

# INTERNATIONAL Herald Tribune

THE GLOBAL EDITION OF THE NEW YORK TIMES

THURSDAY, SEPTEMBER 18, 2008

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## Anger and anxiety grow in milk scandal

### Traces of contaminant widely found

By Jim Yardley

**BEIJING:** At Children's Hospital on the east side of Beijing, harried nurses spent Wednesday behind a small wooden desk, registering infants in a rapidly filling logbook. Anxious parents, fearing they might have unwittingly fed their infants with tainted baby formula, waited for hours to determine if their babies had suffered health problems.

One father, Zhang Gaofeng, 35, had spent more than a day at the hospital with his wife, Wang Hui, and their 22-month-old daughter, Yue. The couple had fed Yue the brand of Sanlu baby formula now at the center of a nationwide food safety scandal that has left three infants dead and more than 6,000 babies sickened. Zhang, a migrant worker, attributed the problems to corporate greed.

"They are trying to make a profit off the people who are not rich enough to afford the imported brands," he said as he waited in the hospital parking lot with other families. "Poor people can only afford the low-end products like this one."

The anxiety at Children's Hospital is just one snapshot of a scandal that has broadened in scope every day since it became public last week. On Wednesday, Health Minister Chen Zhu reported that more than 1,300 infants are hospitalized and that 158 babies have suffered acute kidney failure after being fed formula contaminated with the industrial additive melamine. And the State Council, China's cabinet, pledged an overhaul of the nation's dairy industry.

Melamine is used to produce plastics and fertilizers and is banned from use in food production. But in the past, the additive has sometimes been blended into agricultural products to raise protein levels — and profits. Milk producers who want to increase their milk supplies sometimes do so by adding water. But the diluted milk has lower nutrient levels, so melamine, high in nitrogen, is

added to artificially inflate those levels to meet protein requirements. Infants who drink the formula for sustained periods can develop kidney stones and suffer kidney failure.

Initially, the contamination problem was thought to be confined to baby formula produced by the Sanlu Group, one of the country's largest dairy companies. But investigators have since discovered traces of melamine in some batches of powdered formula produced by 21 other dairy companies, including China's biggest outfit, Mengniu Dairy.

Mengniu and other companies have recalled tainted products, even as government officials are promising to correct the problems so that big operators can resume and even expand production to meet demand.

"They can absolutely undergo a major overhaul in a short period of time," Li Changjiang, head of the General Administration of Quality Supervision, Inspection and Quarantine, said Wednesday during a news conference that was carried live on national television.

Any promise of a quick remedy might seem overly optimistic, given that China experienced a similar baby formula scandal in 2004. And last year, after a string of food and drug safety controversies, government officials promised to root out corruption and strengthen regulation of the food and drug industries. Now, a group of lawyers is organizing lawsuits on behalf of parents against dairy companies.

With anger rising, government officials tried to reassure the public by issuing a statement that "most" of China's baby formula is safe. The authorities have arrested four suspects, offered free medical care to ailing children and dispatched investigators across the country to inspect dairy operations.

Four officials in Hebei Province

CHINA, Continued on Page 8

## U.S. takes radical steps to save AIG



How Hwee Young/European Pressphoto Agency

Hundreds of customers in Singapore on Wednesday thronged a subsidiary of AIG, which the U.S. government rescued hours earlier.

**AIG's troubles and why they matter** American International Group is a giant insurance company that has provided \$440 billion of insurance to investors who bought securities backed by mortgages.

1 Banks wrote mortgages and sold them to investment banks. The investment banks packaged the mortgages into securities and sold them to investors.



2 To protect investors against defaults, AIG sold insurance on those securities. AIG put up collateral to guarantee it could repay investors, if needed.

3 The contracts said that if AIG's credit ratings were cut, it would have to provide additional collateral.

4 Credit rating agencies, concerned about the declining value of AIG's own investment portfolio, cut the company's credit ratings Monday, requiring the company to put up more collateral.

5 If AIG had failed to put up collateral, investors' holdings would have been at risk, perhaps leading to losses around the world.

CREDIT RATING AGENCY

## Across Asia, a sterling image dissolves

### Struggling insurer was revered by clients for prudence and reliability

By Martin Fackler and Heather Timmons

**TOKYO:** American International Group was one of the rare U.S. companies that moved into Asia early and successfully, turning itself or one of its many subsidiaries into household names from Kobe, Japan, to Calcutta.

Now, as AIG tries to pick up the pieces after its brush with bankruptcy, one of its biggest challenges may be trying to save what, until just a week ago, had been one of the most venerated American business franchises in Asia.

While AIG may have dodged the bullet with the rescue Tuesday by the U.S. government, it could find Asian consumers less willing than the United States to give it a second chance. It might also be required to put some of its profitable Asian operations on the auction block to help pay off the government's \$85 billion loan.

For the insurance giant, founded in Shanghai in 1919 and with revenue of \$110 billion last year, losing parts of Asia would be like losing the crown jewels. Its former chairman, Maurice Greenberg, spent decades cultivating ties with Asian leaders and building AIG into the biggest foreign insurer in Japan and China, the two richest markets in Asia. As the region's economy has taken off, it has quickly become one of the largest and fastest-growing markets for AIG, accounting for about 40 percent of its \$54 billion in life insurance premiums and retirement services last year.

In recent years, AIG benefited in particular from a reputation for prudence and reliability, which stood out in a region plagued by shoddy financial companies. So when news broke that the company faced bankruptcy, stunned and irate customers

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## Economy the focus in U.S. campaigning

Senator John McCain and Senator Barack Obama have quickly moved to emphasize the economy — and their grasp of its importance — in their speeches and campaign advertisements. McCain, in particular, had to scramble. **Page 4**

**CLEANING UP** Not much has been done to deal with problems that caused the crisis. **Page 14**

**LEHMAN DEAL** Barclays is ready to buy Lehman's core capital markets businesses. **Page 14**

**INJECTIONS OF CASH** Three Asian nations pumped \$33 billion into money markets. **Page 14**

## The Fed extends \$85 billion bailout, hoping to soothe global markets

By Edmund L. Andrews, Michael J. de la Merced and Mary Williams Walsh

**WASHINGTON:** Acting to counter fears of a worldwide financial crisis, the U.S. Federal Reserve has reversed course and agreed to an \$85 billion bailout that would give the U.S. government control of the troubled insurance giant American International Group.

The decision is the most radical intervention in private business in the central bank's history and came only two weeks after the Treasury took over the federally chartered mortgage finance companies Fannie Mae and Freddie Mac and six months after the Fed provided \$29 billion in guarantees to bail out the investment bank Bear Stearns.

Investors and policy makers across the globe appeared doubtful Wednesday that this latest dramatic rescue of a U.S. financial giant signaled an end to the credit crisis ravaging markets for the past year.

Japan, Australia and India pumped \$33 billion into money markets on Wednesday as lending between banks seized up. An early stock market rally in Asia lost steam as worrying resumed. Shares in Europe were mainly higher midday, but Russia halted trading after a steep fall in share prices there.

"The root causes of the problem such as continued falls in housing prices will likely continue," the Bank of Japan's governor, Masaaki Shirakawa, was quoted by Reuters as saying. "It is hard to determine when U.S. financial institutions will dispose of their losses."

The U.S. government's move to rescue AIG has started a debate in the U.S. presidential campaign over who is to blame for the financial crisis that prompted the latest rescue, which effectively puts U.S. taxpayer money at risk while protecting bad investments made by AIG — which operates in 130 countries — and other institutions it does business with.

The speaker of the House of Representatives, Nancy Pelosi, Democrat of California, quickly criticized the bailout, calling the \$85 billion a "staggering sum" that was "just too enormous for the American people to guarantee."

With time running out after AIG failed to get a bank loan to avoid bankruptcy, President George W. Bush received a briefing on the rescue plan Tuesday afternoon. The secretary of the Treasury, Henry Paulson Jr., and the chairman of the Federal Reserve, Ben Bernanke, then convened a meeting with House and Senate leaders on Capitol Hill about 6:30 p.m. to explain it.

They emerged just after 7:30 p.m., with Paulson and Bernanke looking grim. The bailout was announced at 9 p.m. Tuesday in Washington, during the business morning Wednesday in Asia.

The decision was a remarkable turn-

AIG, Continued on Page 15



Yemen News Agency, via Reuters

## U.S. Embassy attacked in Yemen

Smoke billowing from the embassy in Sana after a suicide car bomb exploded outside Wednesday. At least 16 people were killed, including 6 attackers. **Page 5**

## A new Thai leader, but protests go on

Somchai Wongsawat, a brother-in-law of the ousted leader Thaksin Shinawatra was elected prime minister of Thailand on Wednesday, drawing an angry response from protesters who say the government remains a puppet of Thaksin. **Page 3**

## Top Israeli party picks leader

Polls indicated that the favorite is the foreign minister, Tzipi Livni, who says her goal is to charge ahead on peace talks. **Page 8**

## Blind masseurs' court battle

A South Korean court will rule on a law that allows only the visually impaired to become professional masseurs. **Page 2**

## FASHION

A special report

## From the Stone Age to the space age

Inspired by the prehistoric ("Planet of the Apes") to the futuristic (Pac-Man), the designers Christopher Kane, Giles Deacon and Eley Kishimoto brought energy

and fun to the London catwalk, Suzy Menkes writes. A spring/summer

2009 dress by Kane, left, was created from a series of orange fabric circles. **Page 19**

Chris Moore/Karl Prouse

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OIL New York, Wednesday, noon	
Light sweet crude	\$92.48 ▼ \$0.25
STOCK INDEXES Wednesday	
The Dow noon	10,759.64 ▼ 2.71%
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Nikkei 225 close	11,749.79 ▲ 1.21%

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## New U.S. agency proposed to handle toxic securities

By Stephen Labaton

**WASHINGTON:** As the administration of President George W. Bush has lurched from pillar to post in the financial crisis, some lawmakers and experts are considering a longer-term legislative solution that would create a new agency to dispose of the mortgage-related assets at the core of Wall Street's woes.

Proponents of a more systematic government role to help relieve financial institutions of their toxic securities range from Lawrence Summers, a former Treasury secretary in the Clinton administration, to two former Federal Reserve chairmen, Paul Volcker and Alan Greenspan.

In Congress, the idea gaining traction centers on the creation of a new agency that would purchase troubled assets from hobbled companies.

The idea was floated Tuesday by Representative Barney Frank, Democrat of Massachusetts, who heads the Financial Services Committee of the House of Representatives. Among those signaling that it merited serious consideration were Senate Majority Leader Harry Reid and the House speaker, Nancy Pelosi.

With seven weeks until the U.S. presidential election, no one expects Congress or the White House to move

quickly to create a new federal agency that puts taxpayers at risk for hundreds of billions of dollars in bad assets.

Representative Steny Hoyer, the House majority leader, said there was no time to consider any new proposals in the two weeks remaining before Congress adjourns.

But in its ad hoc approach to the crisis, the Treasury and the Federal Reserve have, in effect, already embarked on a course similar to the proposals in Congress.

In the case of Bear Stearns, the Fed took \$29 billion of the investment bank's mortgage-related assets as collateral for a Fed loan to JPMorgan Chase, which then agreed to acquire Bear Stearns. In the case of Fannie Mae and Freddie Mac, the Treasury Department placed the companies in a conservatorship and explicitly backed the \$5.3 trillion of mortgages they own or guarantee.

The Treasury also agreed to buy an unspecified amount of Fannie's and Freddie's mortgage-backed securities on the open market, starting with a \$5 billion purchase this month. Those securities are to be managed and ultimately sold for the government by an investment house on Wall Street.

But government officials remain

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