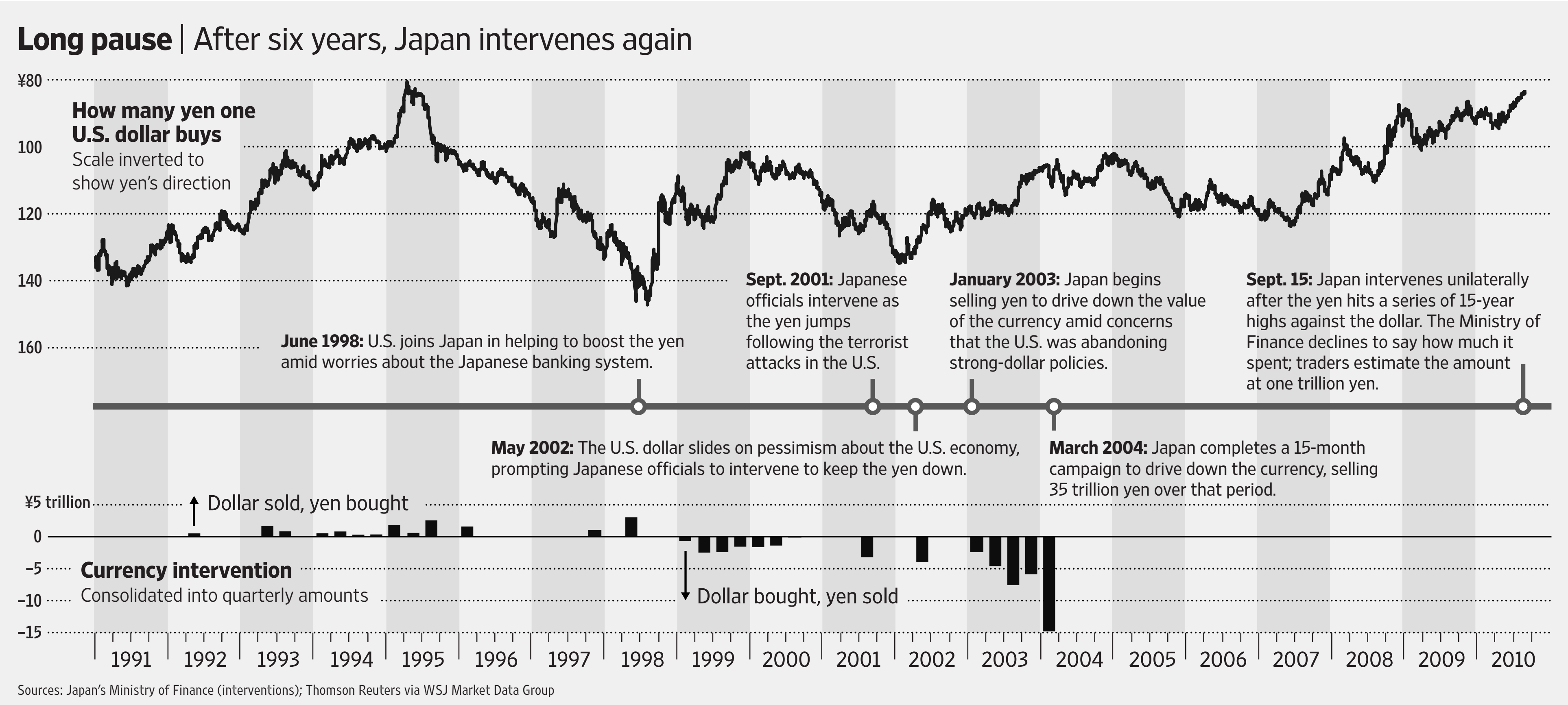
Mr. Hayward said one of the key factors in the disaster was BP's management of "low-probability, high-impact risks." He said BP had identified the risk of an oil spill in the Gulf of Mexico, but the steps it had taken to prepare for such an event were insufficient.

However, he said BP wasn't alone in that. The oil industry had grown complacent after drilling about 5,000 wells in deep water over the last 20 years without a major incident, he said, and no company was prepared to deal with a blowout in water depths of 5,000 feet.

Addressing concerns that the Gulf spill could be repeated in the North Sea, Mr. Hayward insisted BP had a better-than-average safety record there, where deep-water wells tended to be easier to drill than in the Gulf of Mexico.

Meanwhile, he said, BP was building up its capacity to deal with spills in the North Sea.

THE YEN INTERVENTION



Japan's currency move bucks trend

By Alex Frangos

Japan broke international convention and intervened in its currency for the first time in six years.

The question is: Will it work in a world where currency trading is now a $4 trillion affair?

Unilateral currency intervention, once a common tool among industrialized economies, fell out of favor in recent years, amid a perception that it was unfair to trading partners and ineffective over the long term.

"That philosophy of intervention changed because of free-market principles, but also because the foreign-exchange markets are so much bigger. ... You need a lot more firepower to move a major currency these days," says Sean Callow, currency strategist with Westpac in Sydney.

Daily trading in the dollar-yen market is now $568 billion, a 73% increase from when Japan last intervened in 2004, according to the Bank for International Settlements. Around the world, about $4 trillion of currencies changes hands overall daily.

The only other developed country to intervene recently is Switzerland. To fight the euro's fall against the Swiss franc, the Swiss National Bank bought about €90 billion (about $111 billion) before pulling back on serious intervention in June. Despite the intervention, the euro has fallen 12% against the franc this year.

Exactly how much currency Japan injected into currency markets Wednesday isn't clear, but presumably it will need more than last time. When Japan intervened over a 15-month period to March 2004, it pumped 35 trillion yen into markets, or about $320 billion in 2003 exchange rates. In the end, intervention changed little, with the yen trading roughly where it did at the start of the operation.

Hampering its efforts, Japan acted alone on Wednesday, rather than in concert with other central banks.

"To make this move stick, it needs the U.S. to play, as well as the Chinese," says Denis Gould, AXA Investment Managers' director of investment for Asia and Japan. That is unlikely, he says.

"Nobody will do it in a coordinated manner because nobody wants their currency going up," Mr. Gould says. "Everywhere in the world there are problems with economic growth."

The Group of Seven richest economies, of which Japan is a member, have generally agreed in recent years that direct intervention should be used only to counter alarmingly rapid currency jumps, particularly those stemming from speculative attacks. The yen's recent climb doesn't fit that bill.

That means that if the Bank of Japan keeps selling yen on the Ministry of Finance's behalf, U.S. officials and others may start issuing carefully worded criticisms of the Japanese move, making tense international relations on the currency markets even frostier.

Some market watchers say they believe that the intervention, even on this scale, will dodge international criticism, particularly given the yen's surge over recent months to a series of 15-year highs against the dollar. With the Japanese economy looking shaky and exports crucial to its revival, many have seen intervention as the Ministry of Finance's only option, even despite pressure on China to let the yuan rise and fall in line with market forces.

Among developed economies, Japan is highly reliant on exports to drive its growth, and therefore its exchange rate has an outsize impact on its economy.

Before 2004, Japan conducted several currency operations to boost its export sector. In April 1995 Japan intervened. Within a month the yen had weakened 8% and by the end of 1995 it had weakened 23%. A U.S. economic recovery at the time reinforced the dollar's rebound.

Government intervention in currency markets was a cornerstone of economic policy in the 1980s. Two international pacts, the Plaza Accord and the Louvre Accord, ushered in massive, multilateral currency management to adjust the levels of the dollar and the yen in an attempt to promote stability among the world's largest trading powers.

But the ascendancy of free-market thinking in economic-policy circles led to the promotion of letting exchange rates float free of government intervention.

Japan's move, while unlikely to trigger copycats among major economies, comes amid a pullback from the international consensus that governments shouldn't try to tame capital flows.

This year, the International Monetary Fund and the Asian Development Bank separately raised the idea that capital controls are useful for some economies dealing with massive inflows of capital that can lead to asset bubbles and inflation. Such controls could include taxes on investors taking money in or out of a country or minimum periods for which investors would be required to keep money in a particular market.

—Katie Martin in London contributed to this article.

Bank of Japan may not mop up extra yen sold

Continued from first page

strategist Hideyuki Ishiguro said. "The timing came as a surprise," he said, for traders who had believed intervention was less likely after Prime Minister Naoto Kan was re-elected president of the Democratic Party of Japan on Tuesday. Mr. Kan was seen as less inclined to push back against the yen's rise than his opponent.

Corporate leaders in Japan, who had urged the government to act as profits from overseas markets shrank, applauded the news. Sony said it hopes the government will continue to take appropriate steps to stop the yen's rise.

Japan Chamber of Commerce chairman Tadashi Okamura said that had the government not waited so long, "the intervention would have been more effective." He also said that it would be "appropriate" for the dollar to rise to 95 yen.

If history is any guide, Wednesday's intervention was just the opening salvo. When Japan last intervened in the market to push the yen down, it sold an estimated 35 trillion yen ($421 billion) from January 2003 to March 2004.

"More likely than not, more intervention is coming," said Robert Lynch, currency strategist at HSBC Bank in New York. The Japanese government "wouldn't begin an effort like this without thinking it was going to have to be something more than a 'one and done' operation."

Adding extra weight to the intervention are signs that the Bank of Japan is leaving the yen it sold in the financial markets. In the past it has mopped up the extra liquidity—a process known as "sterilization."

A person familiar with the thinking of the Bank of Japan told Dow Jones Newswires that the central bank sees "no need to absorb" the yen sold, since it would blunt the effectiveness of the government's efforts to weaken the currency.

Analysts saw this as an important measure to increase Japan's monetary base and a further weapon to fight a long deflationary spiral that has dragged down the economy. Financial analysts have criticized the central bank for refusing to take strong steps to end Japan's deflationary cycle.

But the Japanese government has a tough battle on its hands. Analysts attribute most of the yen buying to Japanese exporters repatriating profits, and a desire by global investors to park their money in a currency that appeared to have few risks amid a turbulent global economy.

"The yen is rising on the back of global moves to keep home currencies weak and amid continuing expectations for further monetary easing in the U.S.," said Yutaka Miura, senior technical analyst at Mizuho Securities. "Unless there are fundamental changes in these areas, it will not be possible to stem the yen's rise," he added.

Many analysts say a recent increase in China's buying of Japanese government bonds also helped push up the value of the yen. Data from Japan show China's 2010 yen purchases have hit $27 billion, more than six times China's combined yen buying in the previous five years.

The Chinese yuan pared its gains against the dollar on news of the yen intervention. Beijing, which closely manages the value of its own currency, didn't comment on Japan's move Wednesday. China has long rebuffed foreign criticism of its currency practices by saying that countries should have the right to determine their own exchange-rate mechanisms.

Some analysts have speculated that China was intentionally pushing up the yen to aid its own exporters by making Japanese goods more expensive. But there is no evidence to support that, and the composition of their exports is quite different, with Japan more concentrated in capital-intensive goods like cars and advanced equipment than China.

"I don't think Japan's move will have any substantial impact on China's exports," said Liu Yuhui, a researcher on economics and finance at the state-funded Chinese Academy of Social Sciences.

—Jason Dean in Beijing contributed to this article.

THE YEN INTERVENTION

Yen move boosts Japan Inc.

BY MARIKO SANCHANTA AND YOSHIO TAKAHASHI

Getty Images

Exporters should get a lift from a weaker yen. Here, a Japanese worker assembles a Lexus at a Japanese plant in 2006.

Japan's leading exporters, having complained vociferously about the yen's strength for months, cautiously welcomed Wednesday's effort by the government to weaken the currency. But for many, including **Sony** Corp., **Toyota Motor** Corp. and **Nissan Motor** Co., it won't be enough to help this year's profits reach expectations.

That is because the companies' income projections for the rest of the fiscal year, which ends March 31, are betting on an exchange rate of 90 yen to the dollar. The likelihood that Japan's unilateral intervention will weaken the yen to that level or beyond over the next few months is considered slim.

"Whether the intervention can really help car makers depends on how long the intervention continues," said Tatsuya Mizuno, analyst at Mizuno Credit Advisory. "The best scenario is to go back to 90 yen."

Doubters include the chairman of Japan's influential Chamber of Commerce and Industry, Tadashi Okamura, former chairman of **Toshiba** Corp., who said Wednesday he isn't confident the intervention will succeed in raising the dollar into the 90-yen range. It "would have been more effective," he said, if the government had acted earlier.

The strong yen has been a huge concern for the exporters because it hurts them two ways. It makes their products more expensive overseas and reduces the value in yen of their foreign-currency earnings. These companies, with their strong brand names, are the engine of Japan's economy—which recently slipped to No. 3 in the world, behind China.

"If you left the yen's rapid strengthening unmanaged, it would cause severe damage to the Japanese economy, and we think that's why the government and the Bank of Japan have just taken a concrete stance," **Canon** Inc. executive vice president Toshizo Tanaka said. "We think that this step is meaningful as a message to the rest of the world."

Shares of the country's leading exporters rallied following the intervention. Toyota was up 3.8% to 3,010 yen, **Mazda Motor** Co. gained 6.3% to 201 yen, and Sony rose 4.1% to 2,596 yen.

The yen has been strengthening gradually for several years, and auto and electronics companies have sought to adjust by cutting costs and shifting production overseas. But the dramatic rise this year has pushed some to take further steps.

Mazda raised prices of some models in some European markets on July 1 to cope with the yen's strength against the euro. A Mazda spokesman said the company will consider increasing vehicle prices in the future in both Europe and the U.S. if the strength of the yen makes it necessary.

A Toyota spokeswoman said the company hasn't raised prices yet, but last month, Takahiko Ijichi, a senior managing director at the car maker, said it would consider price increases as a way of coping with the yen's strength in the short term.

—Atsuko Fukase, Juro Osawa and In-Soo Nam contributed to this article.

Beginners' guide: How intervention gets done

BY YOREE KOH

The headlines took the finance world by storm Wednesday morning: "Japan's finance ministry intervenes in the foreign-exchange markets for the first time in six years."

But what does that mean exactly? Below is a brief guide to the intricacies involved in Wednesday's yen intervention.

How does intervention happen?

Japan's Ministry of Finance decides the country's currency policy, with the minister, in this case Yoshihiko Noda, giving the final green light. The ministry crafts the entire strategy, including the timing of the intervention and at what levels to step in. Wednesday's intervention involves selling yen and buying U.S. dollars, a move that fattens the country's foreign reserves and increases the yen supply in the market, which dilutes the yen's value.

What prompted the intervention?

The Japanese currency's inexorable surge against the dollar has threatened the country's export-reliant economy. The toll on the shares of exporters has driven the Nikkei Stock Average down considerably this year, as the rising yen made Japanese products less competitive than those of its overseas rivals. The strong yen has also added to deflationary pressures. Market concern mounted around these effects in the last two weeks, and showed itself in full form when the dollar dropped to a 15-year low against the yen Wednesday. The ministry tends to act when it is believed the market has gained a fixed one-sided momentum, in which case the government swoops in from the other side to realign bets to ensure investors believe there is a two-way risk. In other words, it might no longer be as safe as it has been in recent months to keep buying yen.

How do you 'sterilize' intervention? And why would you want to leave it 'unsterilized'?

The ministry's intervention has in a sense tossed the ball into the central bank's court in that it is now up to the Bank of Japan, the institution in charge of monetary policy, to decide whether to let all the new yen slosh around in the market, or to absorb the newly injected supply and thereby "sterilize" the intervention. The Bank of Japan's traditional role is to try to keep the supply-and-demand scales in balance by injecting or taking money out of the market. If the central bank chooses to let the money be, the value of the yen will likely become cheaper against the dollar, a process known as "unsterilizing" the market supply. In this case, a cheaper yen is the ministry's objective.

Why is this a big deal?

It's a big deal because if Japan doesn't tame the strong yen, the impact on its big exporters could mean reduced profits and investment and threaten the country's economic recovery. That is why in a single day, Japan spent a trillion yen, or about $20 billion, in what will need to be a sustained effort if it is to succeed.

Quick fix leaves problems lingering

BY YUKA HAYASHI

TOKYO—The Japanese government's currency-market intervention Wednesday was an attempt to apply short-term emergency treatment to rapidly deteriorating economic conditions, while avoiding measures to address the underlying causes.

One reason policy makers resorted to intervention, despite widespread doubt about its effectiveness: They have largely exhausted their options for more-powerful cures. After nearly two decades of trying to prop up the economy with extensive fiscal and monetary steps, Japan is grappling with government debts nearly twice the size of its economy, and interest rates hovering at or near zero since the mid-1990s.

Wednesday's trillion-yen currency-dumping operation was immediately effective in pushing the Japanese currency down sharply against the dollar and the euro, and then pushing up Japanese stocks. But it did nothing to address what many economists consider to be the key drivers of the yen's recent rise. One is the fact that American and European central banks have more room to lower rates than their Tokyo counterparts, boosting the relative value of yen-denominated assets. Another is Japan's persistent deflation, which also makes the yen—and yen-based investments—grow in value, compared with other currencies.

Behind those problems, Japan has for years dragged its feet on implementing more-painful steps to fix structural problems, such as a hefty dependence on profits generated from exports. Lingering regulation has left domestic sectors, such as finance and retail, ineffective and weak. And women's participation in the workplace remains low.

Tokyo Stock Exchange President Atsushi Saito called the intervention merely "symptomatic therapy."

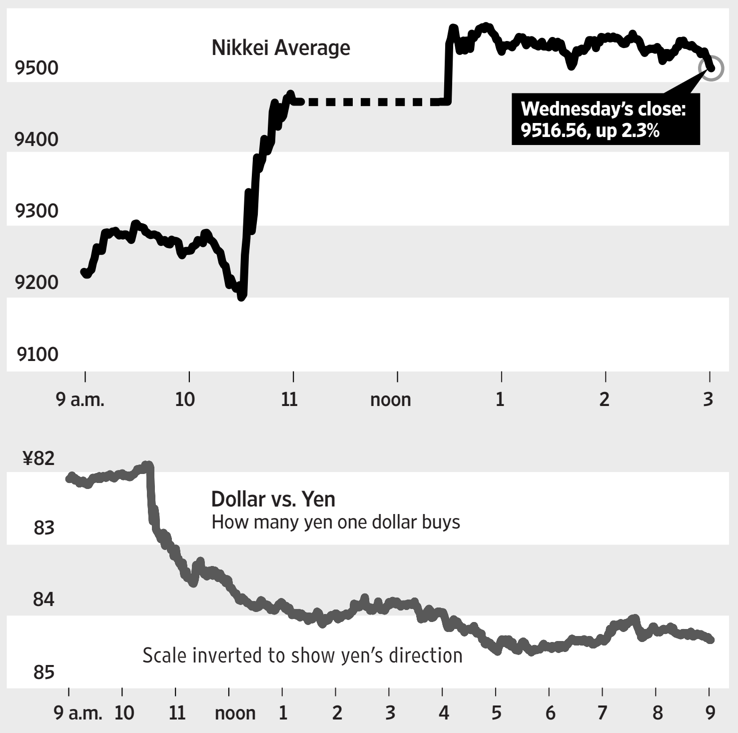
"Intervention is like putting a Band-Aid on a person—in this case a country bleeding from deflation. ... This [intervention] is not a fundamental solution," added Okasan Securities strategist Hideyuki Ishiguro.

Any short-term relief provided by the currency move could even delay further reforms. "We are worried that by providing temporary relief from the pain of a strong yen, [the intervention] will again allow Japan to postpone steps needed to address fundamental problems it must solve," said Hiroshi Shiraishi, an economist for BNP Paribas in Tokyo.

The yen's steady rise in recent months has played a role in dampening what had been a moderately optimistic outlook for the Japanese economy. A higher yen threatens to undermine business confidence by shrinking yen-based revenues for Japanese exporters. It also can undermine employment by causing manufacturers to shift production overseas. The annualized rate of growth in the Japanese economy slowed sharply to 1.5% in the April-June quarter, compared with 5% in the first quarter. Economists say a higher yen, and slowing momentum in overseas markets, could limit Japan's growth further in coming quarters.

Separate ways

Japanese stocks surged while the yen retreated after the government intervened in the currency market. Minute-by-minute Wednesday.



Note: Times are local

Source: Thomson Reuters

Religion remains U.K. issue

Pope is arriving in a country where anti-Catholicism has diminished, but still exists

By Dave Kansas
And Stacy Meichtry

Pope Benedict XVI arrives Thursday in the U.K., a country where anti-Catholic sentiment has diminished but still bubbles beneath the surface.

Catholics now hold important public positions, mostly without fanfare. In the past decade, immigrants from predominantly Catholic countries in Europe, especially Poland, have boosted church attendance and given Catholics a more cosmopolitan profile. Recent Catholic converts include former Prime Minister Tony Blair, who waited to leave office to do so.

Francis Campbell, the first Roman Catholic to hold the post of British ambassador to the Holy See, said British Catholics have largely overcome their onetime status as outsiders in British society. But, he said, the pope tends revive the "old ghosts" of British anti-Catholicism. Until 2005, Catholics were legally barred from serving as ambassador to the Vatican.

Most of the protesting in England will come from nonreligious political pressure groups focused on social issues such as gay rights or abortion rights.

David Voas, a professor of population studies at the University of Manchester who focuses on religious communities, recalls watching an old World War II film that included a scene of British servicemen trying to escape back to the U.K. from behind enemy lines. Moving through Belgium, the group must stay overnight in a Catholic Church. Two Welsh Protestants debate intensely about whether they can set foot inside the church, even though their lives may depend on it. (They stayed at the church.)

"Those kinds of sectarian arguments are inconceivable today," said Mr. Voas. "Just in the past two or three decades, there's been an enormous shift in the whole mindset of Catholics and other people's views of Catholics. Really, it doesn't matter so much anymore."

The U.K.'s anti-Catholic streak, based in the Church of England's breakaway from the Roman Catholic Church in the late 1500s, remained widespread well into the 20th century. For centuries, British Catholics were an eclectic mix of aristocrats who rejected the Church of England and Irish immigrants who arrived mainly in the 19th and 20th centuries.

But the relationship between the Church of England and the Vatican is now largely friendly and the first papal state visit to the U.K. is causing deep sectarian alarm only among a small band of hard-core Protestants.

Outside of England and Wales, relationships between Catholics and Protestants can still be fractious. In Scotland, the country splits roughly down the middle, with Catholics stronger in the West and Protestants, chiefly the Church of Scotland (Presbyterians) stronger in the East. Glasgow is a key flash point, where a football rivalry between Glasgow Celtic, whose backers are predominately Catholic, and Glasgow Rangers, predominately Protestant, is referred to as the Old Firm and can still spark sectarian scuffles.

Protestants in Northern Ireland, and to a lesser degree in Scotland, are also opposing the pope's visit. By contrast, most of the protesting in England will come from nonreligious political pressure groups focused on social issues such as gay rights or abortion rights, underscoring a more common religious-secular divide that has supplanted many of the old sectarian divisions.

Indeed, a number of prominent intellectuals, atheists and celebrities have signed an open letter protesting the pope's visit, citing the Catholic Church's handling of various sexual-abuse scandals and its refusal to ordain women priests or to support reproductive rights, among other issues. The group adds that the pope, as a European and a religious leader, is free to visit his large U.K. flock, but they are vigorously opposed to the pope receiving a state visit.

Reuters

A worker polishes a statue at London's Westminster Cathedral on Wednesday.

The letter comes as the British Broadcasting Corp. highlighted a poll that shows most Britons don't really care about the visit. Newspapers weighed in on everything from the public's share of the visit's cost—£12 million ($18.6 million)—to pedophile priests.

The Vatican said the British media are vastly overstating any apathy or even opposition to the pope's visit.

Inside the Vatican, though, the U.K. is regarded as a bastion of secular thought that runs counter to many of the church's teachings, such as opposition to marriage between gays, abortion and artificial contraception.

In an interview published Monday in the German magazine Focus, the Vatican's recently retired head of ecumenical dialogue, Cardinal Walter Kasper, warned of "an aggressive Neo-atheism [that] is especially prevalent in England. If you wear a cross on British Airways you are discriminated against."

British Airways replied that the "cardinal has been serious misinformed. It is completely untrue that we discriminate against Christians or members of any faith."

On Wednesday, the church said Cardinal Kasper would skip the trip because of health reasons.

The Vatican's concerns about secularity notwithstanding, Catholics have become deeply interwoven into the British social and cultural fabric.

Conservative Prime Minister David Cameron has enthusiastically welcomed the pope and local Catholic bishops have endorsed Mr. Cameron's social programs.

Other prominent British Catholics include the nation's top civil servant, Gus O'Donnell, Mark Thompson, the BBC's director-general, historian Paul Johnson and Lord Patten of Barnes, the last colonial ruler of Hong Kong.

Lord Patten is also the government's point man on the pope's visit.

BOE tries to sell unions on austerity

Continued from first page

thing, he stressed, is to fix the system to ensure that banks never again are in a position to endanger economic prosperity.

Mr. King also sparked laughter and applause with his response to a delegate's proposal that the government close tax loopholes, take decisive action against criminals engaged in massive tax evasion, and raise, rather than reduce, the number of staff involved in doing so.

"The way you put it makes it almost irresistible that one should agree with it," Mr. King said. "I fear I have to say that this is not the responsibility of the bank. ... But I hear your points and they sound persuasive," he quipped.

The major focus of the governor's remarks was the necessity of the coalition government's austerity drive, which plans for a £113 billion ($176 billion) fiscal consolidation over the next five years, based in large part on spending cuts.

This week, the TUC passed a motion approving possible joint union industrial action against the planned public-service cuts, including a call to "support and coordinate campaigning and joint union industrial action nationally and locally in opposition to attacks on jobs, pensions, pay or public services."

Mr. King was contrite about the need for cuts, saying that it was the financial sector and policy makers who had "let it slip" and now the public at large is paying the price.

But he threw the ball back into the unions' court, noting that while there is room for a wide variety of views on how the budget deficit should be reduced, it is "no good just making vague statements."

"It's not enough just to say, 'We shouldn't cut, we shouldn't reduce the deficit,' " Mr. King said, adding that the country can't afford to delay fiscal tightening.

"If you want to oppose what is being done, I think the onus is on those [people] to come up with an alternative, a credible and convincing plan for a better way of reducing the deficit," he said.

"We have," said one delegate.

TUC General Secretary Brendan Barber said members were impressed by Mr. King's willingness to engage with their agenda. "Although [Mr. King] insisted the deficit must be tackled, he clearly recognized that unions had every right to argue for a different timetable and a different balance between spending cuts and tax increases," he said.

A spokesman for the U.K.'s largest union said Mr. King would be better off talking to Chancellor of the Exchequer George Osborne about problems with U.K. banks.

A spokesman for Unite, the U.K.'s largest union, said Mr. King would be better off talking to Chancellor of the Exchequer George Osborne about problems with U.K. banks, rather than trade unions. "Mervyn King says he is willing to listen to alternatives. Using the state-owned banks to pump money into struggling businesses would be a great start," he said.

Meanwhile, Mr. Crow, the Rail, Maritime and Transport union leader, said he found it patronizing that Mr. King was given 45 minutes to lecture the TUC while some delegates had only three minutes to speak. "Does anyone honestly believe that when Mervyn King left here at lunchtime he went back to the Bank of England and said: 'Do you know what? I think the TUC are right. I think we should change the way that we go forward in future.' "

"If it's not the workers' fault, why have the workers got to pay for it?"

Lawmakers in France extend age to retire

By David Gauthier-Villars

PARIS—France's National Assembly voted to raise the retirement age Wednesday, bolstering the government's plan to fix its debt-choked pension system.

The plan, pushed by the government of President Nicolas Sarkozy, would raise the standard retirement age to 62 years from its current 60. The bill is scheduled to be taken up by the Senate—the upper chamber of France's parliament—later this month.

Labor unions have vowed to keep fighting against an "unfair and unacceptable" plan with a nationwide strike and rallies on Sept. 23.

The proposed pension overhaul is a major test of Mr. Sarkozy's capacity to govern France, at a time when the president is facing a variety of troubles. In particular, his government is under fire from the European Union over its deportation of foreign Gypsies, also known as Roma, over the summer. Also on Wednesday, EU Justice Commissioner Viviane Reding demanded an explanation of France's expulsions of Roma.

The National Assembly, where Mr. Sarkozy's ruling Union pour un Mouvement Populaire party has a majority, passed the pension bill by 329 votes to 233 during a turbulent session.

Opposition Socialist lawmakers voted against the bill, saying 60 should remain the standard retirement age. They complained that the lower house's speaker, Bernard Accoyer, had curtailed Wednesday's debate. He said he had decided to fast-track the vote because he thought Socialist lawmakers were "obstructing proceedings." In an attempted filibuster, opposition parties had lined up more than 120 lawmakers to exercise their parliamentary right to give a five-minute speech, in order to upset the bill's passage.

Mr. Sarkozy is trying to fix a shortfall in the nation's mandatory, state-run pension system. The system has been under pressure for several years, because French people are living longer and thus spend more years drawing pensions. But the shortfall widened sharply after last year's recession caused a sharp drop in payroll-tax revenue. This year's shortfall could reach €32 billion ($41.34 billion).

Socialist lawmakers said the recession was caused by the financial crisis, and that ordinary workers are victims of this.

"We can't accept that victims should pay the price for the crisis," said Jean-Marc Ayrault, head of the Socialist lawmakers at the National Assembly, during Wednesday's debate. The Socialists have recommended increasing corporate taxes to balance out the pension system, but Mr. Sarkozy has ruled out such an option, saying France already has some of the highest levies among industrialized countries.

Unions have said they hope to rally more than two million people for nationwide marches on Sept. 23. They say they want the standard retirement age to remain 60, an age adopted in 1983.

EUROPE NEWS

Economy boosts Sweden's Reinfeldt

By Charles Duxbury

STOCKHOLM—Swedish Prime Minister Fredrik Reinfeldt heads into Sunday's general election on the crest of the sharpest economic recovery among Europe's major countries.

As other European governments promise more taxes and expenditure cuts to narrow dangerous budget deficits, Mr. Reinfeldt is offering tax cuts and more spending over the next four years.

It helps explain why one recent poll puts Mr. Reinfeldt's Alliance coalition of center-right parties at 51.7% support, with 42% for the center-left grouping of Social Democrat and Green parties, or Red-Greens.

Behind those numbers is the biggest success story in post-recession Europe, standing out among Sweden's well performing Scandinavian neighbors and even surpassing Norway when oil prices are rebounding.

The pace of the recovery worries the Swedish central bank, which this summer raised interest rates twice to curb inflationary pressures, joining its Norwegian counterpart as the only major central banks in Europe with the confidence to raise the cost of credit.

Sweden's brisk revival after taking a steep dive in the recession came on a combination of early budget tightening, policy responses to the global economic crisis and an export-oriented heavy industry that was well placed to catch the rebound in bigger economies in Europe and overseas.

Economists at Goldman Sachs Global Economics noted Sweden's exposure to a brisk pick-up in world trade. The sum of Sweden's imports and exports amounts to 90% of the country's gross domestic product, twice the level for France, Italy, and Spain, Goldman Sachs said. "Given the importance of capital goods production to the economy, Sweden would benefit disproportionately from the normalization in global investment," Goldman Sachs wrote.

Sweden led Europe's larger economies in the second quarter with a 4.6% annual growth rate that topped even Germany's recovery.

Stockholm's public finances also are better, with a general government budget deficit amounting to only 2.1% of GDP this year, according to the European Commission. That is well inside the European Union's 3% limit that many governments, including Germany, are struggling to reach.

Demotix Images

Prime Miinister Fredrik Reinfeldt during an election rally in Malmö Tuesday.

The opposition Social Democrats, who have governed Sweden for 65 of the past 78 years, rely on a strong Swedish tradition of progressive politics. But its leaders, ousted by Mr. Reinfeldt's 2006 victory, have moved to middle political ground to avoid too stark a contrast with the government's successful economics.

"With the emergence of the two blocs, we thought that the voter would have a clearer choice, but research shows that the blocs have become more similar and been drawn to the middle ground," said Jonas Hinnfors, political-science professor at Göteborg University.

One of the defining policies of the Alliance's four years in office has been a tax reduction for those in work, incentivizing employment over Sweden's generous jobless benefits. This key policy has been widely supported by the Red-Greens, said Göteborg University's Mr. Hinnfors, who expects tax policies to stay the same whoever wins the election.

Mr. Reinfeldt has made himself vulnerable by supporting lower taxes on domestic servants, something critics say favors richer households. On the right, he is coping with some defections to the anti-immigration Swedish Democrats, who, polls suggest, can count on 4.6% of the vote.

Mr. Reinfeldt and his finance minister, Anders Borg, have come in for criticism for the changes they have made to the welfare system in Sweden, particularly sickness and unemployment benefits.

Critics, including Social Democrat leader Mona Sahlin, say this shows that the Alliance favors the strong and disregards the needs of Swedes who are sick or unemployed.

Greece hopes cuts revive confidence

BY TERENCE ROTH

LONDON—The high cost of longer-term Greek government debt can't be sustained over time, but Athens is counting on results from its austerity plan to regain market confidence after the end of this year.

Finance Minister George Papaconstantinou, speaking in an interview between meetings here with investors, said even the €110 billion ($143 billion) in bridging support from the rescue program from the European Union and the International Monetary Fund doesn't fully compensate for being effectively locked out of the capital markets.

"Clearly this is not a tenable long-term situation," he said.

As long as Greece is forced to pay substantially higher rates on its debt than other countries it becomes much harder for Greek banks to wean themselves from special financing from the European Central Bank and stand on their own feet.

On the positive side, Mr. Papaconstantinou said that the government has reduced its budget deficit by just more than half of the €12 billion target set for this year, putting it ahead of schedule.

The program has been accompanied by public protests as austerity packages cut deeply into household incomes.

"It would be impossible to think that pulling €12 billion out of the economy through lower expenditure and higher taxes would not have a detrimental affect on the economy," Mr. Papaconstantinou said.

He said he regretted tough decisions such as cutting pensions, slashing public-sector wages, and raising the value-added tax on retail goods by four percentage points.

"The alternative would be a catastrophe," Mr. Papaconstantinou said. "The alternative would be not having this program and the country going bankrupt."

Since the May rescue package, Athens has been fighting expectations in financial markets that Greece will likely have to restructure its debt if it can't pump more revenue out of a deepening recession.

Mr. Papaconstantinou acknowledged that investors have to be convinced that the government will stay the course, arguing that a welter of economic reforms will soon result in new demand in the economy.

"There will soon come a point when early evidence increases and people say this is an opportunity," the minister said. When that will come, he couldn't predict.

Over the summer, markets have remained skeptical. At stake, market experts calculate, is a potential hit of up to 30% of the value of their Greek holdings if Athens is forced to default.

Greece is in a race against the clock. Its funding requirements for this year are largely satisfied and it needs to raise only €4.8 billion in 2011.

From there it gets progressively steeper. In 2012, Greece has to repay €31.7 billion in principal and €11.1 billion in interest on its bonds, according to market data.

In 2013 total repayments of principal and interest add up to €36.7 billion. And these figures don't include the rollovers of Treasury bills.

Greece also has to repay the various tranches of IMF and EU loans in four to five years and the bulk of amortization is concentrated in the 2014-15 period with about €70 billion of repayments a year.

Mr. Papaconstantinou said even this could be accomplished if Greece has by then regained the confidence of capital markets after Athens returns to primary budget surpluses and economic growth.

Among other early signs, he said, has been the successful capital increase by a major Greek bank and a successful issue this week of shorter-term T-bills, which Greece is still able to sell even as it remains locked out of longer-term bond markets.

Other plans include issuing special bonds to Greek expatriates living and working overseas, representing an asset base often tapped by fiscally stressed governments in

Agence France-Presse/Getty Images

George Papaconstantinou, pictured here in May, said investors have to be convinced Greece will stay the course.

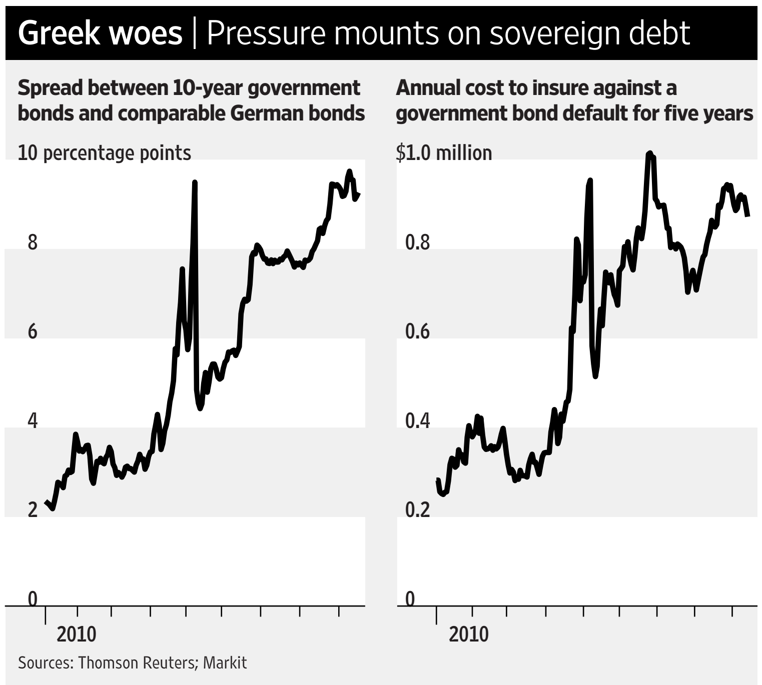
the emerging world. But there are as many Greeks in Europe, the U.S. and elsewhere as there are in Greece, he pointed out. Terms will be favorable, Mr. Papaconstantinou said, but added there would be a special appeal to help the home country.

It would become the latest in a barrage of fiscal decisions made by Europe's busiest finance minister over the past nine months.

So busy, in fact, he paused when asked to recall his worst moment.

"I have many difficult moments over the last nine months," Mr. Papaconstantinou said. "But perhaps some of the worst ones were when we were racing against the clock for the [EU/IMF] support package to be ready in time for Greece to be able to continue to service its debt."

The solution, he said, "came just in time."



Warning signs in U.K. data

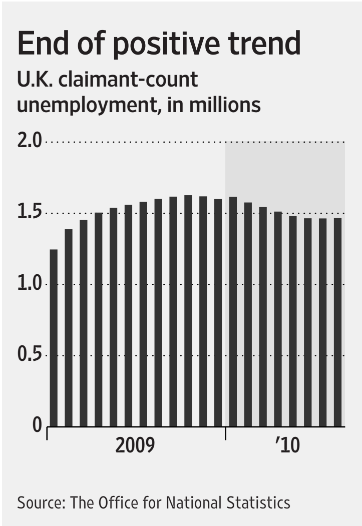
BY ILONA BILLINGTON
AND AINSLEY THOMSON

LONDON—U.K. claimant-count unemployment rose in August for the first time since January, hinting at tough times ahead once government spending cuts begin to bite, data from the Office of National Statistics showed Wednesday.

However, another measure of unemployment, the broader International Labor Organization figure, fell by 8,000 in the three months to July. ILO employment rose by 286,000 over the period, the biggest rise since records began in 1971, the Office of National Statistics said. The widely watched claimant-count measure of unemployment rose by 2,300, giving a jobless rate of 4.5%. That compared with a revised drop of 1,000 and a rate of 4.5% in July.

The rise in the claimant count came as a surprise, as economists had forecast a fall of 5,000. The ONS revised its claimant-count estimate for July after originally reporting a decrease of 3,800.

The government will welcome the news of an increase in employment, to 29.2 million people, the



highest level since last year's first quarter. The record increase reflected new positions in both full-time and part-time employment. Full-time staff numbers rose by 121,000, but part-time jobs grew even more, by 166,000.

The increase in the number of full-time workers was the largest since from April to June 2007, before the global credit crunch.

But the rise in the claimant count, along with recent surveys showing employment intentions on the wane, points to more job losses ahead, said Vicky Redwood, senior U.K. economist for Capital Economics. "Together with the fact that many of the survey measures of employment and employment intentions have started to fall, [the claimant count rise] suggests that the labor market may have reached some sort of turning point—even before the public-sector job cuts start in earnest," she said.

The decline in the ILO's unemployment measure saw the number of jobless total 2.5 million, for an unemployment rate of 7.8% in the three months to July, unchanged from the three months to June.

Separately, the euro zone's annual inflation rate eased in August, indicating the European Central Bank has ample room to maintain its ultra-loose monetary policy.

Average annual inflation in the 16 countries that share the euro fell to 1.6% from 1.7% in July, in line with the preliminary estimate published Aug. 31, Eurostat said.

Irish terror group threatens banks

BY ALISTAIR MACDONALD
AND DAVID ENRICH

Dissident Irish Republican terror group the Real IRA told a British newspaper that it may target banks and bankers in the U.K., a threat that registered a note of familiarity with law enforcement and banking interests that have been monitoring the prospects for such an attack for some time.

The group's leaders told the Guardian newspaper that it wants to target bankers for "financing Britain's colonial and capitalist system" and referred to bankers as criminals for their role in the financial crisis.

Attacks on mainland Britain have all but disappeared following the success of the peace process in Northern Ireland. Still, hard-line Republican groups such as the Real IRA and Continuity IRA have kept up a steady drumbeat of attacks in Northern Ireland over the past year or so. That included the killing of two British soldiers last year.

The Northern Ireland Office issued a statement indicating the public threats aren't new to law enforcement.

The minister for Northern Ireland, Owen Patterson, recently told a parliamentary committee that the U.K. shouldn't underestimate the dangers "a small number of determined people" can present.

"I do not see them destabilizing the political process, but they do present a physical danger," he told the Northern Ireland Affairs Committee.

One person at a London financial institution said that the threat to banks isn't new. The bank's security consultants have been tracking the possibility of a Real IRA attack on banks and bankers for the past 18 months or so. Banks have been monitoring the IRA based on unspecified intelligence that the group could be preparing to target London financial institutions.

U.S. NEWS

Conservatives mobilize, disrupt Republican plans

Associated Press

Christine O'Donnell scored an upset in Delaware's Republican Senate primary.

U.S. Senate candidate Christine O'Donnell's upset primary victory in Delaware Tuesday provided further evidence that conservative voters have mobilized, but the result also demonstrates how the tea party can pose a dilemma for the Republican establishment.

By ***Peter Wallsten, Neil King Jr.*** *And* ***Laura Meckler***

Ms. O'Donnell soundly defeated Republican Party fixture Mike Castle in one of the nation's most Democratic-leaning states. Mr. Castle was considered the strongest candidate to help his party pick up the seat, which until last year was held by Vice President Joe Biden, and strategists in both parties say a Republican victory now appears remote.

In the New Hampshire Republican Senate primary, attorney Ovide Lamontagne made a strong run at the party-backed candidate, former Attorney General Kelly Ayotte.

The state on Wednesday certified Ms. Ayotte as the winner, though Mr. Lamontagne could seek a recount.

In New York, a political novice who claimed the tea-party banner won the Republican nomination for governor, defeating the choice of party leaders, and embattled Democratic Rep. Charles Rangel beat back a primary challenger in Harlem. With 98% of precincts reporting, Carl Paladino, a Buffalo developer, had 62% of the vote to 38% for former Rep. Rick Lazio in the GOP gubernatorial race. The state's attorney general, Andrew Cuomo, is the Democratic nominee for governor.

In Washington, D.C., voters denied a second term to Mayor Adrian Fenty. The campaign had focused in part on Mr. Fenty's support for overhauling city schools and firing underperforming teachers.

The Delaware results were viewed as the most meaningful. With all precincts reporting, Ms. O'Donnell had 53.1% of the vote to Mr. Castle's 46.9%. Mr. Castle, a sitting congressman, is one of the most liberal Republicans in the House.

Still, party officials considered his support for abortion rights, his vote for a "cap and trade" energy bill and other policy stances to be a good fit. Moreover, Delaware voters had elected Mr. Castle to two terms as governor and to nine in Congress.

Ms. O'Donnell, by contrast, opposes abortion rights and, like many Republicans, advocates reducing taxes and federal spending. She called for a two-year elimination of capital-gains taxes. She also opposes the Democrats' health-care overhaul. Her opponents focused on her personal finances. Ms. O'Donnell failed to pay nearly $12,000 in federal taxes in 2005 and defaulted on her house payments in 2007, records show. Ms. O'Donnell drew support from former Alaska Gov. Sarah Palin.

"I'm disappointed" by the Delaware result, said former GOP Sen. Norm Coleman of Minnesota, who is leading a conservative group, American Action Network, that is spending money to help Republicans in congressional races.

"The tea-party movement has been a tremendously positive force, but it doesn't mean that in every state the candidate who is either furthest to the right or the most out of the mainstream is necessarily the best candidate," Mr. Coleman said. He said the O'Donnell win meant the GOP "lost the prospect of a seat.

Strategists in both parties believe the number of competitive Senate races has now dropped to 10 from 11, which means winning the chamber would require Republicans to take every one of those races. Democrats and independents who caucus with them currently hold 59 seats in the 100-member Senate.

Other races of interest:

—In Maryland, the tea party suffered a setback as former Gov. Robert Ehrlich defeated investor Brian Murphy in the Republican gubernatorial primary.

—In New York, Democratic Rep. Charles Rangel, who has represented Harlem for 40 years, won his primary race. It was his first election since the House ethics committee accused him of a series of violations.

U.S. NEWS

Associated Press

Faisal Shazad (above) tried to bomb Times Square in May. Prosecutors say Mohammad Younis was a source of funding.

New charge in bomb plot

By Michael Rothfeld

A New York man was arrested on Wednesday and charged with running an illegal business that helped fund the attempted Times Square bombing earlier this year.

Mohammad Younis, 44 years old, was accused of passing on thousands of dollars to Faisal Shahzad, who has pleaded guilty to a failed attempt to bomb Times Square on May 1. Prosecutors said they had no indication that Mr. Younis knew the money would be involved in preparations for the bombing.

Mr. Younis allegedly gave Mr. Shahzad the money at the direction of an unidentified co-conspirator in Pakistan through an unlicensed money-transfer business known as a hawala, according to an indictment unsealed by federal prosecutors in Manhattan.

He is also accused of transferring tens of thousands of dollars for other customers of his business from January until May of this year.

Mr. Younis pleaded not guilty in federal court in Manhattan Wednesday to charges of conducting an unlicensed money-transmitting business and of conspiracy. He faces a maximum of five years in prison on each charge.

"Mr. Younis has no ties to terrorism," said his attorney, Phil Solages, after the hearing. "Mr. Younis is a hard-working family man."

A hawala is an informal system for making money transfers without the use of banks, a method that can be used to evade government detection. When used for international transfers, money doesn't actually cross national borders but is transferred through a broker who arranges corresponding payments in each country.

U.S. authorities have attempted to step up enforcement of such unlicensed transfers, and to crack down on financing for militants in other countries. Over the last several years, federal prosecutors have brought charges against people across the U.S. in connection with alleged money transfers involving Hamas, al Qaeda, Chechen militants and terrorists in Afghanistan.

Last month, a former Manhattan consultant with McKinsey & Co. was sentenced to 30 months after a jury found him guilty of making money transfers through a hawala involving his relatives in Iran, although there were no allegations the transfers related to terrorism.

Mr. Younis, of Long Island, New York, is accused of speaking to Mr. Shahzad by phone on April 10, less than a month before the bombing attempt, to arrange the payment. He allegedly met Mr. Shahzad to pass the money later the same day on Long Island.

Prosecutors said Mr. Shahzad told investigators that the transfer was arranged by associates of Tehrik-e-Taliban, a militant group in Pakistan that trained him in the use of explosive devices. "By engaging in the alleged conduct, Mohammad Younis unwittingly funded a terror plot that, if successful, would have caused mass casualties in New York City," Preet Bharara, the U.S. Attorney in Manhattan, said in a statement.

On the day of the bombing attempt, Mr. Shahzad, of Shelton, Conn., parked a Nissan Pathfinder near 45th Street and 7th Avenue, and walked away to listen for an explosion, which never happened.

Inside the car, police found several bags of fertilizer, two five-gallon gasoline canisters, 152 M-88 fireworks, three propane canisters and two alarm clocks connected to wires.

Mr. Shahzad pleaded guilty in June in federal court in Manhattan to a 10-count indictment that included charges of conspiracy to use a weapon of mass destruction, attempting an act of terrorism and transportation of an explosive.

—David Benoit and Evan Perez contributed to this article.

Industrial output eases in U.S.

By Luca Di Leo

U.S. industrial production cooled in August, suggesting only weak progress in a key area of support for the economy.

Separately, import prices rose more than expected last month on higher energy and food prices, a move that should contain fears the U.S. economy may fall into deflation.

Industrial production last month increased by just 0.2% as car makers reduced output after a surge in July, the Federal Reserve said Wednesday. July's production figures were revised down to a 0.6% gain from the 1.0% rise initially reported.

Capacity utilization also increased in August, climbing slightly to 74.7% from a revised 74.6% in July. While improving, the operating rates remain well below the 1972-2009 average of 80.6%.

Manufacturing has been a primary driver of growth for the economy as other segments such as consumer spending have remained weak. A rise in retail sales for August provided some hope that consumers are shopping again, but a persistently high unemployment rate and modest wage gains are keeping Americans cautious. Year over year, industrial production was up 6.2% in August.

The industrial production report was just below expectations, with economists surveyed by Dow Jones Newswires forecasting a 0.3% monthly rise in output for August and capacity utilization of 75.0%.

The details of the industrial-production report were mixed. The headline increase was restrained by a 5.2% drop in the production of motor vehicles and parts. Excluding autos, manufacturing output rose 0.5%, the best performance since May.

The sharp drop in car production for August compared with the previous month was influenced by General Motors' decision not to have its usual shutdown of plants in July for retooling.

A separate report from the Labor Department showed that the price of goods imported into the U.S. rose 0.6% in August from July, led by an increase in fuel prices.

With voters deeply divided, strong leadership is crucial

[Capital]

By David Wessel

Even in a country as committed to democracy as the U.S is, economic policy cannot and should not be made by public opinion polls, particularly when the public is so closely divided.

Consider the latest Wall Street Journal/NBC News poll. Respondents were asked which of two statements comes closer to their view: "Government should do more to solve problems and help meet the needs of people" or "Government is doing too many things better left to businesses and individuals." The result: 47% for the first and 47% for the second.

Asked in the same poll if they'd be comfortable with or enthusiastic about a congressional candidate who favored repealing the Obama-backed health-care law, 45% said yes, and 42% said no.

A recent Allstate/National Journal poll gave people three options, and got similar results. The choices: Government should cut taxes, as well as reduce spending and regulation, even if that means a bigger budget deficit (39%). Government should increase spending on infrastructure, education, research and the like even if that means a bigger deficit (33%). Government should reduce the deficit even if that means higher taxes and cutting spending on programs like Medicare and education (20%.)

No wonder certainty, the rallying cry of American business executives these days, is so elusive.

Neither left nor right commands a convincing majority at the moment. Swing voters are in the middle, and they, well, swing. And when they do, so does control of Congress and with it the nation's economic policies. Even if Congress extended all the Bush tax cuts next week, no one would prudently consider the tax issue settled. And it's not at all clear which still-to-be-implemented provisions of the Obama health law will be repealed or starved for funding if Republicans take control of the House.

Americans like change. They voted to reject Republicans and elect Democrats in 2008. It looks like they are about to reject Democrats this November and elect a lot of Republicans. But, cautions Republican pollster Glen Bolger of Public Opinion Strategies, Republicans surely will overinterpret their likely gains as a mandate for their positions—just as Democrats did two years ago.

It's not hard to see now why many voters are rejecting the Obama economic strategy—with blue-collar men, hit hard by the recession, particularly hostile to the president and, at least in polls, more inclined to favor Republican congressional candidates. With a 9.6% jobless rate and little prospect of a quick decline in unemployment, the best Mr. Obama and Democrats can say is "It could have been worse." As Rep. Barney Frank, the Massachusetts Democrat once put it, that isn't a winning bumper sticker for an incumbent.

But with the exception of an aversion to tax increases, it isn't clear what alternative economic policies a Republican Congress would embrace—and the primary victories of GOP insurgents make any semblance of consensus among Republicans even more elusive.

Inside the Beltway, the big question is how Barack Obama will handle a more Republican Congress. When Republicans took the House and Senate in 1995, President Bill Clinton tacked right and, for the most part, outmaneuvered Republican leader Newt Gingrich, though divided government did produce a landmark welfare reform and a modest deficit-reduction compromise before impeachment proceedings erupted.

Mr. Obama could choose to protect his formidable, if somewhat unpopular, legislative victories—namely, financial regulation and health care—and spend two years baiting and bickering with Republicans. Or he could take advantage of any Republican desire to show they can govern by pursuing, say, free-trade pacts or business-friendly tax cuts.

Outside the Beltway, though, the question is less about Mr. Obama and more about whether the political leadership of the U.S. will get anything substantial done at all. It's sometimes said that the best thing Congress can do is nothing, a view that sees gridlock as a welcome respite from activist government. This would be a bad time for that.

In the near term, the economic recovery may need more help from Congress and the president, whether tax cuts or more spending. And without any congressional action, the tax code will do strange things, such as revert to an estate tax of 55% on everything above the first $1 million.

Then there are longer-term issues, though ones that won't wait forever, such as the large cadre of unemployed workers who may never find another good job, a baroque tax code that doesn't foster growth, daunting budget deficits that will loom even after the economy recovers. In a joint appearance in Washington this week, Bush Treasury Secretary Hank Paulson and Clinton Treasury Secretary Bob Rubin both expressed pessimism about the capacity of the political system to cope with the formidable challenges to American prosperity. "Business," Mr. Rubin said, "underestimates the difficulty of issues the government faces."

In the past, divided government occasionally has produced surprising and durable compromises—the Social Security fix of 1983, the Tax Reform Act of 1986. But that requires politicians who spend less energy scoring points before the next election and more on getting something done.

It's called leadership.