## Unrest spreads in Middle East

WORLD NEWS 12-13

## Time for you men to get in the pink

NEWS 3


# THE WALL STREET JOURNAL.

VOL. XXVIII NO. 252 EUROPE Thursday, January 27, 2011

DOWJONES A News Corporation Company europe.WSJ.com


## Medvedev says attack won't crush Russia


Agence France-Presse/Getty Image

Dmitry Medvedev addressed the World Economic Forum on Wednesday. The Russian president gave the keynote speech but canceled most of his appointments after the Moscow airport bombing. **Related article on page 5; Davos coverage on pages 6-9, with updates at WSJ.com/Davos.**

# U.S. deficit is closing in on $1.5 trillion

By Corey Boles

WASHINGTON—The Congressional Budget Office painted a grim picture of the federal government's finances Wednesday, saying the budget deficit would jump to nearly $1.5 trillion in the current fiscal year, largely because of a tax-cut extension enacted last year.

In its twice-annual forecast of the U.S. economy, the nonpartisan agency said the gross domestic product would grow 3.1% in 2011 but the jobless rate would remain high for the foreseeable future. The new forecast compares with a $1.3 trillion deficit in fiscal 2010.

The CBO said the deficit as a share of U.S. gross domestic product would jump to 9.8% in fiscal 2011 from 8.9% in fiscal 2010. That would make the deficit the highest since the 10% mark recorded in fiscal 2009, which was the worst in 65 years. The agency said the deficit as a proportion of GDP would then decline to 7% in fiscal 2012.

The agency said the current unemployment rate of 9.4% would fall to 9.2% by the fourth quarter of 2011 and drop to 8.2% by the end of 2012. It won't revert to its "natural rate" of 5.3% until 2016, the CBO said.

On a positive note, the agency said inflation would remain "very low" through 2012. This news will be welcomed at the Federal Reserve Board, which is watching whether its bond-buying program will fuel inflation.

"Although recent actions by U.S. policymakers should help support further gains in real GDP in 2011, production and employment are likely to stay well below the economy's potential for a number of years," the CBO said.

The tax compromise reached between Democrats and Republicans in December added $858 billion to the federal budget deficit over the next 10 years. The deal renewed Bush-era income-tax rates for all Americans for two years despite the misgivings of many Democrats who wanted to see the rates for wealthiest Americans revert to higher rates.

The accord also reinstated the estate tax at a rate of 35% for individuals with assets worth more than $5 million and couples with assets exceeding $10 million. The tax had expired at the end of 2009 and was set to be re-

*Please turn to page 10*





# Exxon's bullish bet on gas hints at a shift in energy

By Angel Gonzalez

In **Exxon Mobil** Corp.'s crystal ball, the future of natural gas is looking increasingly rosy.

Global demand for natural gas, commonly used for heat and generating electricity, will increase by 2% a year through 2030, the Texas oil giant says, raising its year-ago estimate from 1.8%.

This is no small change. It means that Exxon expects the world in 2030 to burn seven quadrillion British thermal units of gas more than it predicted a year ago. That's about the same amount of energy consumed by California in a year.

While oil will remain the dominant fuel, even in 2030, gas will have nearly closed the gap, according to Exxon's annual Outlook for Energy, scheduled to be released Thursday.

Gas usage is expected to grow three times as fast as oil and coal, as developing countries scramble to bring electricity to billions of people and rich countries replace aging coal-fired power plants with gas-fired facilities, the report says. Clean-burning natural gas represents less of a global warming threat than coal or oil. Other low-emitting forms of energy, such as nuclear and renewable power, are also expected to grow their share of the world's energy pie.

Exxon's Outlook for Energy is closely watched, as it underpins the strategy of the world's largest publicly-traded oil company. "It provides the foundation for the different [Exxon] businesses to present their investment plans," says Bill Colton, the Exxon executive in charge of the outlook.

It's no surprise that Exxon is bullish on natural gas. The company last year became the largest gas producer in the U.S. when it bought XTO Energy Inc. for $25 billion. XTO was one of several North American companies to have

*Please turn to page 3*




THE WALL STREET JOURNAL.

Bahrain BD 1.50 - Egypt $1.75 (C/V) Jordan JD 2 - Kuwait KD 1 - Oman OR 2 Qatar QR14 - Saudi Arabia SR 14 £1.50

PAGE TWO

# Will the stress be stressful enough?

[ Agenda ]

By Simon Nixon

The last set of Europe-wide bank stress tests are now widely considered a joke. In July 2010, Europe's national regulators investigated their banking systems and concluded all they needed to survive their worst-case scenario was €3.5 billion ($4.7 billion) of fresh equity spread across seven banks. Four months later, the Irish banking system imploded, triggering an €85 billion bailout of the entire economy.

Now the European Union is having another go, promising that a new set of stress tests to be conducted this spring will learn the lessons from the past exercise, win vital credibility from the markets and help Europe finally to draw a line under its sovereign-debt crisis.

To do this, of course, it will need to do what it so comprehensively failed to do last time: persuade a ragbag of different European institutions, national governments and regulators to sign up to a coherent, credible, demanding plan rather than settle for the lowest common denominator. What are the chances of that happening? Pretty low, I fear.

The credibility of the tests rests on a whole range of issues on which the EU has yet to agree—and on which a sensible consensus may be hard to reach.

First, there are the stress test scenarios. The scenarios being worked up by the European Central Bank and newly created European Banking Authority will be "plausible" rather than extreme, according to someone familiar with the situation. In other words, they will be outside the market's baseline forecast but won't necessarily exceed its gloomiest forecasts.

That will raise fears that the stress tests will once again be insufficiently stressful and that, as with the Irish economy last year, reality turns out to be worse.

Bloomberg News

A euro sign sculpture at the European Central Bank headquarters in Frankfurt.

The second issue concerns the quality of capital to be tested. The last round of tests required banks to meet a hurdle of only 6% Tier 1 capital, which allows subordinated debt and other quasi-equity instruments to be included, rather than focusing on higher quality Core Tier 1 capital, which was the measure used in the U.S. stress tests in 2009. The reason given last year was that Tier 1 is the only legally defined measure of capital and that Core Tier 1 is not a useful measure for calculating the capital needs of Europe's many savings banks. But the market is likely to blow a very loud raspberry if the EU opts for the same hurdle again, particularly since Basel has introduced a 7% Core Tier 1 minimum and is likely to add a further common equity buffer for the world's largest banks.

The third issue concerns liquidity, the biggest omission of the last tests. What ultimately triggered the collapse of the Irish banking system was that it was running out of eligible collateral it could use to access ECB funding. Many European banks, particularly those from Greece, Spain and Portugal, continue to make heavy use of ECB facilities as they are denied access to market funding. But I understand any liquidity test conducted as part of the new stress test process will be a separate exercise and the results won't be disclosed.

The fourth issue is what approach the new stress tests will take toward sovereign debt. The last tests largely ducked this issue: although it applied haircuts to sovereign bonds held on trading books, it did not do so on bonds held in banking books, which is where the vast majority of banks hold them. What's more, the haircuts assumed in some notable cases were less than the losses implied by market prices. The EBA has not yet decided what approach it will take this time but believes that the extensive disclosure of bond portfolios was one of the successes of the last stress tests, according to someone familiar with its thinking. It seems reasonable to assume it will adopt the same approach again, so it will be left to the market to give the final verdict on the results.

The fifth issue concerns the need for peer review of national results. This is crucial and was missing from the last results. But while peer review is certain to be a feature of the new process, it is unlikely to go nearly far enough. One of the key failings of the Basel capital accords is the wide degree of discretion it hands to individual banks and national regulators to calculate their own capital requirements based on their own internal models. There is widespread suspicion among investors that some regulators have colluded with their banks in the use of overly optimistic assumptions, enabling banks to overstate their regulatory capital ratios. Any credible peer review process must include detailed review of these internal models and the underlying assumptions. This one won't, I am told.

The sixth issue is disclosure. Incredible to relate, but the EU authorities are genuinely debating whether to disclose anything from the stress tests at all. At the heart of the debate is a standoff between the EBA and national governments on whether there will be credible resolution plans for banks that fail. If there isn't a credible plan, the EBA fears disclosure will simply destabilize the system further, according to someone familiar with the situation. Given the blow to confidence if the results aren't disclosed, the EBA should win this game of chicken—but it is astonishing that it has to be played at all.

This inevitably gets to the heart of the final problem with the stress tests—and the reason why the EU is finding it so hard to extricate itself from this crisis. Many of the countries with stressed banking systems do not obviously have the capacity to bail out banks that fail the tests—or at least not without putting huge pressure on their sovereign-credit rating, which will feed back into the banking system via higher funding costs, regardless of how well capitalized are its banks.

The snag is that the only solution to this problem is to use Europe's bailout facilities such as the European Financial Stability Facility to recapitalize the banks and guarantee their debts. That of course is anathema to national governments, who do not want to saddle their taxpayers with the debts of their reckless neighbors. Besides, no government would ever sign up to it without credible stress tests—which brings the argument full circle.

## What's News

■ **A top ECB official urged** euro-zone members to make their crisis fund more flexible so it can buy bonds of fiscally distressed governments and offer short-term credit lines, a signal the bank wants to trim its role in fighting the bloc's debt crisis. 4

■ **The IPO that Glencore** is preparing could be quickly followed by another blockbuster deal: a combination of the Swiss commodities trader with miner Xstrata. 21

■ **Toyota will recall** more than 1.7 million vehicles because of faulty parts including defective fuel devices. 21

■ **SAP's quarterly profit** fell sharply as the software maker took a $1.28 billion charge related to its lawsuit with Oracle, overshadowing strong sales growth. 23, 36

■ **Internet-phone company** Skype won't hold its IPO until the second half of the year, later than some investors had expected. 24

## Inside

How to handle the sympathy when a friend is grieving. 31

Doubling back: Paes and Bhuphati chase an elusive title. 32

## ONLINE TODAY

### Most read in Europe

1. Fighter Jets Escort Plane to U.K.
2. Rep. Ryan Is GOP Point Man
3. Why Chinese Mothers Are Superior
4. U.K. Suffers a Reversal
5. Rioters Rock Egypt

### Most emailed in Europe

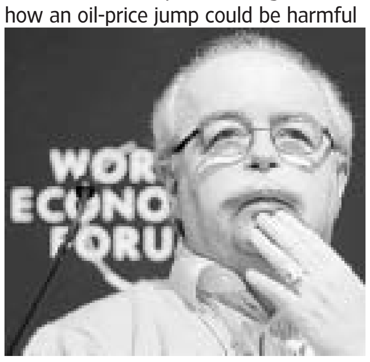
1. Why Chinese Mothers Are Superior
2. Is Barcelona Soccer's Best Team Ever?
3. Karzai to Inaugurate Parliament
4. Santander's Succession Problems
5. Historic Dutch Mansion

### Davos Live

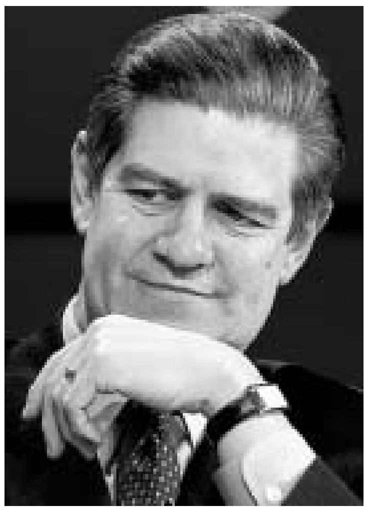
blogs.wsj.com/davos

'$100 a barrel is probably the limit—if it goes too quickly above this level we will be hurt'

Total CEO Christophe de Margerie on how an oil-price jump could be harmful



### Continuing coverage



Follow the latest news and updates from the World Economic Forum in Davos at **wsj.com/davos**

### Question of the day

**Vote and discuss:** Do you expect any achievements to come out of the annual meeting in Davos?

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

### Previous results

**Q:** Is the U.K. headed for a double-dip recession?

| | |
|---|---|
| Yes | 64% |
| No | 36% |

THE WALL STREET JOURNAL EUROPE
(ISSN 0921-99)
Commodity Quay, East Smithfield, London, E1W 1AZ

**SUBSCRIPTIONS, inquiries and address changes to:** Telephone: +44 (0) 20 3426 1234. Calling time from 8 a.m. to 5 p.m. GMT. E-mail: subs.wsje@dowjones.com. Website: www.services.wsje.com

**ADVERTISING SALES** worldwide through Dow Jones International. Frankfurt: 49 69 29725 390; London: 44 203 426 1111; Paris: 331 40 17 17 01.

Printed in Belgium by Concentra Media N.V. Printed in Germany by Dogan Media Group / Hürriyet A.S. Branch Germany. Printed in Switzerland by Zehnder Print AG Wil. Printed in the United Kingdom by Newsfax International Ltd., London. Printed in Italy by Telestampa Centro Italia s.r.l. Printed in Spain by Bermont S.A. Printed in Ireland by Midland Web Printing Ltd. Printed in Israel by The Jerusalem Post Group. Printed in Turkey by GLOBUS Dünya Basinevi.

Registered as a newspaper at the Post Office.

Editeur responsable: Patience Wheatcroft M-17936-2003.
Registered address: Boulevard Brand Whitlock, 87, 1200 Brussels, Belgium

NEWS

Getty Images; Associated Press; Maurits Sillem

From left, men's coats from Jil Sander, Bottega Veneta and Burberry. Designers hope bold colors such as pink and peridot will inspire men to buy new outerwear.

# Amazing Technicolor coats

BY RAY A. SMITH

Gentlemen, you may have the winter blues, but are you ready for winter pinks?

Start bracing yourself. Next fall, stores may be carrying some very colorful overcoats, thanks to designer labels such as Bottega Veneta, Burberry, and Jil Sander. They were among the brands that showed wool and cashmere overcoats in vivid colors such as cherry red, Fanta orange and Pepto-Bismol pink during the men's fall/winter 2011 collections in Milan and Paris this month.

As shocking as the pinks may be, the coats fit in with a series of recent efforts by the menswear industry to push men out of their color comfort zones.

In recent years, American men—long a staid lot when it comes to syle—have responded to designers' promptings to add color to their wardrobes. There was a colorful-striped-shirt craze in 2004, and orange, lilac and cobalt blue showed up on sweaters, shirts and sport coats last spring. Blinding, multicolored plaid shirts have been popular for more than a year, and this spring, some in the fashion industry are pushing colorful trousers.

Still, dressy coats are a new frontier. Overcoats have long been a color-free zone for men, going no brighter than camel.

It's not at all clear that guys will warm up to bright overcoats if menswear designers choose to show them during New York fashion week next month.

Of course, these coats are appearing on European runways first precisely because European men tend to be more open to colorful clothes. Continental men have long worn dress shirts, trousers, jackets and accessories in a wide range of colors, as well as the recent wave of bright-colored cotton and linen pants.

Retailers hope that colorful coats will inspire men to shop because they don't already have such items in their wardrobes.

"It's always color that draws a person to a rack," says Eric Jennings, men's fashion director at Saks Fifth Avenue in New York City. He adds that the retailer plans to carry some of the colored outerwear—"especially in our contemporary zone," which is aimed more at a customer who is very into fashion.

Some of the brightest colors, like other extreme runway looks, could be somewhat toned down by the time they make it to stores. Bottega Veneta called the colors it used in its fall 2011 men's show "Technicolor brights" including "vivid sapphire, peridot, orange resina and a fiery red called corniola."

# *Exxon's bet on gas hints at a shift in energy*

*Continued from first page*

perfected a method to extract gas by fracturing tight rock formations called shales. Exxon also bought small shale producer Ellora Inc. for $695 million and natural gas shale assets from Petrohawk Energy Corp. for $575 million.

But Exxon's enthusiasm comes amid some Wall Street criticism of its recent bets on natural gas, which has traded cheaply since the financial crisis started, while oil has surged of late and thus has been more profitable. And it was a heavy investor in 1970s U.S. shale oil projects that failed to deliver.

Natural gas prices have fallen from above $13 per million British thermal units in mid-2008 to about $4 per million British thermal units in January 2011. Oil prices, on the other hand, were trading as low as $40 per barrel in early 2009 as a result of the recession, but have recovered steadily. On Wednesday, crude futures in New York traded at $87.22 per barrel.

Nonetheless, Exxon, which has its roots in John D. Rockefeller's Standard Oil monopoly, believes the world is tilting toward a natural-gas dominated future and is preparing to embrace it.

Some other large Western energy companies are heading that direction. Earlier this month, Royal Dutch Shell PLC Chief Executive Peter Voser said in an internal publication that, in 2012, the Anglo-Dutch oil giant would for the first time produce more natural gas than oil.

Mary Barcella, a consultant with IHS Cambridge Energy Research Associates, says that new technology underpinning shale-gas discoveries "is a game-changer" that revolutionized the once waning U.S. natural gas business; Exxon and others intend to take that expertise to other regions of the globe.

Exxon's Mr. Colton says that shale and other unconventional types of gas began playing a prominent role in the company's predictions about three years ago, when it realized that a major technological shift had occurred.

Exxon forecasters say that the world will consume about 35% more energy in 2030 than in 2005, driven by population growth and the rapid enrichment of developing nations, especially in the Asia-Pacific region.

Natural gas will quench 26% of the world's demand, up from about 21% in 2005, the report says. That means that gas usage will double from 2000 levels, but a supply crunch is unlikely, due to the newfound abundance of the fuel, says Mr. Colton. "The world is looking at a very robust supply of natural gas," he said.

*—Russell Gold contributed to this article.*

# U.K. police to reopen inquiry on hacking

BY PAUL SONNE AND CASSELL BRYAN-LOW

LONDON—U.K. police said Wednesday that they are reopening an investigation into the reporting tactics of the News of the World tabloid, a move that came as the newspaper announced it had fired a senior editor.

The developments are the latest in a multiyear saga involving the paper's use of private investigators to obtain personal information about celebrities, politicians and other public figures, notably through breaking into mobile-phone voice mailboxes, or hacking.

The News of the World's royal-family correspondent and a private investigator employed by the Sunday tabloid were jailed in 2007 after a two-year investigation found them guilty of hacking into the phone messages of the royal family.

News of the World's parent—**News Corp.**'s News International—initially described the case as the work of a single reporter.

But new information has surfaced through civil suits brought against the paper by a number of people, including actress Sienna Miller.

That led News International to suspend Assistant Editor Ian Edmondson in December following what it called "a serious allegation." The company then launched an internal investigation and material found during that process led to his dismissal, News International said Wednesday.

**News of the World's parent initially described the case as the work of a single reporter. But new information has surfaced through civil suits brought against the paper.**

London's Metropolitan Police Service, known as Scotland Yard, said Wednesday that it received "significant new information" from News International in relation to the allegations of hacking in 2005 and 2006.

"News International has informed the police, and handed over the material it has found and will give its full cooperation going forward," the company said.

Mr. Edmondson didn't respond to requests for comment.

News Corp. also owns Dow Jones & Co., publisher of The Wall Street Journal.

The renewed investigation comes less than a week after the tabloid paper's former top editor, Andy Coulson, resigned his post as U.K. Prime Minister David Cameron's chief media adviser amid continuing scrutiny of the hacking case.

Mr. Coulson, who stepped down as the paper's editor in January 2007, has denied the hacking went beyond the reporter involved, and said he was unaware that such practices were used in his newsroom.

*—Alistair MacDonald contributed to this article.*

# ECB urges flexible crisis fund

By Brian Blackstone
And Nathalie Boschat

PARIS—A top European Central Bank official urged euro-zone governments to make their €440 billion crisis fund more flexible so it can buy bonds of fiscally distressed governments and offer them short-term credit lines. That is a signal the ECB wants to reduce its role in fighting the currency bloc's debt crisis.

Bank of France Governor Christian Noyer, who sits on the ECB's governing council, also said in an interview with The Wall Street Journal that the recent rise in euro-zone inflation should prove temporary, indicating that the ECB isn't in a rush to raise interest rates despite its tough anti-inflation rhetoric.

Mr. Noyer's call for the euro zone's main bailout fund—the European Financial Stability Facility, or EFSF—to weigh bond purchases suggests that ECB officials are anxious to wind down the central bank's own bond-buying program amid signs that economic recovery is taking hold in much of the 17-country currency zone.

The ECB's purchases of government bonds since May have helped to protect financially weak countries such as Ireland and Portugal from an even-greater battering in bond markets.

But the program has drawn fire from the German Bundesbank, which fears that the ECB could lose its independence if it becomes a source of funding for governments.

Mr. Noyer, 60 years old, expressed sympathy for proposals currently being considered by European governments to transfer some or all of the bond-buying activity from the ECB to the bailout fund.

Giving the EFSF the power to buy bonds in financial markets "would probably be an interesting feature in some cases, if only to facilitate access to the market" for governments, Mr. Noyer said.

The ECB has bought €76 billion of struggling euro members' bonds since May. Officials including ECB President Jean-Claude Trichet have signaled a preference for the EFSF to play a broader role in managing the debt crisis on the euro zone's periphery, without being specific. Mr. Noyer is one of the first officials to call openly for the EFSF to assume responsibility for bond purchases.

"Another possibility would be that of precautionary programs [such as credit lines], like what the IMF is doing," Mr. Noyer said.

The IMF has credit lines designed to help otherwise sound countries get through tough patches resulting from a crisis, including Mexico and Poland. Those lines, which don't have to be tapped into, send a signal of confidence to financial markets before conditions erode.

In contrast, the EFSF acts only after a country is effectively shut out of credit markets as a source of funding and has no other recourse than a rescue.

Mr. Noyer argued that the euro zone has responded effectively so far to the crisis of investor confidence in its weakest members' finances, contrary to the view of critics who accuse Europe of dithering in the past year.

But Mr. Noyer called on governments to ensure that the EFSF can use its full lending capacity. The fund is equipped with €440 billion ($602 billion) in credit guarantees, but strict collateral rules and other restrictions mean it can lend closer to only €250 billion.

The fund is the main component of a bailout mechanism that also includes aid from the European Union's executive arm and the IMF.

So far, only Ireland has used the bailout mechanism, but the EFSF could quickly run dry if both Portugal and Spain were to need assistance. That risk has forced governments to discuss ways to boost the EFSF's capacity.

"It is appropriate to think about [enlarging the EFSF] even if there is no immediate need," Mr. Noyer said.

Mr. Noyer cautioned that letting the stability fund come to countries' aid in more flexible ways raises questions about the conditions that should be attached to such support.

Some governments fear that making aid available too easily could reduce pressure on euro members for fiscal discipline.

Mr. Noyer said governments "can probably find answers to that."

Bloomberg News

Bank of France Governor Christian Noyer called on governments to ensure the crisis find can use its full lending capacity.

**WSJ.com**

**ONLINE TODAY:** For the full Q&A with Christian Noyer, go to **WSJ.com/Europe**

# Turkey seeks a time out in monetary adjustments

By Joe Parkinson

ISTANBUL—Turkey's economy minister said the country's central bank should wait before making further changes to monetary policy, the government's first public sign of concern over the bank's unorthodox strategy of cutting interest rates amid booming demand.

"We don't want an uncertain environment in Turkey. After this, for a while, I think watching the results is necessary," deputy prime minister for the economy Ali Babacan told reporters Wednesday in Ankara, before flying to Switzerland for the annual meeting of the World Economic Forum in Davos.

Mr. Babacan said the central bank's policy—cutting interest rates to deter potentially destabilizing inflows of short-term investment, while at the same time raising reserve requirements for commercial banks to rein in a domestic credit boom—was adopted in coordination with other institutions. But his warning over uncertainty followed recent grumbling in the markets that the central bank was failing to explain its complex policy clearly.

Turkey's central bank surprised financial markets last Thursday when it again cut its key interest rate to a record low, triggering a sell-off of Turkish assets. The bank on Monday raised commercial banks' reserve ratios aggressively to combat surging domestic loan growth.

It was the second time the bank has delivered such a one-two punch, but came just days after Turkey's Central Bank Governor Durmus Yilmaz had stressed to reporters that the strategy represented a net tightening of monetary policy, in an economy that grew by around 8% last year. Markets had taken those remarks as an indication the bank was not about to cut rates again, only to be proved wrong.

Already in Davos on Wednesday, Mr. Yilmaz continued to defend his policy. He acknowledged that foreign investors had sold off the Turkish lira following the bank's latest move, but stressed that the measures would have an impact in restraining domestic demand next month.

Mr. Yilmaz took a less combative stance toward media criticism that he had failed to communicate his strategy, creating an atmosphere of unpredictability.

The bank "cannot be driven by the market," Mr. Yilmaz said in Davos, during an interview with Turkish television channel CNBC-e. "We are doing something completely new so it's natural that people will ask questions... But we know what we are doing and we think we will get a result."

While Wednesday brought the government's first expression of concern over the central bank strategy, Mr. Yilmaz has repeatedly warned the government to keep its fiscal policies tight. In Davos, he warned again that maintaining fiscal discipline was "critical" to safeguarding financial stability, as a loosening could further aggravate the country's mushrooming current account deficit.

# Riksbank greets a stronger krona

By Charles Duxbury

STOCKHOLM—Swedish central bank Governor Stefan Ingves believes that the soaring krona is long overdue and won't hurt the country's competitiveness.

"We have said for 15 years that the krona will get stronger and now it actually has happened," the Riksbank chief said in an interview at his Stockholm office.

His stance contrasts sharply with Switzerland's deep concerns at the growing strength of the Swiss franc. Swiss exporters have sounded the alarm and the government is considering measures to counter the problem. The Swiss National Bank has intervened in currency markets to reverse the trend, without success.

The Swedes are less alarmed. Fueled by one of the strongest economic recoveries among major European countries, the krona in recent months has soared to reach a ten-year high against the euro. Mr. Ingves said this doesn't necessarily threaten Sweden's competitiveness.

"When it comes to the Swedish economy, the issue is by far not only the exchange rate," Mr. Ingves said. "The issue is what is going on with the rest of the world, which is global growth," he said. Mr. Ingves said Sweden had benefited from rapid economic expansion in China, among other countries. Demand for Swedish goods and services led to a "very good outcome last year and as far as we can judge continued good growth for the coming year."

**Strong krona**

Cumulative performance of the U.S. dollar and euro against Sweden's currency


Source: WSJ Market Data Group

The Riksbank forecasts Swedish gross domestic product growth of around 5.5% in 2010 and 4.4% in 2011. The European Union, meanwhile, estimated that Swedish GDP grew 4.8% in 2010, which would make it the top performer in the EU.

As Sweden seeks to steer its rebounding economy, the country has attracted attention by raising its key interest rate four times in a row, to 1.25% from a low of 0.25%. More increases are seen likely this year.

Sweden's GDP grew 6.9% in annual terms in the third quarter of 2010 as exporters like truck maker **Scania AB** reported strong numbers as orders, deliveries, revenues and profits jumped with key markets like Brazil booming.

Riksbank Deputy Governor Karolina Ekholm has said that the stronger krona, 13% higher against the euro than a year ago, will damp inflation, as she put her case for delaying interest-rate increases, a view Mr. Ingves disputes. Inflation has remained low in Sweden, but the consumer-price index jumped to 2.3% year-to-year in December, bringing prices more in line with the Riksbank's target of 2%.

"What happens with the krona will affect inflation a bit but the situation is quite different today compared to, let's say, in the early nineties," Mr. Ingves said. The effect of the exchange rate then was more pronounced, he said, adding today the krona is "just one component" in inflation.

The gravest threat to the Swedish economy comes from increased household debt, the central bank governor said. The ratio of loans to disposable income has doubled since the nineties, which is "not sustainable."

"That doesn't mean that there is a problem today but it is not good if it continues," he said.

Mr. Ingves, 57 years old, had no comment on his future, with his term as governor set to end at the close of 2011. Whether he would sign on for another six-year term was a "matter for the Riksbank's general council" he said.

Two deputy governors—Svante Oberg and Lars Nyberg—have already said that they will leave the six-member executive board at the end of 2011. The general council has said it will announce the appointment of three members later in the year.

EUROPE NEWS

# More strikes are set to sweep Greece

By Alkman Granitsas
And Nick Skrekas

ATHENS—After a year full of strikes protesting reforms and budget cuts, Greece is bracing for more unrest. The Socialist government's efforts to liberalize the country's service industries are threatening to provoke a storm of protests from groups ranging from taxi drivers to bakers.

Early next month, the Greek parliament is expected to vote on legislation that would abolish regulations on up to 150 cosseted professions. The proposed law would sweep away rules that govern everything from minimum fees to geographical restrictions and the number of permits issued each year.

The focus is mainly on a handful of sectors—such as lawyers, auditors, architects and notaries—but the scope of the plan promises to shake up the Greek economy.

It is hard to overstate the stifling level of regulation in Greece, which has suffered for decades from outdated protections that have weighed on economic growth and hamstrung any economies of scale.

Pharmacies are guaranteed a 30% profit on their sales—a huge burden for the Greek public health system and consumers. Pharmacists are also protected by fixed working hours, a restricted number of licenses based on the total population, and the right to pass on those licenses to their children.

As a result, Greece has a surfeit of pharmacies—about 10,000 in all—and pays some of the highest drug prices in Europe.

Likewise, Greece's 45,000-odd lawyers collect the highest fees in Europe thanks to set minimum fees. Each year, 1,000 attorneys join the profession and there are now more lawyers in Greece, relative to its population, than in the U.S.

Auditors, architects and engineers will see standardized minimum fees abolished and will in the future have to pitch competitively for work. The streamlining of bidding for public-works projects should help engineers without direct experience win orders for government tenders more easily.

According to economists, the sweeping reforms, which follow a similar overhaul of the trucking sector last year, could boost Greece's economy more than €20 billion (about $27 billion) over five years.


Associated Press

Pharmacists put the keys to their businesses in a box during a protest against government reforms in Thessaloniki on Wednesday.

**Opening up**

Among changes to the services sector, Greece aims to...

- Abolish the right of pharmacists to leave pharmacy licenses to their children
- Scrap minimum fees charged by lawyers, engineers and accountants
- Abolish special licenses for workers who load trucks
- Allow hypermarkets to sell gasoline and fresh bread
- Let Athens' lawyers work in the provinces, and provincial attorneys work in the capital

Source: WSJ research

Many say the measures will also help boost employment, attract new foreign investment and even put a brake on the country's chronically high inflation rate.

"After the reforms to fix public finances, this is the most important structural reform Greece is undertaking, and one that is being most closely watched by the foreign community," said Nikos Magginas, a senior economist at the National Bank of Greece.

"The reform will have strong direct gains for various sectors of the economy, but also a series of second round benefits as well," he said.

In May, Greece avoided default with the help of a €110 billion bailout from the European Union and International Monetary Fund in exchange for measures to cut its deficit and overhaul its heavily regulated economy. Since then, Greece has narrowed the government deficit from a record 15.4% of GDP in 2009 to 9.6% last year.

The government has also ushered in measures to reform the social security system, liberalize the labor market and restructure unprofitable state-owned enterprises, among other changes.

Greece must also pass legislation opening up the so-called closed professions by the end of next month, and this will be a key consideration when the EU and IMF decide whether to approve the next disbursement of their loan.

But the measures also threaten many sacred cows and brings warnings from those affected.

"The government's bill will abolish minimum fees for our services but that will certainly create chaos," warns Pantelis Roussos, a 51-year-old Athens-based engineer with 26 years of experience in the profession.

Opposition to the plan is mounting. Lawyers around the country, not including Athens, have held a 72-hour strike to protest a measure that would abolish geographic protections in their profession.

Civil engineers walked off the job last week over government plans to eliminate minimum fees, while doctors and dentists have also held their own recent strikes.

More disruptive was a three-day strike last week by Greece's pharmacists, who are facing sweeping reforms in their sector under a companion piece of legislation. A second 72-hour walkout is scheduled for this week, and more strikes are planned after that.

"The idea that our hours have to be completely liberalized is absolutely unacceptable and ignores the structure of the pharmacy sector in Greece," said Savvas Tsakiris, a 48-year-old pharmacist and sole proprietor of a pharmacy for 22 years. "Most Greek pharmacies are owned and run by a single person. So to expect us to work up to 70 hours a week is just not feasible. And we can't hire staff because the cost won't allow us to survive."

The strikes come as Greece's economy is already in intensive care. In the third quarter, GDP contracted by 4.6% from a year earlier, and 1.3% on a quarterly basis, with little signs of improvement since then. A turnaround isn't expected until the second half of the year at the earliest.

However, even with the disruption that the strikes are sure to bring, most Greeks support the reform. A poll in the Proto Thema Sunday newspaper this month showed 63% of Greeks approve of government efforts to pry open closed professions.

"Greece is the last Soviet-style economy in Europe," said Yannis Stournaras, director general at the Foundation for Economic and Industrial research, a think tank.

"These reforms will bring about a lot of resistance, but it won't last. "And as details of these closed-shop professions emerge, public support will grow," he said.

# Medvedev fires police official over bombing

By Richard Boudreaux

MOSCOW—Russian President Dmitry Medvedev fired a senior transport police commander for failure to prevent Monday's suicide bombing at the country's busiest airport. He gave officials two weeks to devise new plans to prevent such attacks against airports, trains, subways and buses.

Mr. Medvedev's action Wednesday, hours before his speech at the World Economic Forum in Davos, Switzerland, was meant to reinforce assurances to leaders of international business that Russia is a safe bet for their investment.

The bombing at Moscow's Domodedovo Airport killed 35 people, including eight foreign citizens. There has been no claim of responsibility, and investigators have named no suspects or presented a clear account of the attack in a lightly patrolled area of the airport's international arrivals hall.

Officials have said they believe the attack was the work of Islamist insurgents based in the Caucasus region of southern Russia. On Wednesday, Prime Minister Vladimir Putin said the attack "isn't related to the Chechen republic," one of several southern republics where the insurgency is active. He didn't elaborate.

The Kremlin's initial diagnosis of the lapse spawned confusion and finger-pointing. Mr. Medvedev at first criticized airport management for failing to secure the hall, prompting an unusual public response by airport officials, who cast blame on the transport police.

Mr. Medvedev eventually called the transport police to account, dismissing Maj. Gen. Andrei Alexeyev, the commanding officer in the region that includes Moscow. In addition, Russia's interior minister fired the chief of the transport-police division at Domodedovo and two subordinates.

"Those who did not work properly must be punished," Mr. Medvedev told a meeting on security matters at his residence outside Moscow.

He added that inspections at airports and on public transport must be "intrusive" and include some kind of terror alert system.

Moscow observed an official day of mourning Wednesday for the bombing victims. Major television channels suspended entertainment programming, and people lined up to donate blood to help treat the 116 wounded who remain hospitalized.

In his Davos appearance, Mr. Medvedev pushed for international cooperation in the fight against terrorism.

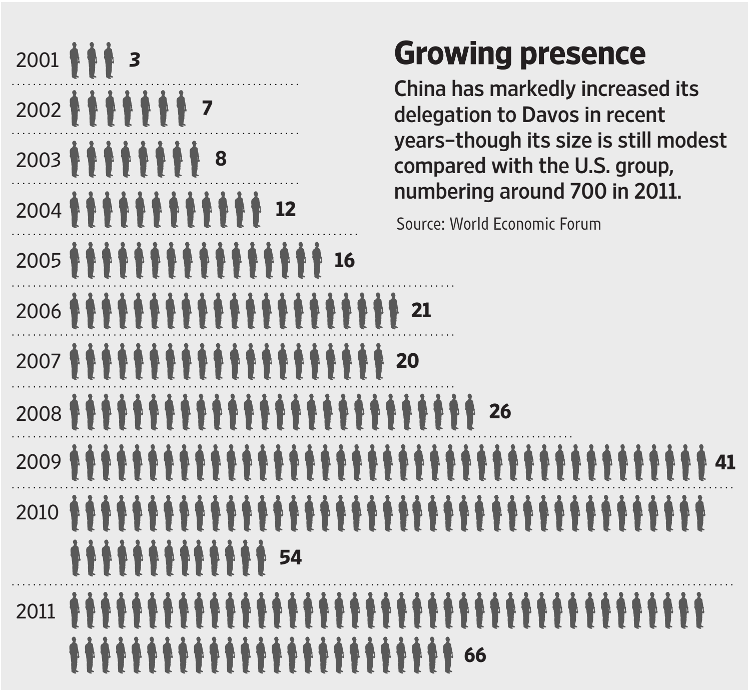
"What has happened will only strengthen our resolve to find a solution to the international problem of terror," Mr. Medvedev said. The perpetrators sought to hurt Russia and "prevent its president from being able to attend this event today, among other things."

Mr. Medvedev then changed course to list reasons why Russia is still a good place to do business, including its aspirations to join the World Trade Organization this year and a new initiative to set up a government fund that invests Kremlin cash alongside that of foreign investors, with the goal of modernizing Russia's economy.

Mr. Medvedev also touched on other issues. Asked about Tunisia, Mr. Medvedev said the recent events are a "substantial lesson for all regimes" about leaders who sit "in their armchairs" and avoid engaging with the rest of society. He championed Internet freedom, even though Russia has been criticized for the state's moves to dominate the media, especially in television.

Asked about WikiLeaks disclosures, Mr. Medvedev, an avid Twitter user, said that "at the end of the day, I believe Wikileaks will make the spirit of international relations healthier" amid increased transparency.

DAVOS: WORLD ECONOMIC FORUM


Bloomberg News

Liu Mingkang, chairman of the China Banking Regulatory Commission, left, speaks as Peter Sands, chief executive of Standard Chartered Group, listens at a session in Davos, Switzerland, on Wednesday.

# China ascendant at global gathering

BY SHEN HONG

SHANGHAI—China is sending its largest-ever delegation to the World Economic Forum at Davos, Switzerland, this week, continuing an expansion of its presence in recent years that underlines the country's growing influence on the global economy.

Leading the 66-person-strong group is China's commerce minister and its top banking regulator, along with the chairman of **Industrial & Commercial Bank of China** Ltd., the world's biggest lender by market capitalization, and the head of **China Ocean Shipping Group** Co., which runs the world's largest bulk cargo fleet.

In addition to a few regulars among state-enterprise executives and government think-tank economists, a growing number of young and rising stars from China's private sector, such as the head of an MP3 maker and the founder of a U.S.-listed solar energy firm are also attending.

The size and stature of the Chinese delegation follows President Hu Jintao's recent state visit to the U.S. and Vice Premier Li Keqiang's extensive European tour, both of which generated big export deals for the host nations' manufacturers and service providers.

As skepticism has grown on the utility of Davos in recent years—especially in the aftermath of the financial crisis—Beijing is showing strong affection for the forum, capitalizing on its relaxed atmosphere to convey its policy messages and to promote its corporate sector.

Among highlights of China's recent participation at Davos was Premier Wen Jiabao's broader 2009 European "trip of confidence," when he pledged that China would shore up its own economy and aid other ones. He then left Europe with huge Chinese orders for European goods ranging from new aircraft to telecommunications equipment.

Last year, Vice Premier Li, who is widely expected to take over from Mr. Wen in two years, used Davos to make his most high-profile international debut.

The top Chinese leadership won't be in Davos this year, but the size of the nation's delegation has risen to 66 people from 54 last year, the forum's organizers said.

The Chinese group is still dwarfed by the delegations of other countries, such as that of the U.S. with about 700 people this year, the U.K. with nearly 300 people and India with more than 100. But it is a big contrast from 2001, when Beijing sent three people.

Commerce Minister Chen Deming will be China's highest-ranking official at the forum this year, along with Liu Mingkang, chairman of the China Banking Regulatory Commission and Peng Sen, vice chairman of the National Development and Reform Commission, the country's economic planning agency.

Mr. Chen is scheduled to co-chair a plenary session with Pascal Lamy, director-general of the World Trade Organization, focused on China's impact on global trade and growth.

Apart from familiar statements on resurrecting the dormant Doha Round of trade talks and opposing trade protectionism, Mr. Chen is expected to call for the European Union to lift restrictions on high-tech exports and arms and grant China market economy status, which would give Beijing better protection against trade penalties.

As a guardian of China's labor-intensive export industry, Mr. Chen is also likely to defend China's contested exchange-rate policy, arguing it isn't a cause for global trade imbalances. He is also expected to address the protection of intellectual-property rights.

Mr. Liu, who studied in the U.K. and is fluent in English, spoke on a panel with mostly Western bankers about international financial regulatory reforms. Mr. Liu is widely regarded as favoring a cautious approach on issues such as managing systemic risks, Chinese overseas bank forays and the use of financial derivatives.

Accompanying these government officials will be senior executives of China's various corporate giants, including Jiang Jianqing, chairman of ICBC and Gao Xiqing, president of **China Investment Corp.**, the country's $300 billion sovereign-wealth fund and Wei Jiafu, president of Cosco, the container company. A group of less well-known leaders of large state-owned enterprises, such as **Tianjin Port (Group)** Co. and **Bohai Steel Group** Co. will also attend.

Apart from the state sector, a marked trend in recent years at Davos has been the growing presence of a new breed of Chinese entrepreneurs. This year features Shi Zhengrong, founder and chairman of **Suntech Power Holdings** Co., a New York-listed firm that is on the threshold of becoming the world's largest solar-panel maker. Gao Jifan, chairman and chief executive of **Trina Solar** Ltd., another U.S.-listed industry solar company, will also attend. Well-known Chinese technology firms such as **Huawei Technologies** Co. and **Lenovo Group** are sending executives to the forum.

# Gates advocates global case for vaccination

BY NOUR MALAS

ABU DHABI—Billionaire philanthropist Bill Gates will press the case at the World Economic Forum in Davos, Switzerland, this week that investing in preventing disease can aid the long-term stability of developing nations, after securing his first Middle East partnership to tackle two disease trouble spots.

Mr. Gates's Bill & Melinda Gates Foundation on Wednesday committed $50 million, alongside a similar sum from Abu Dhabi's crown prince Sheik Mohammed bin Zayed Al Nahyan, to vaccinate children in Afghanistan and Pakistan against a range of diseases.

The highly contagious polio virus remains deeply entrenched in those two countries, as well as in Nigeria and India. The Gates Foundation—with the World Health Organization, Unicef, and others—supports a global polio-eradication initiative that has managed to reduce incidence of the crippling disease by 99% world-wide in the past 20 years.

"If governments look at the numbers—the impact of this—it compares favorably to almost anything else you can do to help a country," Mr. Gates said in an interview in Abu Dhabi. Preventing disease helps stem population growth by encouraging smaller family sizes, which in turn allows governments to focus on development issues from unemployment to food security, Mr. Gates said.

"If you don't, if you let the population growth stay high—like it is in countries with very poor health—whether it's stability or education, all of it is kind of out of reach," he said.

The largest chunk of the $100 million pledged Wednesday will be focused on increasing the number of Afghan children that get vaccinated for diseases including hepatitis B, diphtheria and whooping cough. The money also will support delivery of a new vaccine for pneumococcal disease, which causes pneumonia, one of the main killers of children world-wide.

A smaller amount, $34 million, is focused on fighting polio in Pakistan and Afghanistan, neighboring nations in conflict that are stuck in a cycle of reinfection.

The new money comes at a major crossroads in the effort to eradicate polio. For more than two decades, organizations including the WHO and Rotary International have spent $9 billion trying to wipe out the disease, but it has bounced back again and again. The group last year set the end of 2012 as a new goal for getting close to eradicating the disease.

"We're trying to get the current donors to step up a bit to make sure funding doesn't hold us back, and having new donors like Abu Dhabi is a very positive thing," Mr. Gates said. On Friday, he will announce a polio-related milestone with U.K. Prime Minister David Cameron.

Mr. Gates said the new money committed Wednesday brings the global polio initiative's funding gap for the two-year period to 2012 to $700 million—with the campaign's funding needs at about $1 billion a year.

He also said he is confident the campaign could raise the rest, and optimistic on the new plan with Abu Dhabi's crown prince. Targeted vaccines, which target areas by the type of polio that is common there, are part of a new strategy that has helped the campaign bring down the number of cases in recent years, Mr. Gates said.

The money from the Abu Dhabi prince won't do much to bridge that gap but it is focused on two of the places that need it the most, and could make it easier to hit the high coverage-ratio target with a regional partner monitoring results. In Pakistan—where increased migration and last year's floods have made it difficult to reach children—the Pakistani and U.S. militaries take part in helping vaccinators reach the children in need, Mr. Gates said.

Pakistan last year experienced a surge in reported polio cases—to 140 cases in 2010 from 89 cases a year earlier. The government there this week announced a national emergency plan to eradicate polio.

Mr. Gates planned to head to the World Economic Forum's annual meeting in Davos later Wednesday, and he will stop for meetings in the African Union before traveling to New York for the release of his foundation's annual letter on Monday.

In Davos, he will argue that the targeted investments his foundation supports—getting vaccinations to the people who most need them and wiping out cases of polio—have dramatic effects that even budget-conscious governments cannot ignore.

"The case has to be made that there's real impact—whether you care about the humanitarian impact or whether you care about letting these countries be stable and self sufficient—that these are great investments," Mr. Gates said.

His 2011 annual letter will focus on polio eradication and the experience of eliminating smallpox, the only human disease ever to be eradicated.

"In the annals of public health and improving human lives, the smallpox eradication and then that increase in vaccination use—those are the most amazing things ever done," Mr. Gates said. "Having a successful polio [eradication] would really energize the whole field."

*—Robert A. Guth contributed to this article.*

DAVOS: WORLD ECONOMIC FORUM

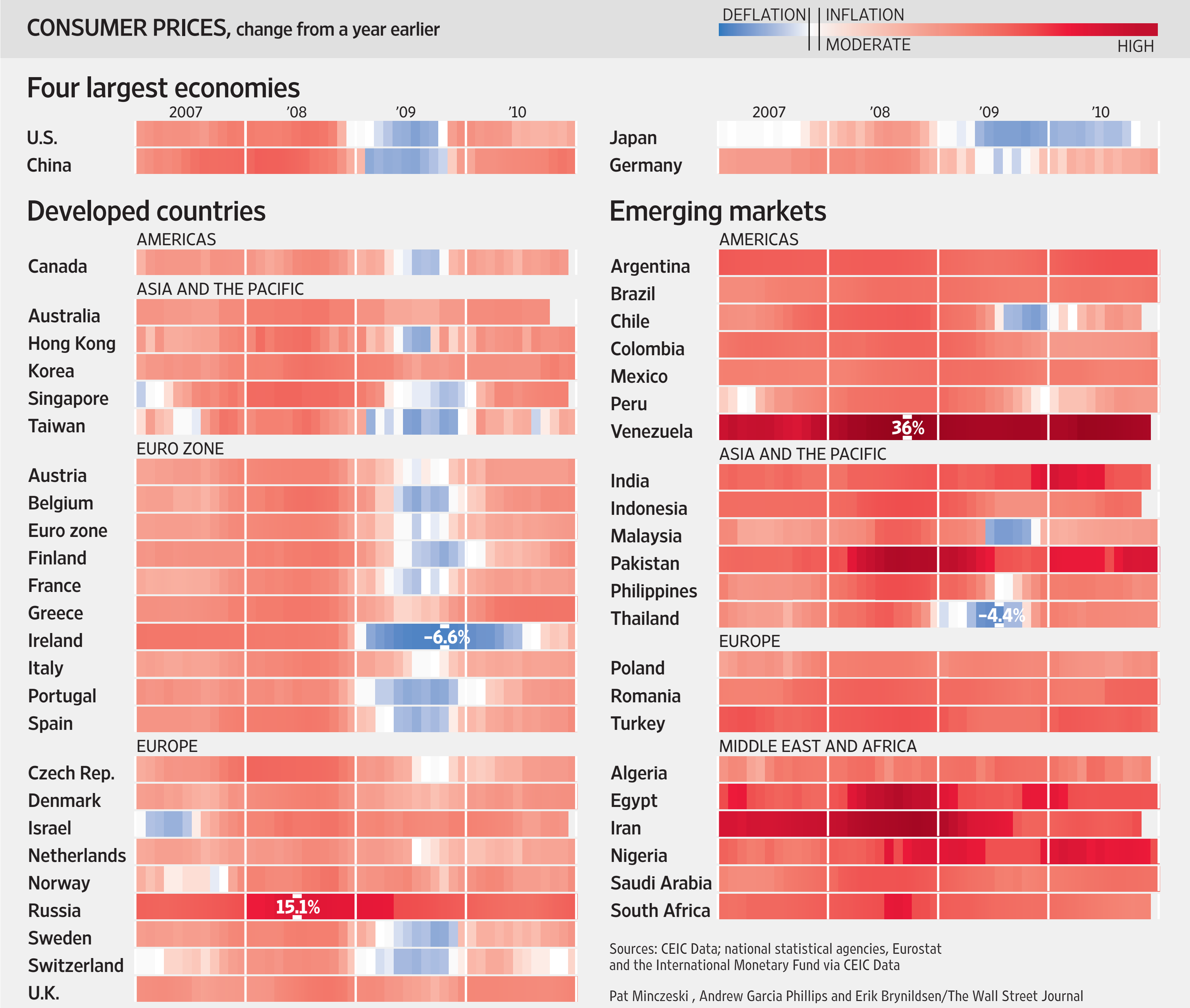
# Inflation tops policy-maker agendas

BY STEPHEN FIDLER
AND ANJALI CORDEIRO

## Feeling the heat: global inflation

Consumer-price inflation spreads unevenly. Inflation remains moderate in the U.S., which faces high unemployment and economic slack. In fast-growing China, prices are rising quickly.

In Japan's stagnant economy, deflation is an ongoing problem. Germany's economy is recovering faster than the rest of the euro zone, so its inflation is edging up faster, too.




Sources: CEIC Data; national statistical agencies, Eurostat and the International Monetary Fund via CEIC Data

Pat Minczeski , Andrew Garcia Phillips and Erik Brynildsen/The Wall Street Journal

DAVOS, Switzerland—With the risks of a double-dip recession apparently receding in most parts of the world, another economic challenge is emerging: inflation.

Rising prices for food, energy and other commodities are reducing the disposable incomes of poor people across the planet, providing a trigger for street protests in North Africa and posing a deep conundrum for policy makers world-wide.

It is one of the issues on the agenda of the World Economic Forum in Davos that wasn't around last year. Though the phenomenon hits the hardest in poor countries, where people spend most of their incomes on food and to a lesser extent energy, it is also a worry in countries such as the U.K.

New British data this week showed the economy didn't grow in the fourth quarter even as inflation has accelerated. That raises the specter of stagflation—high inflation and low growth—that last hit Britain in the 1970s, economists and bankers say.

In the euro zone, rising prices could lead the European Bank to increase interest rates, intensifying pressures on weak economies such as Greece and Ireland that use the common currency. On Wednesday, new data showed the prices of German imports rose at their fastest clip for two decades.

Simon Johnson, a professor at Massachusetts Institute of Technology and a former chief economist at the International Monetary Fund, says the only major country where commodity-price inflation isn't an important concern is the U.S., because imported food accounts for a tiny proportion of U.S. consumer spending.

And, while inflation hits the poor and those on fixed incomes, it can have benefits.

"For the U.K., it's the escape hatch," says Mr. Johnson. Inflation lessens the burden of repaying Britain's heavy government debts. Moreover, for now, interest rates on government debts remain low—10-year U.K. bonds were yielding 3.7% Wednesday, exactly the same as consumer-price inflation in 2010—suggesting that investors don't believe the authorities will let inflation rip.

In poorer countries, the disadvantages are more evident. In Tunisia, Algeria and Egypt, rises in food prices—such as a 30% increase in cooking oil in Algeria—have acted as a spark for street protests. Rising food prices heighten financial pressures on governments in the region because they are often direct buyers of commodities such as wheat, sugar and coffee, and they subsidize prices heavily, says Francis Ghilès, a senior research fellow at the CIDOB Foundation in Barcelona.

In India, the chief executives of some of the country's largest companies cited quickly rising food prices as a problem because it hurts the poorer sections of India's population and could translate into political uncertainty.

"Inflation is really our key priority...it's top of the government's priority," said Azim Premji, chairman of one of India's largest technology companies **Wipro** Ltd. He said he hopes that government support programs for the poor will help unrest from growing in the country's rural population.

"What keeps me awake [at night] is that India Inc. can price itself out of the market because our costs seem to be running higher than [they] should," says C.P. Gurnani, chief executive of technology company **Mahindra Satyam**, referring to the global technology and outsourcing market. "My highest costs are my employee costs."

Zhu Min, a Chinese economist who advises the International Monetary Fund, told one panel that higher food costs would have a significant impact in China and India. Food accounted for 47% of the basket of products that make up India's consumer-price index and 34% of China's. He said the world was experiencing a three-speed economic recovery, with advanced economies likely to grow at just over 2.5% in 2011 and the emerging economies at just under 7%, with the U.S. in between, growing at 3%.

Nouriel Roubini, a professor at New York University's Stern School of Business, said political instability deriving from higher food and energy and commodity prices, as seen in North Africa, was one factor that could hurt world growth.

However, Mr. Roubini, a noted bear at recent meetings here, said he now saw the risks between economic growth and contraction evenly balanced.

On the upside, there was a stronger economic recovery in emerging markets; the small risk of a double-dip recession had receded, except in parts of Europe; and corporate balance sheets were strong.

But on the downside, he said, public and private sectors were still trying to cut debts in the advanced economies, a threat to growth. Also undermining the positive outlook was the possibility of sovereign default in the euro zone.

"Some countries are effectively insolvent," Mr. Roubini said, noting Greece's debt was soon expected to exceed 150% of its annual output.

In the U.S., worries centered on high unemployment, a housing market where prices were again pitching downward, and the weak condition of the finances of some state and local governments.

# Hypothetical bank crisis finds risks remain

BY VIVEK AHUJA

For all the rhetoric about a new financial order and improvements made since the start of the financial crisis in 2008, many risks remain and it would take little to create a fresh crisis, consultancy **Oliver Wyman** said in a report released Wednesday at the World Economic Forum in Davos.

The report, "The Financial Crisis of 2015: An Avoidable History," looks at a hypothetical bankruptcy of a bank in 2015 and tries to piece together shortcomings in the banking system in the four years leading to the collapse.

The firm said the report uses the hypothetical scenario to stress-test the design of the current financial system, and concludes that many risks that were present before and during the financial crisis remain. The basic regulatory framework that existed before the crisis, featuring bank-debtor guarantees and minimum levels of bank liquidity and capital, has been maintained with "tweaked parameters." Shareholders, bondholders and executives still have incentives that might herd them towards excessive risk-taking, the firm adds.

"Regulators should put less effort into holding the lid down on banks and more into addressing the financial-market distortions that fuel the pressure under the lid," the report said. "And bankers should use scenario analysis to take an honest look at the risks to which their strategies expose them."

The drivers of Oliver Wyman's hypothetical bank bankruptcy include the formation of emerging-market asset bubbles and sovereign-debt restructurings in developed markets.

*—More at efinancialnews.com*

DAVOS: WORLD ECONOMIC FORUM

# *Looking to save traders from themselves*

**[ Davos Dispatches ]**

REPORTS FROM BLOGS.WSJ.COM/DAVOS

Adair Turner, the chairman of the U.K.'s Financial Services Authority, is under no illusion that regulators have permanently solved the problem of periodic financial crises—but he does have some interesting, if wonky, ideas on how to reduce their frequency. "Have we banished forever any danger of financial volatility and crisis? We haven't changed human nature," he said on the sidelines of Davos. "And the risk will be that as memories fade and good times return, there'll be new innovations, new exuberance and a new variant of 'this time it's different.'"

What's a regulator to do? Curbs on so-called proprietary trading, where banks try to profit by gambling with their own capital, have gained traction in some quarters, including with former Fed Chairman Paul Volcker and his eponymous rule. But skeptics note that banks can easily circumvent such rules by classifying prop trading under the umbrella of legitimate market-making activities, or flow trading.

Lord Turner's idea: One way to distinguish between proprietary trading and flow trading at a bank is to monitor a histogram of trading results. If a bank has a pretty consistent run of daily profits with the odd variance up or down, then it is probably flow trading. If they are more volatile, it raises a red flag that there is more proprietary risk-taking in the mix. Regulators can force the flagged bank to hold more capital.

*—David Enrich, Thorold Barker*

## The upside to austerity

Many participants in Davos are fretting about anemic Western economies and the potential for inflation elsewhere in the world. Michael Dell isn't one of them.

The **Dell** Inc. CEO said the era of austerity could actually be good for his company in some ways. Mr. Dell reckons it will prod governments, corporations and other institutions to look for ways to boost productivity, and technology is the obvious answer.

Dell, which he said derives about 80% of its profit from its commercial segment, could be a beneficiary, Mr. Dell told us after mingling with executives from Advanced Micro Devices and a Chinese mobile-phone company. "Even if there are austerity programs within governments, they buy tools," he said. "There are places where it helps."

Nor is Mr. Dell nervous about inflation in emerging markets. "I'm just not all that worried about inflation," he said. "We're creating deflation for our customers in terms of productivity."

*—David Enrich*

## Davos's toughest ticket

Davos is a place to see and be seen. But some of the real action takes place behind the scenes—in the IGWELs. Never heard of an IGWEL? Neither had we. It's Davos-ese for Informal Gathering of World Economic Leaders. They're under-the-radar pow-wows between top officials from some of the world's biggest countries. This year's IGWELs are taking place on Friday and Saturday at an undisclosed location in the sprawling Congress Center. Topics on the agenda: not surprisingly, global financial imbalances and the international monetary system.

*—David Enrich*

# Unanimous Fed stays course on bonds

By Luca Di Leo
And Jeffrey Sparshott

Federal Reserve officials were united Wednesday in deciding to continue buying government bonds to boost the recovery, even as they acknowledged that the U.S. economy has improved.

At their first policy-setting meeting of 2011, central bank officials voted unanimously to push ahead with the controversial $600 billion purchase plan, though three of the four new Federal Open Market Committee members have criticized the move.

The full backing won by Fed Chairman Ben Bernanke could improve the effectiveness of the program—which aims to lift growth by keeping borrowing rates low and boosting stock markets—by indicating to financial markets that it is likely to be completed. It also strengthens Mr. Bernanke's hand as he prepares to update Congress on the central bank's actions to improve the economy.

Fed officials said Wednesday that while global food and raw-materials prices have been rising, their preferred gauge for where prices are heading—which strips out volatile energy and food items—remains within the bank's comfort zone.

"Although commodity prices have risen, longer-term inflation expectations have remained stable, and measures of underlying inflation have been trending downward," the Fed said.

Fed officials noted some progress in consumer spending. In the statement released following their two-day meeting, the Fed said spending "picked up late last year." But they still see the economy constrained by high unemployment, slow income growth and tight credit. Employers "remain reluctant to add to payrolls" and the housing sector "continues to be depressed."

Getty Images

The FOMC's unanimous approval of continued bond buying strengthens Chairman Ben Bernanke's hand before Congress.

Taken together, the improvements weren't strong enough to make the Fed change its course, and officials reiterated they expect short-term interest rates to stay close to zero for an extended period.

Faced with a slowing recovery in the middle of last year and short-term rates already close to zero, the Fed resumed buying bonds in November 2010 in an effort to keep long-term rates low. Unlike the first round of $1.7 trillion purchases to fight the financial crisis, however, the central bank suggested it was ready to scale the program back if the economy gained steam.

That no longer appears likely. With unemployment expected to stay high and underlying inflation low for some time, the FOMC said it would "continue expanding its holdings of securities as announced in November." The Fed already has bought about $200 billion in Treasuries and is scheduled to complete the $600 billion in purchases in June.

The Fed's easy-money policy was opposed by Kansas City Fed President Thomas Hoenig for all of 2010. Three of the four regional Fed presidents who this year got a vote on the FOMC—currently 11 voting members because of a vacancy on the Fed board in Washington—have spoken out against the bond purchases: Richard Fisher of Dallas, Charles Plosser of Philadelphia and Narayana Kocherlakota of Minneapolis.

But nobody was prepared to formally oppose the policy Wednesday. Messrs. Fisher and Plosser worry the policy could make it harder for the Fed to control inflation, while Mr. Kocherlakota has questioned its ability to cut unemployment. At least two officials are likely to dissent later this year if inflation accelerates. Messrs. Fisher and Plosser, who tend to worry more about the risks of high inflation than high unemployment, both opposed the Fed's aggressive rate cuts in 2008. The opposition could complicate Mr. Bernanke's efforts if he plans to extend the program beyond June.

For now, however, the Fed chairman gets a needed boost before his semiannual monetary-policy report to Congress, slated for March 3. Senior Republicans have been among the sharpest critics of the bond purchases, saying they could bring runaway inflation and hurt the dollar.

The last time the Fed voted unanimously was in December 2009, before Mr. Hoenig began to dissent at each meeting last year.

At the latest meeting, officials likely also upgraded their economic projections slightly, although details of their forecasts on growth, inflation and unemployment will only be released with the minutes Feb. 16.

Helped by the recent tax-cut package, the U.S. economy is widely expected to firm this year. The payroll-tax reduction should help keep consumer spending up, following the solid retail-sales gains during the recent holiday shopping season.

Mr. Bernanke recently said he expects gross domestic product, the broadest measure of growth, to rise between 3% and 4% this year, after increasing just under 3% in 2010. By comparison, the latest FOMC November forecasts had put growth between 3% and 3.6% this year. In November, Fed officials also predicted the jobless rate would be still close to 8% at the end of 2012, while inflation was seen well within the Fed's informal target of just below 2%.

# *Bigger deficit is seen*

*Continued from first page*

newed in 2011 at higher rates. The agreement also created a one-year payroll-tax holiday for most working Americans. It extended jobless benefits for long-term unemployed Americans through the current year.

The CBO's updated forecast came the morning after President Barack Obama urged Congress in his annual State of the Union Address to rein in federal spending. The president also called for further investments in education, transportation infrastructure and renewable energy.

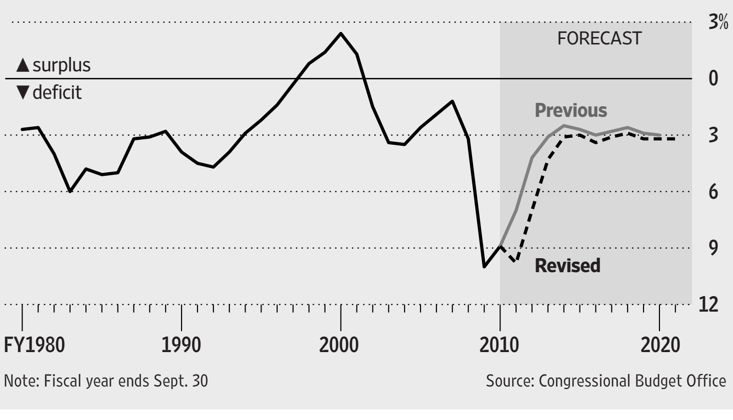
House Republican leaders were quick to jump on the CBO figures to make their argument that they were further evidence of what they characterized as the Obama administration's failed economic policies. "They were exceedingly disappointing," said Rep. Jeb Hensarling (R., Texas), a senior member of the budget committee.

Both Democrats and Republicans have acknowledged the tax deal would add to the budget deficit over the short term, but they didn't want a tax increase to jeopardize the economic recovery.

"As disturbing as those near-term deficits are, the long-term outlook is even worse," said Sen. Kent Conrad (D., N.D.), the chairman of the Senate Budget Committee and a renowned budget hawk. "It is the deteriorating long-term outlook that is the biggest threat to the country's economic security."

**Deeper hole**

**U.S. federal surplus/deficit as a percentage of gross domestic product**




Note: Fiscal year ends Sept. 30

Source: Congressional Budget Office

# Cuts start at Justice agency

By Devlin Barrett

The U.S. Justice Department, preparing for a host of proposed cuts from the White House, has begun its own reductions in the hopes of softening the blow.

The department—which saw years of rapid growth after the 2001 terror attacks—is just one of the federal agencies facing significant cutbacks. In recent weeks, Justice Department officials have been negotiating with the White House on details of a proposed budget, even as they brace for possibly tougher reductions from Congress.

According to internal documents reviewed by The Wall Street Journal, the White House Office of Management and Budget has proposed a number of cost-cutting measures, including:

—Increasing the amount of time deducted from prison sentences for good behavior, which they estimated would save money by immediately qualifying some 4,000 federal convicts for release, and another 4,000 over the next 10 years.

—Eliminating the FBI's National Gang Intelligence Center, for a savings of $8 million.

—Sharing less of the proceeds of property confiscated from criminals with state and local authorities, and eliminating other funding to local police departments for some operations. The change would recoup and save $120 million, according to the White House documents.

A White House spokesman declined to comment before the president's budget proposal is formally unveiled next month.

Some parts of the department are already making cuts, and others are contemplating ending cherished programs.

The U.S. Marshals Service has quietly shelved the Fugitive Safe Surrender Program, which has cleared the books on thousands of low-level criminal cases since it began six years ago. Under the program, law-enforcement officials set up temporary shop in a church or a public setting, urging fugitives to turn themselves in to resolve old warrants and often drawing hundreds in a single day.

U.S. Marshals spokesman Jeff Carter said officials there decided that although the program's goals "were laudable, the agency could not sustain this unfunded initiative."

Supporters of the program say it is an extremely cost-effective way to resolve piles of old cases. But the agency determined that it could not justify the program as part of its core mission, which is capturing violent fugitives.

Last week, Attorney General Eric Holder announced a hiring freeze and reductions in non-essential, non-personnel spending.

Other parts of the department are also weighing reductions. At the Bureau of Alcohol, Tobacco, Firearms and Explosives, the White House had proposed, in a document drafted just before Christmas, a spending cut of 3.5% from what the agency is likely to spend this year—and a 12.7% cut from what the agency had said it needed.

Officials at the bureau spent weeks deliberating whether to scale back Operation Gunrunner, part of the Obama administration's effort to attack Mexican drug cartels by cracking down on illegal gunrunning.

Privately, law enforcement officials say ATF expects to preserve Gunrunner and face a less punishing overall cut in the president's final budget proposal expected next month, in part because of the recent shooting of Rep. Gabrielle Giffords (D., Ariz.) in Tucson.

An ATF spokesman declined to discuss any potential budget decisions.

Mayors Against Illegal Guns, an advocacy group led by New York City Mayor Michael Bloomberg, has argued ATF is already underfunded, even before any new cuts might be imposed.

"This is an agency with important responsibilities, and 500 mayors have called on the administration to give the agency the resources it needs to do its job," said Arkadi Gerney, a special adviser to Mr. Bloomberg.

*—Thomas Catan contributed to this article.*