SUZY MENKES
THE CARNIVAL AT DIOR
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TYLER HICKS/THE NEW YORK TIMES
bels in the territory that will remain its own.

mbing

dan trudges up a hillside about 300 meters, or 1,000 feet, high, lugging pots, water jugs, mats and blankets, the children huffing behind.

She nestles her cooking fire in a crack in the mountain wall, to conceal the smoke. The young mothers around her dangle their legs over ledges as they nurse. Older children play a game similar to jacks, using pebbles on the precarious heights. Old men just sit and stare. At dusk, which usually signals the end of the sorties, most descend. Very few young men are with them.

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ms, this one Strauss-Kahn

Mr. Strauss-Kahn's lawyers responded on Monday evening, saying that he had asked them to file a counter-complaint of slander against Ms. Banon. The lawyers, Henri Leclerc et Frédérique Baulieu, said in a statement that the facts she evokes are "imaginary."

Mr. Koubbi has said numerous times in the past two months that Ms. Banon would bring charges against Mr. Strauss-Kahn, but that he did not want her [illegible] to become mixed up with the one in New York.

The chance that Mr. Strauss-Kahn might have the New York charges against him dropped caused a flurry in France, as some Socialists discussed the

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New setback in planning for bailout of Greece

FRANKFURT

S.&P. leaves Europe little room to maneuver to avoid a default

BY JACK EWING
AND LANDON THOMAS, JR.

As Europe turns from its latest short-term fix for Greece to seeking a longer-term bailout for the country, the ratings agency Standard & Poor's signaled Monday how difficult, if not impossible, it will be to offload some of the cost of rescuing Greece onto banks and other creditors without also provoking a default that could shock the global economy.

Representatives of European governments and banks, continuing talks that have been under way for several weeks, expressed optimism that they could find ways that bondholders could voluntarily contribute to reducing Greece's debt.

But S.&P., responding to a French proposal, seemed to leave little room for maneuver. The proposal would amount to a default, S.&P. said, because creditors would have to wait longer to get repaid and the value of Greek bonds would effectively be reduced.

"Ratings agencies are saying, 'We don't think it's voluntary. It's just a way to hide a default.' Which it is," said Daniel Gros, director of the Center for European Policy Studies in Brussels.

European leaders are trapped between domestic political demands for banks to share the cost of a Greek bailout, and the dire consequences of a default. These would include collapse of Greek banks, probably followed by collapse of the Greek economy and Greece's exit from the euro zone.

A meltdown in Greece could quickly spread to European banks, particularly in France and Germany, which own government bonds or have lent money to Greek individuals and businesses. Ratings agencies have already warned that French banks are particularly vulnerable to Greek debt.

As a result, officials predicted, European governments may have little choice but to abandon or modify the voluntary plan and fill the gap with more money from taxpayer coffers.

A senior figure in the Greek finance ministry, who spoke on condition of anonymity because he was not authorized to speak publicly, said Monday that it was folly to think that the ratings agencies would view a debt swap as purely voluntary and not representing a selective default.

"Now the official sector will need to find another €30 billion," this person said, referring to the amount European political leaders hoped to get from the private sector, about $[illegible] billion. That sum was never realistic in the first place, he said.

But he predicted that leaders would not turn their backs on Greece. "Europe has too much riding on this," the official said. "Greece has done 80 percent of what it is supposed to have done. If Europe were to let Greece go that would be the end of euro zone solidarity."

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Fresh setback for European attempts to fashion long-term Greek rescue

EUROPE, FROM PAGE 1

Europe is seeking to avoid a default at all cost because it could also lead to payment of credit-default swaps, a form of debt insurance typically sold by investment banks, with unpredictable results. There is little public information on which financial institutions have sold credit-default swaps and might have to absorb losses if Greece defaulted.

The shock to the global economy might compare to the collapse of Lehman Brothers in 2008, the European Central Bank has warned.

Mr. Gros said that calls for investors to voluntarily roll over maturing Greek debt could even backfire, by invoking memories of similar stopgap measures that preceded Argentina's disorderly default in 2001.

Despite the discouraging assessment Monday from Standard & Poor's, European governments continued work on a contingency plan that they predicted would ultimately satisfy the ratings agencies and prevent Greece's problems from provoking a wider crisis.

There was somewhat less urgency to the talks after euro zone finance ministers agreed over the weekend to provide Athens with financing of €8.7 billion from the €110 billion bailout agreed to last year, to help the Greek government function through the summer. The new aid eliminates the prospect of a near-term default.

But the finance ministers put off the question of how to provide a second bailout, expected to total as much as €90 billion, to keep the country operating through 2014, when it is hoped that Greece will be able to return to the credit markets.

Negotiators are trying to put together a plan that would offer private investors good enough terms to encourage them to take part voluntarily while, at the same time, convincing angry voters in nations like Germany and the Netherlands that financial institutions are sacrificing, too.

The decision Monday by Standard and Poor's reveals just how difficult that will be. S.& P. also said Monday that it was cutting its long-term rating on Greece three notches deeper into "junk" territory, to CCC from B.

One serious problem is how to prevent a collapse of Greek banks if the country is declared to be in default.

Greek banks, cut off from international money markets, use their holdings of domestic government debt as collateral for low-cost loans from the European Central Bank. If Greece defaulted, the E.C.B. could probably no longer accept the debt as collateral.

Recognizing those difficulties, European officials are working on a contingency plan under which their second bailout is judged a selective default, according to one official briefed on the negotiation, who would not agree to be quoted by name because of the sensitivity of the issue.

In that case, the European governments, rather than the E.C.B., would support the Greek banking sector to prevent a run on financial institutions that could spread to other countries.

In theory the E.C.B. could be persuaded to accept paper deemed to be in selective default, a temporary, less serious, form of default.

The E.C.B., which itself holds billions of euros' worth of Greek debt, has said it could only accept the participation of bondholders in any restructuring if it were "entirely voluntary."

The central bank — which has been helping Greece by buying its debt on the secondary market — "doesn't want to jeopardize publicly its balance sheet anymore," said Gilles Moëc, an economist in London for Deutsche Bank.

"The E.C.B. would be able to accept them if the final structure was relatively healthy," Mr. Moëc said. But he added, "One thing the E.C.B. doesn't want is any infringement of its right to decide on the collateral that it accepts."

YIORGOS KARAHALIS/REUTERS

Evangelos Venizelos, the Greek finance minister, is pressing privatization action.

The S.& P. decision is also expected to have an effect on Greece's aggressive privatization goals. Greece must produce over €6 billion in privatization receipts by the end of this year according to a provisional agreement with Europe and the International Monetary Fund, part of a €50 billion goal by 2014 that makes up a crucial financing component of the planned rescue package.

But the controversy over how much the banks must contribute has created a terrible environment for asset sales, said bankers based in Athens.

"It will be very tough to meet any of these targets by December," said a senior banker in Athens who is directly involved in the privatization process but who was not authorized to speak publicly.

On Monday, according to bankers who were briefed on the talks, the Greek finance minister, Evangelos Venizelos, met with privatization officials and urged them to move ahead quickly with the process of selling stakes and appointing banks to help sell the assets.

Next week, the government is expected to achieve its first privatization payoff — about €400 million for selling its 10 percent stake in its telecommunications company to Deutsche Telekom.

In fact, after a long delay, there has been a rapid progress on the administrative and legal front in setting up a new fund to oversee the asset sales.

Some institutions have drawn interest, like the airport — in which the target is €700 million to €1 billion by the end of the year — but other assets, like the union-controlled power company, will be harder to sell.

Other assets include €1.5 billion to be raised from selling a 34 percent stake in the country's sports betting entity, and — more unlikely given the sickly state of Greek banks — €275 million from a sale of a stake in Hellenic Postbank.

Despite the obstacles to private-sector participation in a Greek solution, officials say they must continue looking for a plan because of the demands of Germany and the Netherlands.

And following elections earlier this year during which a populist party made gains, Finland is demanding collateral from Greece in exchange for loans as part of any new bailout.

Under the French plan rejected by S.& P., private investors would reinvest at least 70 percent of the proceeds of bonds maturing before the end of 2014 into new 30-year Greek debt.

But France has also suggested a second option. Under that plan at least 90 percent of Greece's bonds maturing before 2014 would be invested in new five-year bonds. These would carry a 5.5 percent interest rate and would be listed on a European market with restricted trading to protect them from speculative attack.

Landon Thomas Jr. reported from Athens. Reporting was contributed by Stephen Castle in Brussels, and David Jolly and Liz Alderman in Paris.