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WIDE RELIEF AS DEBT PLAN COMES AT LAST

BERLIN

Merkel takes center stage in 11th-hour bargaining over sweeping agreement

BY NICHOLAS KULISH AND STEVEN ERLANGER

Disparaged at home and abroad for her stubborn brinksmanship over the euro, Chancellor Angela Merkel of Germany once again on Friday found herself taking credit not just for preserving the currency, but for beginning to remake Europe in Germany's austere image.

The recalcitrant chancellor led Europe teetering to what the Greek prime minister, George A. Papandreou, called "the edge of the abyss," as panic grew in the financial markets over the ability of European leaders to find a consensus over Greece's insolvency. In yet another emergency summit meeting on Thursday, preceded by yet another emergency French-German bargaining session, they managed to find a compromise in the form of a €109 billion, or $156.6 billion, bailout for Greece and significant relief for reeling Ireland and Portugal.

President Barack Obama called from Washington. The head of the European Central Bank flew first to Berlin and then to Brussels, as did the president of France. The 20 members of the Greek delegation arrived with significant apprehension and until Thursday evening were not sure they would get the bailout they needed.

These meetings are never without drama, and Mr. Papandreou provided one, angrily rejecting a draft proposal

FERDINAND OSTROP/AP

Chancellor Angela Merkel of Germany managed to get Europe to agree to reforms.

that Greece put up buildings and land as collateral for new European loans. Meanwhile, at critical meetings, lots of food was consumed, everything from duck and potato purée to Gummy Bears.

This is not the first time European leaders have had to come together in the midst of political and market panic to deal with the problems of Greece, euro-zone debt and internal lack of com-

MERKEL, PAGE 13

BRUSSELS

Cautious approval greets Greek rescue in many capitals and markets

BY STEPHEN CASTLE AND NIKI KITSANTONIS

Financial markets, at least one ratings agency and leaders in capitals across Europe on Friday gave cautious to enthusiastic votes of confidence to a sweeping deal struck Thursday that provided Greece with a second bailout. The generally positive reception came despite lingering worries that Europe's leaders had found only an interim solution to the debt crisis that has imperiled their single currency.

Even as some of the initial reactions to the deal were positive, investors were trying to understand its details and long-term implications: most importantly, whether the €109 billion, or $156.6 billion, deal — despite its sweep and unexpected boldness — was a lasting solution for the most indebted countries in the euro zone.

Under the deal's final details, for instance, Greece's staggering debt will only be reduced by about 24 percent, though it totals more than 100 percent of the country's gross domestic product. Analysts said it was also clear that in the end, the contribution from private-sector banks and insurance companies would be relatively modest.

In the immediate term, financial markets gave the deal a positive reception, with bank stocks, in particular, benefiting. Greek, Irish and Spanish bonds rallied as well.

David Riley, head of sovereign ratings for Fitch, actually struck an upbeat tone and said the commitments made by euro area leaders "represent an important and positive step toward securing financial stability in the euro zone."

Mr. Riley added that "the reduction in interest rates and extension of maturities potentially offers Greece a window of opportunity to regain solvency, despite the formidable challenges that it faces."

REACTION, PAGE 13

VICTORY FOR EUROPEAN CENTRAL BANK?
It may be that Jean-Claude Trichet, the E.C.B. chief, quietly prevailed this week in responding to the Greek crisis. *PAGE 12*

EUROPEAN REVIVAL OBSTACLES
To prosper again, bailed-out euro zone states will have to regain ground on Germany, Floyd Norris writes. *PAGE 13*

ROLLING BACK SOVEREIGNTY TO SAVE EURO
E.U. members can have a common currency or fiscal independence, but not both, Floyd Norris writes. *PAGE 12*

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PAGE TWO

The nature of news in a new world

Alan Cowell

LETTER FROM EUROPE

LONDON What is news? News, they used to say at reporters' training courses in Britain, was the kind of snippet you might relay to a housebound relative, an interesting quirk that amused or informed or both. Dog bites man was not news. Man bites dog was.

But in recent times, the news seems to have shifted into ever more improbable terrain, even by the lights of a generation that grew up in the shadow of momentous change.

Consider the events of recent weeks in Britain: a newspaper, The News of the World, sold and read in the nation for 168 years, has been summarily closed by its owner, Rupert Murdoch, who subsequently was splattered by a shaving-cream pie as he testified before a panel of lawmakers about a sordid phone-hacking scandal within his media empire that threatens to rewrite the rules and codes of power built up over decades.

''Over the past two weeks, a torrent of revelations and allegations has engulfed some of this country's most important institutions,'' Prime Minister David Cameron told Parliament. ''It has shaken people's trust in the media and the legality of what they do, in the police and their ability to investigate media malpractice, and, yes, in politics and in politicians' ability to get to grips with these issues.''

But the intertwined issues of trust and seismic shocks to the system spread much wider in a world where the certainties assumed by earlier generations have crumbled.

Since the financial crisis of 2008, the underpinnings of the Western world have fallen into disrepute while China's economic power looms on an ever-closer horizon. Bankers, once accorded a measure of public confidence, now occupy much the same place in public perceptions among the bottom-feeders of a new era as journalists and politicians.

With the fall of the Berlin Wall in 1989, we knew that — or assumed that — the alternative to Communism was democracy. A few years later in South Africa we knew that the alternative to apartheid was freedom. The world was in balance between past and future. Leaders like Helmut Kohl in Germany and George H.W. Bush in the United States believed they could manage the transition to a new world order. But who foresaw a shift that has left Western strategists uneasily eyeing Beijing's century?

In the early 1990s, the Gulf War had clear aims to expel Saddam Hussein's forces from Kuwait and a clear end when they had been routed. A decade later, the attacks of Sept. 11, 2001, turned the kaleidoscope again, propelling Western armies into far murkier commitments in Iraq and Afghanistan.

The Arab Spring, once unthinkable in a regime of iron control by insouciant elites, has turned into the Arab Summer and soon-to-be Fall without a clear vision of where revolutions are going in Egypt and Tunisia, or where bloody uprisings will lead those still fighting stubborn dictatorships in Syria and Libya.

And what alternatives offer themselves at this time, in this specific week? Despite a last-minute bailout of Greece, the longer-term survival of the euro currency, barely more than a decade old, is still a matter of fevered debate. The national stereotypes assembled in the great European project — profligate southerners, industrious northerners — have reasserted themselves over the notion of a common destiny that has driven and expanded Western Europe since the 1950s.

Europe's uncertainty is rooted in runaway debt. The dominoes of potential default stretch from Greece and Ireland to major economies like Italy and Spain. But debt is something that raises an even bigger question in the United States: will America default on its multitrillion-dollar borrowings — a nightmare scenario without coordinates for a way forward? If U.S. Treasury bills can no longer be trusted, what can?

And that perhaps is what makes the news so different now — we know where we came from; but events offer no clear signposts to the future. Previous assumptions are inoperative.

Another adage from journalism school was that all news is local — and so it still is.

Yet, few things remain local in a new and unfiltered world of tweets and social networking, bloggers and broadband. Potentially, all news is global, or at least viral. So the consumer must beware of its provenance — caveat emptor. Nothing, it sometimes seems, can be taken at face value.

The so-called mainstream media have lost their cherished claim to act as the sole filter of raw information. Their exclusive lock on the dissemination of news has dissolved. If events themselves are opaque, then the plethora of versions brings no special clarity.

So what *is* news?

It is, still, the moment of disclosure when hidden facts are revealed: whatever else has changed, the notion of a scoop has not. Indeed, that raw hunger for exclusives was a contributing factor in Britain's phone-hacking scandal, made all the more visceral as traditional newspapers fight for survival against digital upstarts.

News is still the grist of our understanding of the world around us, beyond the narrow perspective of our own backyard. It is the incremental step propelling our comprehension of events.

Once, purveyors of news claimed that their product signaled the destination, too. ''Read all about it,'' the news vendors cried with a degree of chutzpah, as if the stories on those inky front pages contained all the answers.

These days, the call might need some rephrasing — less catchy but more modest — to say: ''Read what we know so far.''

E-MAIL: *pagetwo@iht.com*

Business

WITH REUTERS

E.U. must ditch euro or go forth and integrate

NEW YORK

BY FLOYD NORRIS

If there was one lesson to be learned ...m the European sovereign debt crisis, it was that monetary union by itself cannot work indefinitely. If Europe really wants to preserve the advantages of the euro currency, it will need far

NEWS ANALYSIS

more fiscal and economic integration. Nations will have to give up a significant amount of sovereignty.

European leaders seem to be willing to accept that reality. But persuading their publics may be far more difficult.

After more than a year of claiming that Greece could be bailed out without significant costs either for lenders or the rest of Europe, European leaders pledged Thursday to pump in large amounts of money to try to revive the Greek economy while delaying repayment and reducing interest rates on existing loans.

The deal appears to mean that solvent European nations will have to write some very large checks. Lenders will suffer losses, and some banks may need more bailouts, which Europe will pay for through a collective fund that will be authorized to borrow money backed by European states individually and collectively.

That fund, called the European Financial Stability Facility, will also take over lending to Greece, at rates close to what the facility is forced to pay when it borrows money.

Other parts of the communiqué issued by the European leaders after their summit meeting in Brussels promise that there will be more central control over national budgets and tax policies.

Call it the federalization of Europe.

Unlike in the first Greek bailout, in spring 2010, the European leaders now accept that the Continent has a responsibility not just to prevent collapse but to get the Greek economy moving again.

Over the 12 months ending in March, the Greek economy shrank by 5.5 percent, while unemployment, at 12.2 percent when the country was first bailed out, rose to 15 percent.

"We call for a comprehensive strategy for growth and investment in Greece," the statement said. While it removed a reference to "a European 'Marshall Plan'" that was in a preliminary version that was leaked earlier on Thursday, it promised that the rest of Europe would "work with the Greek authorities on competitiveness and growth, job creation and training."

Pouring money in will not, in and of itself, make Greek industries competitive again and enable the country to flourish. In fact, it was money pouring in for most of the past decade that helped to create the problem. Investors were willing to lend money to Greece at basically the same rate they charged Germany, on the theory that a common currency should mean common interest rates.

Those savings — Greece's effective borrowing rate was cut by more than half from 1998 to 2005 — enabled the government to spend more and tax less than it otherwise would have been forced to do.

That was not what advocates of the euro forecast when the currency was being created more than a decade ago.

The theory was that countries would enact reforms — in labor markets, fiscal policies and even work habits — to become more like Germany. They would do that because a failure to do so would lead a country to lose competitiveness as its costs rose more rapidly than those of Germany while the prices it charged could not do so, since both countries used the same currency.

Europe claims it will change, but there is obviously some resistance to detailed commitments.

The leaked draft included a promise to "introduce legally binding national fiscal frameworks" by the end of 2012. The final communiqué took out the words "legally binding."

The countries previously promised not to run large budget deficits, but they all did when the world went into recession. This time, though, we are assured they really mean it.

With more control over fiscal policy at the European level, Europe is also moving toward something akin to a European monetary fund in the financial stability facility, known as the E.F.S.F. It would be able to buy Greek government bonds on the secondary market, effectively reducing the Greek national debt since Greece would owe what the bonds cost the E.F.S.F., not the higher face amounts.

If there is little enthusiasm in Europe for such centralization of power, there is even less for the obvious alternative: abandoning the euro. Had Greece not been in the euro zone, it probably would have followed the Argentine path of nearly a decade ago: default and devalue. With Argentina's industries newly competitive because the peso lost most of its value within weeks, Argentine exports and the economy recovered faster than many expected.

There is, however, no clear way for a country to leave the euro, and no leaders have advocated it.

But the effort to rescue Greece on the cheap clearly did not work. The deal Europe now advocates will force losses on banks. Major banks have signed on to plans that will force them to accept lower interest rates and extended maturities or, if they prefer, somewhat higher interest rates on bonds whose principal would be reduced by 20 percent. In return, Europe as a whole would effectively guarantee eventual principal repayment.

EUROPE, PAGE 14

E.C.B. loses one but wins a few in deal for Greece

FRANKFURT

E.U. governments agree to take wide responsibility for bloc's performance

BY JACK EWING

Chancellor Angela Merkel of Germany and other European leaders appeared to have acted in defiance of the European Central Bank when they insisted that banks chip in as part of the latest Greece rescue plan. But, in the long-

NEWS ANALYSIS

running clinch between central bankers and politicians over how to handle the crisis, it may be the central bank pre... dent, Jean-Claude Trichet, who quietly prevailed this week.

The E.C.B. lost the battle to prevent European leaders from precipitating a partial default of Greek debt. But, after meeting with Ms. Merkel and other leaders in Brussels on Thursday, Mr. Trichet appeared to have won on a more important issue: getting governments to reclaim the task of preventing collapse of the Greek economy, as well as wider responsibility for fiscal performance of the euro area.

"Have they backed down?" Peter Westaway, chief European economist at Nomura International, said of the E.C.B. "To an extent they have." But in the process, he and other economists said, the central bank extracted concessions that allow it to spend less time saving Greece and concentrate on its day job, overseeing monetary policy.

"The E.C.B. is trying to resist anything that makes it look like monetary authorities are taking on a role that governments should be taking on," Mr. Westaway said.

Mr. Trichet won commitments from governments in Brussels on another longstanding demand. Political leaders agreed to take more concrete steps to reduce their debt and ensure that the Greek disaster does not repeat itself in some other corner of the euro area. Euro area countries promised to cut their budget deficits to below 3 percent by 2013, in line with limits set by treaty but widely violated.

The European countries also agreed to support Greek banks, another task that has been handled primarily by the E.C.B. And the leaders will do more to help Greece fix its dysfunctional economy.

"The decision of member states and of the commission to mobilize all resources necessary in order to provide exceptional assistance to help Greece in implementing its reforms is very, very important," Mr. Trichet said in Brussels on Thursday, according to Reuters.

A high-ranking monetary policy official, who could not be quoted by name because of the sensitivity of the matter, said, "We got what we wanted."

Since the debt crisis began last year, there has been a strong temptation for Ms. Merkel, President Nicolas Sarkozy of France and other leaders to let the E.C.B. do the heavy lifting. Unlike the politicians, Mr. Trichet and his c... leagues on the governing council cann... be voted out of office and were able t... act more decisively. The E.C.B. also ha... extensive financial resources and doe... not need an act of Parliament to deplo... them — though it always took pains t... avoid any appearance that it was print... ing money.

But, though Mr. Trichet always framed the E.C.B.'s actions in terms of monetary policy, he faced increasing criticism that the bank had compromised its sacred independence from politics. He was clearly annoyed at political leaders for their lack of stronger action. During a meeting last year, he even got into a shouting match with Mr. Sarkozy according to several people present.

The package announced in Brussel... late Thursday shifts responsibility for ... number of key tasks from the E.C.B. t... governments. For example, the Eur... pean Financial Stability Fund will hav... the power to buy government bo... open markets to stabilize prices, a... ing the central bank to wind down ... own highly controversial bond-buyi... program. The decision in May 2010 ... the E.C.B. to begin buying Greek, P... tuguese and Irish bonds split the ban... governing council and has left the b... with billions in distressed debt.

"It is no longer necessary for ... E.C.B. to do this job, which is a plu... the E.C.B.," Jörg Krämer, chief ec... mist at Commerzbank, said in Fr... furt.

European leaders will also guar... the quality of Greek bonds even if ... ratings agencies declare the coun... be in partial default. Fitch Rating... Friday that the plan to extract a ... bution from bond investors would... constitute a restricted default.

The European Union gua... mean that the E.C.B. can contin... cept Greek bonds as collateral fo... term loans, maintaining the ...

CENTRAL BANK, PAGE 14

How to make the case for a new stimulus

Economic View

ROBERT J. SHILLER

The fight over the U.S. debt ceiling has deflected attention from the serious problems of fixing the economy and finding jobs for the 14 million unemployed. Worse, it has created strong negative feelings about fiscal policy, just when other measures seem incapable of restoring economic health.

The very term "fiscal stimulus" has become tainted. John A. Boehner, the Republican who is speaker of the House of Representatives, refers to a "misguided 'stimulus' spending binge."

It is a label that reflects how many people have come to think of government expenditures to stimulate the economy — as a binge, maybe like an overdose of amphetamines. For amphetamines, the aftereffects are mental fatigue and depression. For fiscal stimulus, it is the headache of national debt — or at least that is the all-too-common view.

Fiscal stimulus is actually very useful and appropriate in the current circumstances. But rather than despair, we should at least consider what more we should be doing to deal with the pressing issue of unemployment. Let's never give up proposing sensible economic policies.

Find worthwhile jobs for the unemployed, and do not inject stimulus for its own sake.

Over the long haul, we should be engaged in balanced support of the economy, and find worthwhile jobs for the unemployed, and not inject stimulus for its own sake. That means we will need tax increases matched by higher expenditures on public goods. Of course, both ideas are not very popular right now — but they should be. Granted, they will not balance the U.S. budget immediately; trying to do so would damage the economy. Instead, we should plan to restore budget balance eventually, with matching additions on both sides of the ledger.

In December, I wrote about the concept of the balanced-budget multiplier and of raising taxes and government expenditure by the same amount, dollar for dollar. These ideas were first put on the national stage in 1943 by Paul Samuelson, the Nobel laureate. He argued that such a policy would be one-for-one expansionary: each dollar spent is a dollar of new national income. As long as interest rates are near zero — as they were then and are now — there should be no "crowding out" of private ...penditures by government ones.

We can restore some worthwhile projects that have already been cut significantly, including programs in health care, education and other social services; infrastructure; the environment; and the arts and sciences. Beyond that, we should create major new programs, all paid for by additional taxes.

Ideally, these programs should involve real expenditures on goods and services that will immediately create jobs. With enough such support, we should be able to bring down unemployment until increased demand starts taking care of the problem itself.

This is an expansionary change in fiscal policy that will not require additional increases in the national debt.

We should start a dialogue right now about taking action, before the damage of protracted unemployment worsens.

The fighting over the debt ceiling, the concerns about America's credit rating — about the United States somehow go-

DEBT, PAGE 15

KEVIN SCANLON FOR THE NEW YORK TIMES

Whose playhouse is it, anyway?

HOUSTON

Rising sales seem to defy recession as parents buy backyard bling for kids

BY KATE MURPHY

Apart from the open bar arranged by the swimming pool, the main attraction at parties held at the Houston home of John Schiller, an oil company executive, and his wife, Kristi, a Playboy model turned blogger, is the $50,000 playhouse the couple had custom-built two years ago for their daughter, Sinclair, now 4.

Cocktails in hand, guests duck to enter through the low door. Once inside, they could be forgiven for feeling as if they have fallen down the rabbit hole.

Built in the same Cape Cod style as the Schillers' expansive main house, the two-story, 170-square-foot, or 16-square-meter, playhouse has vaulted ceilings, furnishings scaled down to two-thirds of adult size, hardwood floors and a faux fireplace with a fanciful mosaic mantel.

The little stainless steel sink in the kitchen has running water, and the matching stainless steel mini-fridge and freezer are stocked with juice boxes and ice pops.

Upstairs is a sitting area with a child-size sofa and chairs for watching DVDs on the 32-inch flat-screen television. The windows, which open, have screens to keep out mosquitoes, and there are begonias in the window boxes. And, of course, the playhouse is air-conditioned. This is Texas, after all.

"I think of it as bling for the yard," Ms. Schiller, 40, said.

Some people might consider it "obnoxious" for a child to have a playhouse that costs more and has more amenities than some real houses, she conceded. But she sees it as an extension of the family home. "My daughter loves it," she said. "And it's certainly a conversation piece."

Even in a troubled economy, some parents of means are willing to spend significant — if not eye-popping — sums on playhouses for their children that also are a kind of backyard installation art.

There are a number of companies and independent craftsmen in Europe and the United States making high-end playhouses that can cost as much as $200,000, and come in a variety of styles, including replicas of real houses, like the Schillers', and more fantastical creations like pirate ships or tree-top hideouts. And many manufacturers report that despite the economic downturn, they are as busy as ever, selling units as far away as France, Kazakhstan, Australia and India.

Barbara Butler, an artist and playhouse builder in San Francisco, said her sales were up 40 percent this year, and she had twice as many future commissions lined up as she did a year earlier. And the price of the average structure she has been hired to build has more than doubled, to $54,000 from $26,000.

"Childhood is a precious and finite thing," Ms. Butler said, by way of explanation. "And a special playhouse is not the sort of thing you can put off until the economy gets better."

Likewise, Glen Halliday, who has a playhouse business in Portland, Maine, said he had seen profit increase 15 per-

STRUCTURE, PAGE 15

MEGAN THOMPSON LOVOI

Kristi Schiller and her daughter, Sinclair, in the playhouse that is a scaled-down copy of their Houston home. At top, Kate and Barrett Burnham make use of their expansive treehouse in the California backyard of their grandfather, Dan Burnham.

Merkel at center stage in 11th-hour bargaining over accord

MERKEL, FROM PAGE 1

petitiveness. And it is highly unlikely to be the last time.

The issues are fundamental, but they are political as much as economic. European democracy is fraught with the complications and difficulties of 27 nations plus European institutions with unclear or shifting responsibilities. And it was all on display in this crisis: internal German politics, the qualms of the European Central Bank, the plight of the Greeks and the contagion of market anxieties to Italy and Spain, which are too big to bail out. Jean Pisani-Ferry, the director of Bruegel, an economic research institution in Brussels, said the summit meeting "gave something for everyone." It helped ease the growing panic, he said, and "a number of taboos have been broken."

Mrs. Merkel won the participation of private banks she so desperately wanted, but in the process let the European Union slide one step closer to the sort of economic government so deeply abhorred by stingy German taxpayers. Her change of heart reflected loud and growing panic at home this week that her dithering was endangering a European project at the center of German policy and interests since end of World War II.

Yet as she faced reporters in Berlin on Friday Mrs. Merkel seemed supremely confident and at ease. She felt that she had achieved more than what one local paper called "a victory on points," getting more than she gave.

"All of Europe has undertaken reforms that a year and a half ago would not have been conceivable," Mrs. Merkel said, pointing to the higher retirement age in Spain, the sale of state-owned assets in Greece, savings packages in Ireland and Italy and even a new commitment in France to bring down its own budget deficits.

"You have to tackle the problem at the root," Mrs. Merkel said, summing up her prescription of strict austerity measures to reign in budget deficits.

With last-minute German and European Central Bank flexibility, the Europeans came together to find a broad compromise and some structural changes that eased the burden on Greece, gave a modest bill to the private financial institutions and empowered a Europeanwide fund to act more broadly to buy up bad debt. The moves seemed to appease the markets for now, especially with the long European summer holidays on tap.

Still, as usual in the European Union, all steps are partial, and Greece is considered almost sure to need more debt restructuring. But Mrs. Merkel's grudging willingness to put taxpayer money and guarantees more firmly behind the debts of Greece, Portugal and Ireland, and to defend other countries at risk, is a significant step toward the Europeanization of sovereign debt and marks an important moment.

It did not always look like the summit would happen. After the meeting of European finance ministers, Mrs. Merkel told Herman Van Rompuy, the president of the European Council, by telephone, "I'm only going to the council if there's actually going to be something to decide there."

But pressure at home mounted, with even members of her own party attacking her at a volume and with a ferocity unseen during the slowly unfolding crisis, saying she was jeopardizing Europe and in the process the fragile world financial system. President Obama was concerned enough to phone Mrs. Merkel on Tuesday and remind her of her country's responsibility.

On Wednesday afternoon in the German financial capital of Frankfurt, Jean-Claude Trichet, president of the European Central Bank, sat around the donut-shaped conference table in the E.C.B.'s high-rise headquarters with the bank's 23-member governing council. Though they were staunchly opposed to compelling banks to share the cost of the Greece package, the members recognized that Germany was determined to extract a contribution from the private sector, which would mean at least a partial default.

The bank's council agreed to insist on several conditions. European countries must guarantee Greek bonds so that they would still be eligible as collateral for E.C.B. loans. The leaders would have to agree to support Greek banks and to step up assistance to Greece in fixing its economy.

The council was united in insisting that private investors paying a share should not set a precedent that could be extended to other nations like Ireland or Portugal. "It should be unique," said a person with direct knowledge of the discussions, who could not be identified because of the sensitivity of the matter.

President Nicolas Sarkozy of France was worried about the outcome of the summit and even whether Mrs. Merkel would show up. They had spoken on the phone in what he described to aides as a "sterile" conversation. He decided to fly at the last minute to Berlin on Wednesday afternoon, with no return flight to Paris before the summit. Mr. Sarkozy was expecting a late night.

"I need to deploy my energy," Mr. Sarkozy told his cabinet Wednesday morning, before leaving, "but at the same time I need to not hurt anyone's feelings."

After negotiating all afternoon, the president of France and the chancellor of Germany dined on duck with potato purée, but it was not until they were joined around 10 p.m. by Mr. Trichet, and a call was placed to Mr. Van Rompuy, that any conclusions could be reached. The meeting concluded after midnight. A deal had been reached but Mr. Trichet left looking unhappy, as the French newspaper Le Monde reported.

The European Central Bank head had been cajoled into accepting the possibility of a selective default, but everyone had to give something up. Mr. Sarkozy was obliged to table a plan to tax banks; Mrs. Merkel was forced to accept a substantial reinforcement and expansion of the region's rescue fund, the European Financial Stability Facility, or E.F.S.F., by allowing it to buy sovereign debt on the secondary market and from the European Central Bank.

The fund would be responsible for this second Greek bailout, but would also be responsible for recapitalizing troubled banks. It would also be instructed to tender its loans at a wholesale price, with none of the punitive extra interest Mrs. Merkel had earlier favored.

With its new powers, the E.F.S.F. begins to look something like a European monetary fund, making all euro zone taxpayers responsible for guaranteeing most of the debts of countries like Greece, Portugal and Ireland, something German officials and in particular German voters have opposed. But with the government in Athens already unpopular with the austerity-beaten Greek people, concessions would have to be made.

The Greek delegation arrived in Brussels on Wednesday under intense criticism from the right and the left. Mr. Papandreou met with José Manuel Barroso, the president of the European Commission, the E.U.'s executive arm. He received no reassurance that Greece would receive what it so desperately needed: a commitment for more funds as well as financial support for a deal to be cut with its creditors. Aids to the prime minister described his mood as a bit glum.

ERIC FEFERBERG/AGENCE FRANCE-PRESSE

President Nicolas Sarkozy of France talking with reporters after the E.U. summit meeting that agreed on a second bailout for Greece.

But things improved on Thursday, the day of the summit. Evangelos Venizelos, the finance and deputy prime minister who has taken a forceful role in pushing Greece's agenda for change both at home and abroad, met in the morning with Josef Ackermann, the chief executive of Deutsche Bank and chairman of the International Institute of Finance, the international bank group.

Mr. Ackermann went to Brussels on Tuesday and stayed through Thursday, according to a person close to him who was not authorized to speak publicly. Working the phones and meeting privately with the government leaders, Mr. Ackermann acted as an intermediary between the politicians and the bankers, knowing as a German that "it would hardly be possible to bring this package through parliament without private sector participation," as Mr. Ackermann told ZDF television in Germany.

While the final details of the debt extension and so-called haircuts, in which lenders would share the pain, to ease Greece's interest load were not discussed in detail, Mr. Ackermann and bank officials expressed their support and suggested a deal was possible. An early meeting over Gummi bears, cookies and a thermos of coffee with Mrs. Merkel and Mr. Sarkozy was also encouraging.

After opening statements, the European Commission president, Mr. Barroso, spoke for many in the room when he said that the crisis had not been handled correctly. "We should have solved some of these issues before," he said, according to a senior European Commission official.

The atmosphere was serious but constructive, a diplomat involved in the negotiations said, because everyone knew how serious the stakes were. Mrs. Merkel and Mr. Sarkozy "were speaking with one voice," the diplomat said, which was fortunate with all the divisions in the room.

The Greeks were appalled to find language in an early draft of the summit statement, inserted by the Dutch and Finnish delegations, demanding that loans to Greece be secured by those physical assets such as buildings, land and companies slated to be privatized. "We are a sovereign country, not a company," said one member of the delegation. "It was very insulting."

Mr. Papandreou huddled with his advisers and returned to the meetings where he made it clear that such a condition was not acceptable. His message was clear: any notion that Greeks were putting up land as collateral for loans would create a political crisis at home and even the government's fall.

A bit of strategy might have been at play when Mrs. Merkel found herself seated at lunch between Mr. Papandreou and Pedro Passos Coelho of Portugal, both from countries in desperate need of Germany's assistance. Mrs. Merkel, having watched the first Greek bailout and austerity measures fail to produce economic growth, was willing, like the scientist she is, to try something different, understanding that the failure was not just because of Greek actions but also because of flaws in the first bailout.

At last the compromise language was agreed upon. It may have been a sign of how effective the negotiations were that no side felt they had gotten all they were looking for or lost entirely.

While the E.C.B. conceded the battle on private-sector participation, the bank achieved its goal of tightening euro area discipline and shifting responsibility for supporting Greece to European countries — a major victory from the E.C.B.'s point of view. While the E.C.B. has not formally shut down its bond-market intervention program, Thursday's agreement allows the E.F.S.F. to buy European government debt in open markets and also relieve the E.C.B. of that task.

With customary overstatement, Mr. Sarkozy saw the deal as a major move toward more European integration, but

"All of Europe has undertaken reforms that a year and a half ago would not have been conceivable."

there is no question that the new role for the European Financial Stability Facility is the major change, which the French leader described as "the initiation of a European monetary fund."

"Our ambition is to seize the Greek crisis to make a quantum leap in euro zone governance," Mr. Sarkozy said Thursday night.

Aides to Mr. Papandreou and Mr. Venizelos described the two men as very happy and relieved by the outcome. But in keeping with the mood of austerity, there was no shindig at a Brussels restaurant or popping of champagne corks. Instead, following a news conference for the Greek press, the 20-member delegation drove to straight to the airport and took a single government plane home to Athens, arriving, quite exhausted, at 430 in the morning.

Mr. Sarkozy returned home to his expected, possibly required, shower of praise from advisers. Mrs. Merkel got to give a lecture to reporters Friday in Berlin on the importance of solidarity on the one hand but responsibility, meaning austerity, on the other. "A Europe without the euro is unthinkable," said Mrs. Merkel, who described her personal "Merkel-ish" passion for Europe, which had been so questioned all week. "We know that the problem of one is also the problem of all."

Steven Erlanger reported from Paris. Landon Thomas Jr. in London, Jack Ewing in Frankfurt, Stephen Castle in Brussels, Rachel Donadio in Rome, Judy Dempsey in Berlin and Niki Kitsantonis in Athens contributed reporting.

The next step: Playing catch-up with Germany

Floyd Norris

OFF THE CHARTS

If the economies of the bailed-out countries in the euro zone are ever going to prosper again, they will have to somehow regain competitiveness with Germany, the dominant economy in the zone.

New figures released by the European Central Bank indicate that progress is being made, but it is slow.

The figures show that unit labor costs fell 3.3 percent in Greece during the first quarter, and were off 2 percent in Ireland. In Germany, the star economy of the euro zone, unit labor costs fell 0.7 percent.

Those reductions were won at a terrible cost, however. Greece's economy continues to shrink, while Ireland's seems to have stopped losing ground but has yet to grow. Unemployment is above 14 percent in Ireland and even higher in Greece.

The accompanying charts show the changes in unit labor costs in Ireland and Greece, as well as in Germany and four other large economies that use the euro — France, Italy, Spain and the Netherlands. The central bank said similar figures for Portugal, the other bailed-out euro country, were not available.

The first set of charts shows the changes from the first quarter of 2010, just before the first Greek bailout forced the country to agree to a harsh austerity program, through the first quarter of this year, the latest figures available.

During that period, Greek unit labor costs fell 7 percent, nearly twice as much as those in Germany. Ireland's costs were down almost 6 percent.

But all the other major countries continued to lose ground to Germany.

The second set of charts shows the changes in unit labor costs since the end of 2000, when Greece joined the euro zone. The figures are dramatic. Germany's unit labor costs declined nearly 7 percent over the period, a remarkable performance. All the other countries had increases, ranging from 11 percent in France to more than double that figure in Ireland.

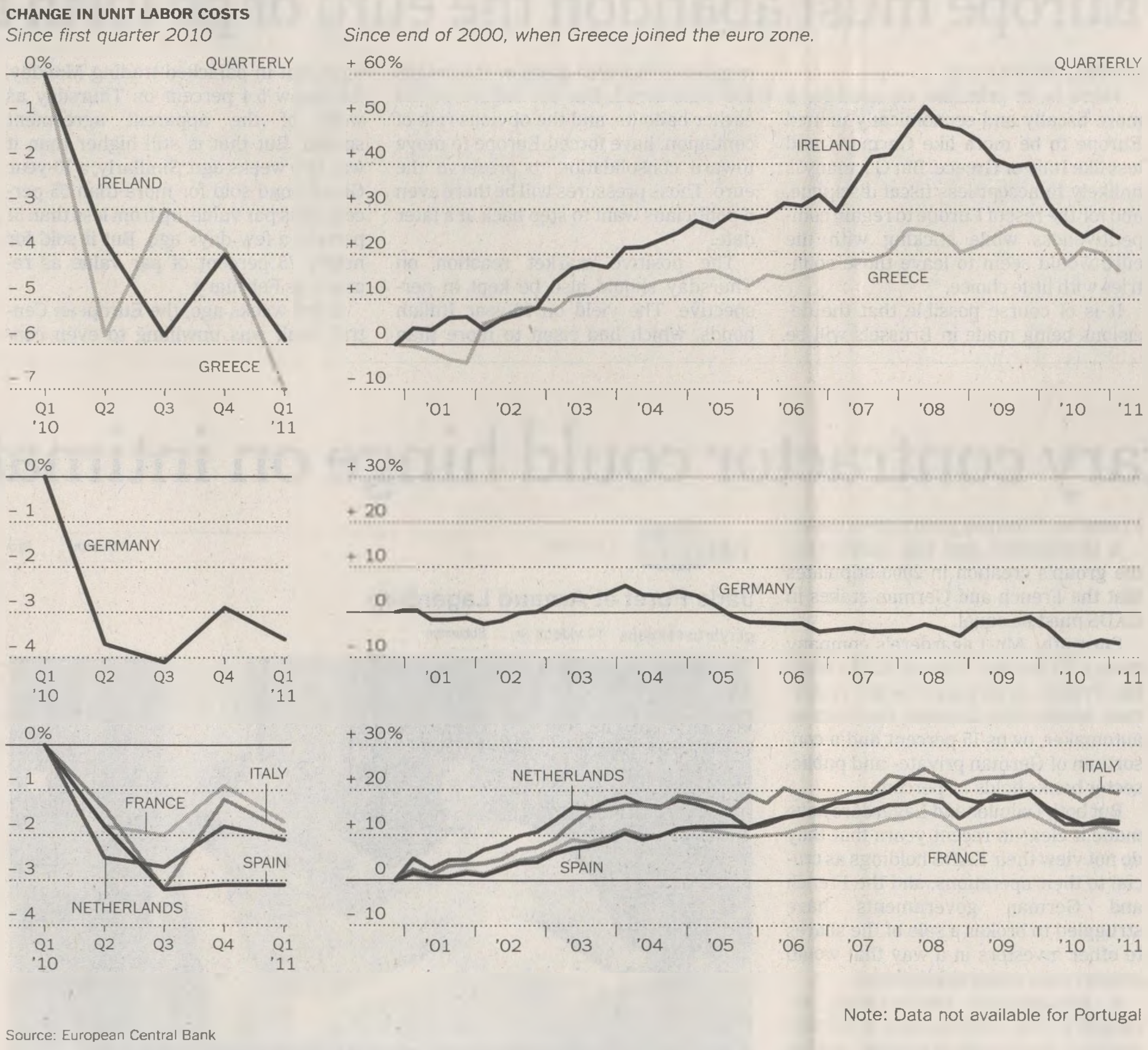
If there were no euro, other European currencies would almost certainly have lost value against the German mark over the past decade. Instead, Germany's trade surplus in goods rose sharply, while the rest of the euro zone's combined trade deficit approximately doubled.

The reconvergence of the economies might be easier if Germany were to accept inflation, but it shows little inclination to do that. Indeed, largely because Germany has been growing at a rapid rate, with some signs of inflationary pressures, the central bank has begun to raise interest rates.

Unit labor costs are not the only variable in a country's trade performance, of course. But they are important. The rest of the euro zone has a long way to go if it is to regain the competitive position it had only a few years ago.

More competitive, but a long way to go

Since harsh austerity policies were imposed in Ireland and Greece, their unit labor costs have fallen faster than in other European countries. But they remain far from competitive, particularly with Germany.



Source: European Central Bank

Note: Data not available for Portugal

Markets lend their support to new Greek rescue plan

REACTION, FROM PAGE 1

The Fitch rating agency said it would place the Greek sovereign debt into "restricted default" and assign a "default" rating to the affected Greek bonds when they are offered to be exchanged for ones with longer terms.

After the new bonds are issued, the agency said it would likely classify the new securities as "low speculative-grade."

Some senior European officials conceded Friday that the desire to have banks share in the losses caused by extending the maturity of loans to Greece had destabilized markets and would have been better avoided. However, the officials said they saw banks' participation as a necessary price to pay to gain the support of the German chancellor, Angela Merkel, who has to assuage a restive public opinion at home.

"I would have preferred not to have this private-sector involvement," said one senior European Commission official speaking on condition of anonymity because of the sensitivity of the issue.

"It was a sine qua non for some member states," the official added, "but it would have been less risky and less expensive without" it.

The deal involves an extra outlay for the donor countries because guarantees will have to be extended to ensure that the Greek banks continue to receive liquidity if Greece is classified as being in default. However the architects of the new rescue hope that this will only be for a short period of time, limiting the cost of the financial maneuver.

Meanwhile, financing has to be put up to fund a bond buyback plan on which, ultimately, the private sector will take a loss. According to the estimates provided by the euro zone countries, the net contribution of the private sector will be an estimated €37 billion from 2011 to 2014.

That will come on top of the €109 billion bailout for Greece, though this total does include an estimated €28 billion in receipts from privatization up to 2014 and €20 billion for financing debt buybacks. The proportion that will be lent by the International Monetary Fund has yet to be determined.

European leaders want to tamp down debate about private-sector losses, which has the potential to increase market worries about other euro countries' debt.

During the summit meeting Thursday, Jean-Claude Trichet, president of the European Central Bank, showed a graph illustrating the movement of bond spreads and how closely they were linked to discussion of the private sector contribution, according to a senior official of the European Commission, the executive of the bloc.

Though leaders pledged in the communiqué that this would not be repeated in any other case, the markets may take more note of the fact that reduced interest rates will make the finances of Ireland and Portugal more sustainable.

"I don't think the euro zone is out of the woods," said Nicolas Véron, senior fellow at Bruegel, an economic research institute in Brussels, "but Ireland and Portugal have been strengthened. It is much more credible that they can meet their commitments than before."

Lending rates for the three countries will fall to around 3.5 percent and loan maturities will be stretched to between 15 and 30 years.

Mr. Véron said that the motivation for involving banks in the deal was primarily political. "If the aim was to have a reduction in Greek debt manageable then it has not been structured effectively but I don't think that was the main intention."

"If you want to keep the scheme voluntary and minimize free-riding you have to take a balance."

Some European officials believe that working with the big banks will help solidify the common currency.

The International Swaps and Derivatives Association said the Greek rescue plan should not trigger credit-default swaps on the country because it would be "voluntary."

The Greek finance minister, Evangelos Venizelos, said the pact hammered out in Brussels on Thursday represented "a strong unified European front protecting Greece" and "an umbrella of protection for Greek banks" as well.

Niki Kitsantonis reported from Athens. Matthew Saltmarsh reported from London. Raphael Minder contributed reporting from Madrid.

Tangled lawsuits embroil staid 3M

NEW YORK

Maker of Scotch tape at center of dispute over test for deadly bacteria

BY BARRY MEIER

It is a legal scrap with tabloid sensibilities: extortion charges, libel claims, British royalty — and a prominent U.S. protagonist, 3M, a purveyor of staples like Scotch tape and Post-it notes.

It began three years ago as a routine lawsuit over a diagnostic test to be marketed by 3M that detected a highly resistant bacterium often found in hospitals. But it has since escalated into a trans-Atlantic swill of suits and countersuits that now ensnare 3M's chairman and chief executive, Britain's secretary of defense and a well-known Washington lawyer and lobbyist, Lanny J. Davis.

In one lawsuit, 3M charged that a big investor in the diagnostic test had tried to blackmail the company into settling its lawsuit for $30 million by suggesting that a knighthood conferred on the 3M chief executive, George W. Buckley, could be derailed. In turn, that big investor, Harvey Boulter, filed a libel suit against 3M, Mr. Buckley and a lawyer for the company. And in a legal filing on Thursday, 3M suggested that Mr. Davis — probably best known for his role in defending President Bill Clinton during his impeachment trial — had been part of a conspiracy to shake down the company.

Mr. Davis, who represents Mr. Boulter's equity fund, had masterminded a series of attacks on 3M that "began as a defamatory media blitz and culminated in the outright attempted blackmail of 3M and its chairman," the company asserts in papers filed in State Supreme Court, a trial court, in New York City.

A 3M spokeswoman declined to make Mr. Buckley available for comment.

Mr. Davis said the company's filing was untrue and intended to divert attention from 3M's own problems. "I am accustomed when speaking publicly in only dealing in facts that can be documented," he said.

The dispute can be traced to 2005 when the equity fund headed by Mr. Boulter acquired a majority interest in the diagnostic test, which was based on technology developed by the British Ministry of Defense. The test, known as BacLite, offered a faster way to identify hospital patients who were carriers of the bacterium methicillin-resistant Staphylococcus aureus, or MRSA. In recent years, MRSA infections, which are resistant to antibiotics, have caused patient deaths and injuries.

Initial studies indicated that BacLite was highly accurate, and in 2007, 3M struck a multimillion-dollar deal to acquire the test, though the majority of that payout was tied to future BacLite sales. Just a year later, however, 3M dropped BacLite, saying that its subsequent studies found a high rate of false results. By then, several competing MRSA tests had also been introduced.

Entities associated with Mr. Boulter's fund, the Porton Group, responded with a lawsuit filed in 2008 in London, claiming that 3M had failed to fulfill its agreement to diligently market BacLite. And over the next three years, the case puttered along quietly until just before it went to trial last month.

In May, Mr. Davis and some patients held a demonstration outside 3M's corporate headquarters in St. Paul, Minnesota, at which he accused 3M of abandoning a "lifesaving" technology.

In addition, Mr. Davis filed a petition with the U.S. Food and Drug Administration asking it to investigate how 3M had conducted its tests of BacLite, which he says the company botched. He also helped set up www.mrsa-injustice.com, a Web site that tells the dispute from the side of Mr. Boulter's fund.

Early last month, Queen Elizabeth II announced that Mr. Buckley, who holds U.S. and British passports, would receive a knighthood. And as the lawsuit against 3M began to unfold in a London court, Mr. Davis and 3M's outside lawyer, William A. Brewer III, spoke about a settlement, though those discussions apparently did not advance far.

Then, in mid-June, Mr. Davis suggested that Mr. Brewer and Mr. Boulter speak directly with each other. Soon, accusations began to fly.

To hear Mr. Brewer tell it, he was biking in Sag Harbor, New York, when he received a cellphone call from Mr. Boulter, who had just arrived in Italy from Dubai, where his fund is based, and was driving down the coast to reach his yacht.

After exchanging pleasantries, Mr. Brewer said that the businessman began making references to talks about BacLite he had been having with Liam Fox, the British defense secretary. The call between the two men then broke off, Mr. Brewer said, as Mr. Boulter drove through a series of tunnels along the Italian coast. Not long after, the lawyer received a lengthy e-mail from Mr. Boulter that 3M said in the lawsuit contained the blackmail threat.

Along with the reference to the "embarrassing situation of George's knighthood," Mr. Boulter also wrote in the e-mail that he had a lengthy conversation earlier that day with the defense secretary on "our current favorite topic." He stated that British officials viewed 3M's decision not to market BacLite as a violation of trust and that, while 3M might prevail in a courtroom, there could be business ramifications for the company.

"It might leave Gov quietly seething for a while, with ramifications for a while — they have memories like elephants," he wrote. He suggested that 3M settle the case, adding that at a "headline of $30mn+ you will allow MoD to internally save face." Mr. Boulter rejected any suggestion that his e-mail contained a

GIUSEPPE ARESU/BLOOMBERG

George W. Buckley, chief of 3M, who was recently named to receive a knighthood.

threat to 3M, adding that he had discussed the note's contents with Mr. Brewer before sending it. He also said that his reference to his discussion with Mr. Fox about "our current favorite subject" was not about BacLite.

"I thought I was in a good-faith confidential settlement discussion," Mr. Boulter said.

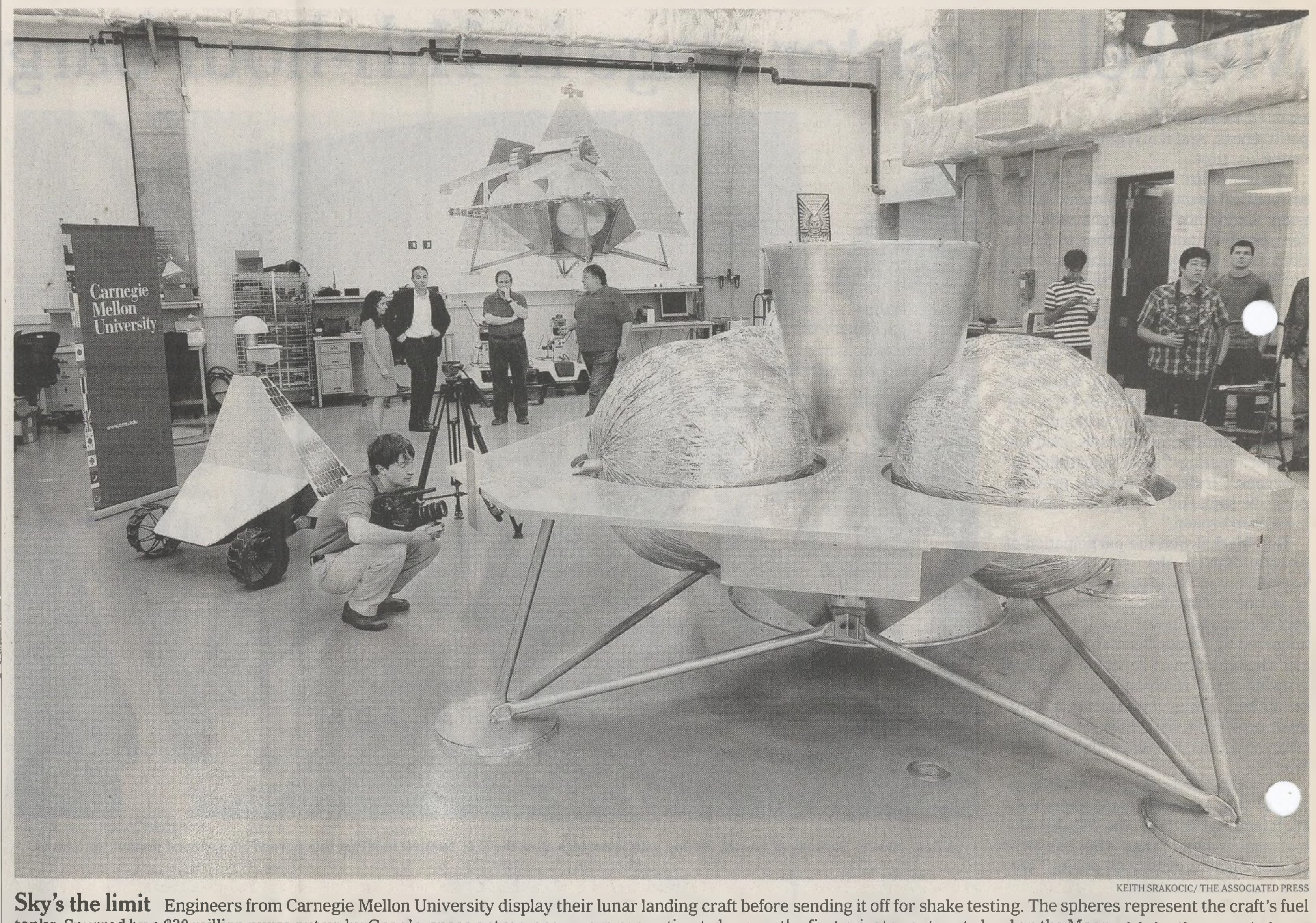
Mr. Brewer said that Mr. Boulter's threat was clear and that he reinforced it in a second e-mail, in which Mr. Boulter cited Mr. Fox again, writing "I need to tell something" to him.

"3M quickly decided that the only way to treat this type of behavior was to push it out into the sunlight immediately," Mr. Brewer said.

Mr. Boulter said that he and the defense secretary had briefly discussed the BacLite lawsuit as part of a broader conversation and that he brought up the potential public relations problems for Mr. Buckley given his knighthood and 3M's behavior in the case. "I said it was unfortunate because it was going to attract a lot of media attention," Mr. Boulter said.

Asked about Mr. Boulter's comments, a spokesman for the Ministry of Defense said that Mr. Fox and Mr. Boulter had not discussed the BacLite case or anyone's knighthood.

A decision in the MRSA-related lawsuit against 3M is not expected for some time.



KEITH SRAKOCIC/THE ASSOCIATED PRESS

Sky's the limit Engineers from Carnegie Mellon University display their lunar landing craft before sending it off for shake testing. The spheres represent the craft's fuel tanks. Spurred by a $30 million purse put up by Google, space entrepreneurs are competing to become the first private venture to land on the Moon. **global.nytimes.com/science**

Ex-China Mobile executive sentenced to death

SHANGHAI

BY DAVID BARBOZA

A former top official at China Mobile, one of the biggest state-owned telecommunications companies in the country, was sentenced to death with a two-year reprieve Friday for accepting bribes, according to Xinhua, the state-run news agency.

The former executive, Zhang Chunjiang, who was vice chairman of China Mobile, the largest cellphone operator in the world by subscribers, was charged with accepting more than $1.15 million in bribes while working at a series of state-run telecommunications companies from 1994 to 2009, when he was removed from his post.

The sentencing, by a court in Hebei Province in northern China, is the latest development in a corruption investigation into this country's powerful telecommunications oligopoly.

While state executives and government officials are regularly arrested on corruption charges, only a handful have received the death penalty in recent years. Four years ago, the head of the Food and Drug Administration in China was executed for corruption and failing to protect consumers.

The former chairman of Sinopec, the Chinese oil giant, was also sentenced to death with a two-year reprieve for accepting millions of dollars in bribes. And this week, two former vice mayors in China were executed for accepting millions of dollars' worth of bribes.

Beijing is in the midst of a major corruption sweep before a leadership change expected next year. In some cases, analysts say, those charged with corruption may be targeted because of their relationships with high-ranking politicians who are engaged in power struggles.

Recently, prosecutors have focused on the telecommunications industry. At least seven other executives from China Mobile are under investigation in corruption cases, according to the state-run news media. And investigators are also looking into the role of several prominent Chinese businessmen, including Zeng Liqing, one of the founders of Tencent, a top Chinese Internet company, according to Caixin magazine, one of the country's most respected publications.

State-run news media said Mr. Zhang, the former China Mobile executive, had confessed to his crimes and so was given the death penalty with a two-year reprieve, which means that with good behavior his sentence could be commuted to life in prison.

Xinhua reported that Mr. Zhang, 53 years old, took the bribes while working as deputy director of the Postal Administration of Liaoning Province and also while working as general manager of China Netcom Group and party chief and deputy general manager of China Mobile.

E.C.B. loses one but wins a few in bailout for Greece

CENTRAL BANK, FROM PAGE 12

E.C.B. funds to Greek banks which are shut out of international money markets.

"In our view this is a very important sign of institutional respect from Europe to the E.C.B.," analysts at Royal Bank of Scotland said in a note Friday.

Analysts cautioned that the rescue plan, outlined in a four-page statement by European leaders Thursday, was short on detail. It is not clear, for example, if the euro area countries are committing enough money to support the Greek banks, Mr. Krämer of Commerzbank said.

He was also skeptical of promises by leaders to do a better job policing each other's fiscal discipline. "I have heard this for 15 years," Mr. Krämer said. "I don't believe it. The E.U. is a consensus driven club. You can't force other countries to do this or that."

Jens Weidmann, president of the German Bundesbank and a member of the E.C.B. governing council, implicitly greeted the greater willingness by leaders to take more responsibility.

"It is decisive for monetary policy during this sovereign debt crisis that no further risk be transferred to the Eurosystem, and that the separation between monetary and financial policy not be further weakened," Mr. Weidmann said in a statement, referring to the network of European central banks.

But, in a sign that not all members of the governing council are happy with the agreement, Mr. Weidmann also criticized what he said was a major step toward collective responsibility for the mistakes of individual states.

"This weakens the fundament of a monetary union built on individual fiscal responsibility," Mr. Weidmann said in a statement. "In the future it will be even more difficult to maintain incentives for solid financial policy."

Europe must abandon the euro or go forth and integrate

EUROPE, FROM PAGE 12

There is, in principle, no need for a more fiscally and economically unified Europe to be more like Germany and less like Italy or Greece. But Germany is unlikely to accept less fiscal discipline, and for the rest of Europe to regain competitiveness while sticking with the euro would seem to leave those countries with little choice.

It is of course possible that the decisions being made in Brussels will be negated or watered down as the details are considered. But the failure of the earlier bailouts, and the obvious risk of contagion, have forced Europe to move toward consolidation to preserve the euro. Those pressures will be there even if politicians want to step back at a later date.

The positive market reaction on Thursday should also be kept in perspective. The yield on 10-year Italian bonds, which had risen to more than 6 percent in panicked trading Monday, fell below 5.4 percent on Thursday as word of the apparent agreement spread. But that is still higher than it was two weeks ago. Similarly, a 10-year Greek bond sold for more than 55 percent of its par value, up from less than 51 percent a few days ago. But it sold for nearly 75 percent of par value as recently as February.

A few weeks ago, the European Central Bank was unwilling to even consider allowing the admission that Greece would have to default. Germany was unwilling to agree to a bailou[illegible]h open-ended costs. Both backed down in the face of economic and market realities.

Those realities will continue to pressure Europeans toward either abandoning the currency union or accepting much more financial union. For now, anyway, they are choosing the latter course.

Leadership plan for military contractor could hinge on intimate video

PARIS

A billionaire's cuddling with his girlfriend raises eyebrows at EADS

BY NICOLA CLARK

Arnaud Lagardère, the French billionaire who has been widely expected to become the chairman of the European aerospace group EADS next year, became an unwitting Internet sensation this past week after a Belgian magazine released a video of him posing and cuddling with his young supermodel girlfriend.

Now some stunned executives within EADS, formally European Aeronautic Defense & Space, and its Airbus subsidiary are privately questioning whether Mr. Lagardère, the 50-year-old heir and chief executive of the Lagardère media-to-missiles empire, is the most suitable candidate to oversee the group.

"People are saying that it is not the image that someone of his stature should project," said one executive, who asked not to be identified by name because of the fears of reprisal.

The nearly three-minute video — more Fashion TV than the financial news network CNBC — has received more than half a million hits since it was posted on the YouTube video sharing site Wednesday. It was shot as Mr. Lagardère and Jade Foret, a 20-year-old fashion model, posed recently for photos to accompany a cover story in the weekend magazine of Le Soir, a Belgian newspaper. The footage shows Mr. Lagardère and Ms. Foret kissing and embracing as they discuss how they met and fell in love this year.

While the video is unlikely to ruffle many feathers within Mr. Lagardère's publishing business, which includes magazines like Elle and Paris Match, it has been viewed with consternation in the more buttoned-down world of aerospace and arms making.

And it has placed the Frenchman in the spotlight at a sensitive time for the board and key shareholders of EADS, who have come under pressure from management to create a new governance structure.

Louis Gallois, the EADS chief executive, said in June that he and other top group managers were pressing for a new arrangement that would allow any investor to buy or sell shares freely in the company, while still preserving the delicate balance of influence between France and Germany in its governance.

A shareholder pact that dates from the group's creation in 2000 stipulates that the French and German stakes in EADS must be equal.

Currently, Mr. Lagardère's company owns a 7.5 percent stake in EADS while the French government holds 15 percent. Meanwhile, Daimler, the German automaker, owns 15 percent and a consortium of German private- and public-sector banks holds 7.5 percent.

But both Daimler and Lagardère have made it clear in recent years that they do not view their EADS holdings as crucial to their operations, and the French and German governments have struggled to broker a sale of the shares to other investors in a way that would preserve the ownership balance.

A management restructuring arranged in 2007 with the help of Nicolas Sarkozy, the French president, and his German counterpart, Angela Merkel, placed Mr. Gallois, a Frenchman, at the helm of EADS and Thomas Enders, a German in charge of Airbus, the group's largest business unit, for five years.

The chairmanship of the group was awarded to a German under the proviso that Mr. Lagardère — also a close friend of Mr. Sarkozy — would take over that post in mid-2012.

YOUTUBE

A scene from a YouTube video of the billionaire Arnaud Lagardère and the model Jade Foret that has raised questions about his ability to lead the European arms maker EADS.

But in recent years, Mr. Lagardère, who holds a seat on the EADS board, has appeared increasingly disinterested in his company's aerospace assets. They are a legacy of his father, Jean-Luc, the former chief of Matra, a military contractor that was eventually merged in Airbus.

According to a number of top managers, Mr. Lagardère's attendance at EADS board meetings has been sporadic and often perfunctory.

Many in the French and German news media have reacted to the video with scorn. Both the German business daily Handelsblatt and the French newspaper Le Monde described it as "embarrassing" and "dis[illegible]ing," while Libération, another French daily, likened the video to a Brazilian soap opera.

Challenges, a French newsweekly, found it "stupefying."

"Maybe this video is the perfect excuse for him — and for the French government — to replace him with someone else," said one group executive, who asked not to be identified expressing his personal opinion.

Mr. Gallois, the EADS chief executive, told The Wall Street Journal as recently as last month that he expected the board would appoint Mr. Lagardère chairman next year. Alexander Reinhardt, an EADS spokesman, would not be drawn out when asked what implications, if any, could follow from the video controversy.

"It is not up to EADS to comment on this," Mr. Reinhardt said.

Ramzi Khiroun, a spokesman for Lagardère, did not return calls requesting comment.