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Continental and United reach deal to create giant

NEW YORK

The merger, if approved, would displace Delta as the world's largest airline

BY JAD MOUAWAD AND MICHAEL J. DE LA MERCED

United Airlines and Continental Airlines on Monday announced a $3 billion merger that would create the world's biggest airline. The deal, all in stock, would form a coast-to-coast American behemoth with a leading presence in the top domestic markets, including New York, Chicago and Los Angeles, along with an extended network to Asia, Latin America and Europe.

The agreement, reached after three weeks of discussions, would give the airlines the muscle to fend off low-cost rivals at home and to take on foreign carriers abroad. United is buying Continental, and the combined company would take the United name and be based in Chicago. It would, however, keep the Continental logo, livery and colors and maintain a large presence in Houston, where Continental is based. Jeffery A. Smisek, Continental's chief executive, would run the company.

If the merger is completed, the airline would replace Delta Air Lines as the top carrier.

But the deal has some major hurdles to clear. The airlines must win approval from the U.S. Justice Department's antitrust division, a challenge given the renewed regulatory zeal in Washington. The merger also needs the backing of employee unions, whose opposition to mergers in the past has undone many of the proposed savings.

The combination would have 10 domestic hubs and serve more than 144 million passengers in 59 countries. Mr. Smisek said he did not anticipate antitrust problems since the companies have few overlapping domestic routes and do not compete internationally. Through the Star Alliance, United and Continental already cooperate on foreign routes and have already obtained antitrust immunity on trans-Atlantic flights.

"From an antitrust perspective, I don't think there is any other airline merger with less concerns," Mr. Smisek said in an interview. "We compete globally, with global competitors. This allows us to operate more efficiently."

On a new Web site, the airlines said the merger would have "minimal" effects on its front-line employees, with reductions in staff mainly from "retirements, attrition and voluntary programs."

Unions representing Continental and United pilots said Monday that they expected a "fair and equitable" seniority

"You will have less choices, fewer routes, higher prices."

integration between the two groups and threatened to oppose the transaction if a new collective-bargaining agreement was not reached.

Unlike the merger of Delta and Northwest Airlines, where a new pilots' contract was agreed to before the merger, the speed of the talks between United and Continental did not allow for negotiations on that front, said United's chairman, Glenn F. Tilton.

The boards of both companies met Sunday to approve the deal. UAL, the parent of United, would issue 1.05 shares for each Continental share, valuing the acquisition at $3.17 billion, based on Friday's closing price. The merger is expected to be completed before year-end.

For consumers, the merger could eventually result in higher prices. Though the new company does not intend to raise fares, according to people briefed on the matter, a rationale for airline mergers is to cut capacity. That reduces the number of seats in the industry and allows airlines to increase fares.

In addition, United and Continental would no longer be competing against each other on some routes, allowing them to save money but offering travelers fewer options. "Airlines are struggling to find a business model that makes sense," said Scott Sonenshein, an assistant professor at the Jones Graduate School of Business, part of Rice University, in Houston. "Consolidation gives them more leverage. As a consumer, you will have less choices, fewer routes, higher prices and more fees."

Combined, United and Continental have 21 percent of U.S. domestic capacity, in terms of so-called available seat miles, or one seat flown one mile. Delta has a market share of 20 percent. Globally, the merged companies would have a 7 percent market share.

United shareholders would own 55 percent of the new company, with Continental shareholders owning the rest. Management would be roughly split between the sides. The entity expects annual cost savings of $1 billion to $1.2 billion, and would still fly to 370 cities in 59 countries.

Bettina Wassener contributed reporting from Hong Kong.

TOBIAS SCHWARZ/REUTERS

Foreign Minister Guido Westerwelle and Chancellor Angela Merkel giving a news conference after a cabinet meeting Monday in Berlin. She said cabinet approval of aid for Greece showed that Germany was acting to stabilize the euro.

The clash of (European) civilizations resurfaces

PARIS

BY KATRIN BENNHOLD

A few weeks after Lehman Brothers went bankrupt and the world plunged into financial crisis, Chancellor Angela Merkel of Germany had this advice for reckless bankers, indebted consumers and profligate governments: Be more like a German housewife.

Addressing fellow Christian Democrats in the southwest German region of Swabia, hub of the Protestant work ethic and Germany's famed Mittelstand, Mrs. Merkel said the financial crisis could have been avoided. "One should simply have asked a Swabian housewife," she noted on Dec. 1, 2008. "She would have told us her worldly wisdom: in the long run, you can't live beyond your means."

Now, as Europe scrambles to avoid its own Lehman experience, saving Greece and thus the euro, the episode says much about the Germans, and their leader.

Led by France, Germany's neighbors have been pressing for months for the country, which has the Continent's biggest economy, to throw its financial weight behind a bailout package and a new system of economic governance for the euro zone. In the process, a reluctant Berlin has been called irresponsible, selfish, even un-European.

But if France wants Germany to be more European, Germany wants Europe to be more Swabian. And once again, to get Europe to a late compromise, it has taken a deal between a German — Mrs. Merkel — and a Frenchman — Dominique Strauss-Kahn of the International Monetary Fund — who met in Berlin last week to pull Greece, and the euro zone, back from the brink.

The Greek saga has brought back to the boil the long-simmering culture clash between the European Union's traditional drivers: federal Germany with its Prussian attachment to rules and an instinctive frugality rooted in past economic traumas, and republican France with a tradition of state intervention and a more Mediterranean attitude to public debt.

Paris and Berlin have had many disagreements post-1945, but few are as deep-rooted as those on economic governance, said John Kornblum, a former U.S. ambassador to Germany.

"This comes from the gut, it's emotional," said Mr. Kornblum, who as assistant secretary of state for Europe in the 1990s watched successive French and German leaders spar over how to govern the future single currency.

If there is no political structure in place to safeguard the euro — a vacuum exposed in the current debt crisis — it is because Germany and France could never agree on one, he said. "There are profound philosophical differences between the two sides," he said.

These differences are in many ways personified by Mrs. Merkel, daughter of a Lutheran pastor, and two flamboyant Frenchmen: President Nicolas Sarkozy, a conservative, and Mr. Strauss-Kahn, a Socialist.

Mr. Sarkozy and Mr. Strauss-Kahn are rivals and may even run against each other in the 2012 presidential election. But they share a belief in state intervention that unites most of the French political elite.

Mr. Sarkozy, a Gaullist whose taste for expensive brands and millionaire friends has not gone unnoticed across the Rhine, first roused German suspicions as finance minister in 2004 when he prevented a takeover by Siemens of Alstom, the French maker of trains. As president, he allowed the budget deficit to rise above the 3 percent euro-zone limit even before

The Greek saga has revived French-German differences.

the economic crisis erupted, and he repeatedly criticized the European Central Bank's interest rate policy.

Mr. Strauss-Kahn, a native of Alsace who speaks German, has been dubbed "Mr. Euro" in France and credited with steering his country into the euro zone as finance minister in 1997. In Germany, he is also remembered for serving under then-President Jacques Chirac, a staunch advocate of a political counterweight to the E.C.B.

So when the two men independently revived calls for an "economic government" of the 16 countries that share the euro, resistance in Germany was instinctive.

"It smacks of yet another attempt of compromising the independence of the E.C.B. and on top of it institutionalizing German subsidies not just to Greece but to all of southern Europe," said one senior German diplomat, who declined to be identified because of the sensitivity of the situation.

"Who else is going to pay? The French?" he asked, noting that the French budget deficit has widened to 7.5 percent of gross domestic product, more than twice the German level.

In Germany, where many lost their savings twice in the 20th century — once to hyperinflation in 1923 and again to currency reform after World War II — central bank independence and budgetary discipline have become part of the national narrative.

Fear of inflation and broad-based aversion to debt also help to explain a striking divergence in the perception of Germany's wealth at home and abroad. At 3.3 percent of G.D.P., Germany's budget deficit is low by crisis standards and frequently cited as a justification to appeal to Berlin for solidarity with poorer countries. But Germans, who have absorbed East Germany and face a decline in their population, do not feel rich.

"Germans fear going bankrupt themselves," said Mr. Kornblum, now a consultant in Berlin.

Jean-Pierre Jouyet, a French former minister of European affairs who now leads the French stock market regulator, noted: "The fundamental difference between France and Germany is that, for the French, budgetary, financial and currency stability is a means to an end. For the Germans it is an end in itself."

"The French have a culture of accommodation. There are rules but we accommodate them," he added. "For Germans, rules are rules."

Mrs. Merkel, a physicist raised in communist East Germany, has a hard-working, parsimonious lifestyle, and an analytical, somewhat bland personality that in many ways reflect the national value system, said Gerd Langguth, author of a 2005 biography of the chancellor.

While Mr. Sarkozy resides in the majestic Élysée Palace and has an army of staff members, Mrs. Merkel still lives in the central Berlin apartment she occupied before her election in 2005 and has been spotted doing her own shopping.

There are limits to national stereotyp ing. Mrs. Merkel's more outgoing prede cessor, Gerhard Schröder, made con mon cause with the French in breakin the euro zone's budgetary limit. And r German could have defended the lega of the Bundesbank more vigorously th the president of the E.C.B., Jean-Clau Trichet, nicknamed by some in Paris "that Frenchman in Frankfurt."

But understanding the radically d ferent contexts in which German ar French positions are honed is crucial a Europe's two foremost powers grapp with the crisis, said Jean Pisani-Ferr director of Bruegel, a research institut based in Brussels.

"Ultimately this is about whether Ger many is ready to lead," Mr. Pisani-Ferry said. "And leading means compromising, rather than only insisting on red lines."

Hungary's new leaders warn of rising deficit

BERLIN

Conservative party plans to cut taxes and spend on consumer stimulus

BY JUDY DEMPSEY

Hungary's budget deficit could grow by about a third this year despite the new government's determination to "stick to a tight fiscal policy," the country's economy minister said Monday after being named to the post.

Gyorgy Matolcsy, who is returning to a job he held from 2000 to 2002, blamed weak domestic demand and reduced tax revenue for the projected shortfall.

He said the program of the new government, led by the conservative Fidesz party, would include cutting taxes, introducing a stimulus package to increase consumer spending, and fighting corruption.

But speaking a day after the International Monetary Fund and the European Union settled with Greece on a €110 billion, or $145 billion, aid package, Mr. Matolcsy said the government had no choice but to bring Hungary's deficit under control.

"From the aspect of public debt, Hungary is one of the world's 10 most vulnerable countries," he said during a news conference in Budapest.

"There is a new wave of thinking in the world which says that countries in a situation like Hungary must focus on cutting state debt and start economic growth," he added.

The budget deficit in Hungary last year was 4 percent of its gross domestic product. It had been expected to fall to 3.8 percent this year, according to the Economy Ministry. It rose beyond 9 percent in 2006 under the former Socialist government.

But Mr. Matolcsy said the deficit goals the new government inherited from the former Socialists might not be met this year because of the weak economy. He projected that the figure for 2010 could reach "between 4.5 percent and 6.5 percent" of G.D.P., adding that "global financial markets certainly would not tolerate" anything higher.

"We must also say clearly that from whatever deficit level we start this year, in the next three or four years we must reduce it," he said. "So we must stick to a tight fiscal policy."

Hungary was among the East European countries hit hardest by the global financial crisis, along with Latvia and Ukraine.

In 2008, the previous Socialist government agreed to reduce the deficit and introduce other legislative changes in exchange for €20 billion in loans from the I.M.F. and the Union to prevent it from defaulting. Among other things, it increased the retirement age, reduced the public-sector work force and raised taxes.

These measures were highly unpopular — one of the reasons why the Socialists were routed in parliamentary elections last month.

Viktor Orban, the prime minister-designate, presented no detailed economic program during the election campaign. "This creates unlimited scope for the new government to do anything without being confronted with pre-election promises," said Sandor Richter at the Vienna Institute for International Economic Studies.

Mr. Orban last week said the budget deficit would overshoot the 3.8 percent target, adding that he would seek a new accord with the I.M.F. when the current one expires in October.

But the I.M.F wants further measures, including tougher regulation of the financial and banking sector and tackling the unprofitable public transport system.

"We will be able to come to an agreement with the I.M.F. about the contents of the package that will take effect already this year but we will not accept diktats," Mr. Orban said at a news conference last week.

Striking a more conciliatory tone, Mr. Matolcsy said Monday that "we must by all means come to agreement with the I.M.F and the E.U and we must inform them continuously and we must cooperate continuously as they are among our most important financiers."

David Nemeth, a macroeconomist at ING Financial Markets in Budapest, said, "The new government will want to find ways to increase consumer demand but also ways to increase the country's competitiveness."

He said that much depended on when Hungary wanted to join the euro zone. Mr. Matolcsy said Hungary has to be ready to lay out its timetable by next year.

LASZLO BALOGH/REUTERS

Hungary's prime minister-designate, Viktor Orban, front, introducing his cabinet Monday.

Germany clears bailout for Greece

BERLIN

BY JUDY DEMPSEY AND JACK EWING

Some of the uncertainty lingering around the financial rescue for Greece cleared Monday, as the German government approved its share of a huge bailout, and the European Central Bank said it would accept Greek bonds as collateral for loans, regardless of any future downgrades.

Chancellor Angela Merkel said her cabinet had approved up to €22.4 billion, or $30 billion, in loans for Greece over three years, clearing the way for parliamentary approval. The German finance minister, Wolfgang Schäuble, said the bill could be passed in Germany, and al the other euro-zone countries, by the end of the week.

"The cabinet decision is not jus about helping Greece," Mrs. Merke said in Berlin. "It is about underpinnin the stability of the euro."

The German cabinet meeting can just hours after the E.C.B. ended unce tainty about how it would deal with ar further downgrades of Greek debt.

The moves took some of the pressu off interest rates on Greek debt on Mo day, while the euro fell below $1.32 fo the second time in five days. The Inter national Monetary Fund and othe European Union countries approved o Sunday a €110 billion rescue plan fo Greece.

BAILOUT, PAGE 19