

"All the News
That's Fit to Print"

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Arizona: A few high clouds in the northern highlands, otherwise sunny. Highs 65-72 in Phoenix, Tucson and nearby deserts, 50s in northern highlands. Weather map, Page A2

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MOISES SAMAN FOR THE NEW YORK TIMES

ISRAELI BREATHER Israeli soldiers rested Wednesday in the Gaza campaign as officials braced to discuss cease-fire terms. Page A12.

Gaza War Role Is Political Lift For Ex-Premier

By ETHAN BRONNER

JERUSALEM — A few weeks ago, Defense Minister Ehud Barak was considered a dead man walking in Israeli politics. Members of his Labor Party were plotting to replace him after elections on Feb. 10, if not before. Under his leadership, the storied party of David Ben-Gurion and Golda Meir had sunk so low in the polls that there was serious talk it might disappear.

No one is talking like that now. Twelve days into a punishing war that he is leading against Hamas in Gaza, Labor's poll numbers are spiking. Mr. Barak is everywhere, in sunglasses and leather jacket, striding among his military commanders, talking strategy, calculating the next move.

"The respect I get when I go into schools since the war is amazing, and it is all about Barak," remarked Daniel Ben-Simon, a Labor Party candidate for Parliament. "Israel's MacArthur is back."

There is, however, much irony — and uncertainty — in this political upheaval. Although Mr. Barak has gained from the war, he was opposed to it for far longer than any of the other top leaders and has been the most eager of them for a cease-fire since it began. Many abroad recall Mr. Barak as the prime minister who in 2000 went further than any Israeli leader in peace offers to the Palestinians, only to see the deal fail and explode in a violent Palestinian uprising that drove him from power.

If the current war goes on for long and kills many young Israeli men on the battlefield — so far casualties have been few and his shock-and-awe approach of the first days has been widely admired in Israel — Mr. Barak's gains may again disappear. But

Purple Heart Is Ruled Out for Traumatic Stress

By LIZETTE ALVAREZ
and ERIK ECKHOLM

The Pentagon has decided that it will not award the Purple Heart, the hallowed medal given to those wounded or killed by enemy action, to war veterans who suffer from post-traumatic stress disorder because it is not a physical wound.

The decision, made public on Tuesday, for now ends the hope of Iraq and Afghanistan veterans who have the condition and had hoped that the Purple Hearts could honor their sacrifice and help remove some of the stigma associated with the condition.

The disorder, which may go unrecognized for months or years, can include recurring nightmares, uncontrolled rage and, sometimes, severe depression and suicide. Soldiers grappling with P.T.S.D. are often unable to hold down jobs.

In May, Defense Secretary Robert Gates said awarding Purple Hearts to such service members was "clearly something that needs to be looked at" after he toured a mental health center at Fort Bliss, Tex.

But a Pentagon advisory group decided against the award because, it said, the condition had not been intentionally caused by enemy action, like a bomb or bullet,

and because it remained difficult to diagnose and quantify.

"Historically, the Purple Heart has never been awarded for mental disorders or psychological conditions resulting from witnessing or experiencing traumatic combat events," Eileen Lainez, a Pentagon spokeswoman, said. "Current medical knowledge and technologies do not establish PTSD as objectively and routinely as would be required for this award at this time."

One in five service members, or at least 300,000, suffer from post-traumatic stress disorder or major depression, according to a

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ERIK S. LESSER FOR THE NEW YORK TIMES

Fred Milani, an Atlanta builder, says it is time to move out of the house he built seven years ago.

ATLANTA JOURNAL

Hard Times Find This White House Up for Sale

By ROBBIE BROWNE

most as long as President Bush has been in Washington, Mr. Milani, an Iranian-American home

said. "But I will."

Last month, Mr. Milani, 57, placed his house, in the North

China Losing Taste for Debt From the U.S.

Key Lender Finds Uses
for Money at Home

By KEITH BRADSHAW

HONG KONG — China has bought more than \$1 trillion of American debt, but as the global downturn has intensified, Beijing is starting to keep more of its money at home, a move that could have painful effects for American borrowers.

The declining Chinese appetite for United States debt, apparent in a series of hints from Chinese policy makers over the last two weeks, with official statistics due for release in the next few days, comes at an inconvenient time.

On Tuesday, President-elect Barack Obama predicted the possibility of trillion-dollar deficits "for years to come," even after an \$800 billion stimulus package. Normally, China would be the most avid taker of the debt required to pay for those deficits, mainly short-term Treasuries, which are government i.o.u.'s.

In the last five years, China has spent as much as one-seventh of its entire economic output buying foreign debt, mostly American. In September, it surpassed Japan as the largest overseas holder of Treasuries.

But now Beijing is seeking to pay for its own \$600 billion stimulus — just as tax revenue is falling sharply as the Chinese economy slows. Regulators have ordered banks to lend more money to small and medium-size enterprises, many of which are struggling with lower exports, and to local governments to build new roads and other projects.

"All the key drivers of China's Treasury purchases are disappearing — there's a waning appetite for dollars and a waning appetite for Treasuries, and that complicates the outlook for interest rates," said Ben Simpford, an economist in the Hong Kong office of the Royal Bank of Scotland.

Fitch Ratings, the credit rating agency, forecasts that China's foreign reserves will increase by \$177 billion this year — a large number, but down sharply from an estimated \$415 billion last year.

China's voracious demand for

Continued on Page A10

OBAMA PROMISES BID TO OVERHAUL RETIREE SPENDING

HUGE DEFICITS LOOMING

Potential for Risky Fight
Over Social Security
and Medicare

By JEFF ZELENY
and JOHN HARWOOD

WASHINGTON — President-elect Barack Obama said Wednesday that overhauling Social Security and Medicare would be "a central part" of his administration's efforts to contain federal spending, signaling for the first time that he would wade into the thorny politics of entitlement programs.

As the Congressional Budget Office projected a record \$1.2 trillion budget deficit for this year, even before the costs of the nearly \$800 billion economic stimulus package being taken up by the House and the Senate, Mr. Obama stepped up his effort to reassure lawmakers and the financial markets that he plans a vigorous effort to keep the government's finances from deteriorating further.

Speaking at a news conference in Washington, he provided no details of his approach to rein in Social Security and Medicare, which are projected to consume a growing share of government spending as the baby boom generation ages into retirement over the next two decades. But he said he would have more to say about the issue when he unveiled a budget next month.

Should he follow through with a serious effort to cut back the rates of growth of the two programs, he would be opening up a potentially risky battle that neither party has shown much stomach for. The programs have proved almost sacrosanct in political terms, even as they threaten to grow so large as to be unsustainable in the long run. President

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Shift on Security Posts

Barack Obama is expected to scrap the way President Bush oversaw domestic security in the White House. Page A18.

Survival Lesson in Pittsburgh: Shedding an Industrial Past

By DAVID STREITFELD

PITTSBURGH — This is what life in one American city looks like after an industrial collapse:

Unemployment here is 5.5 percent, far below the national average. While housing prices sank nearly everywhere in the last year, they rose here. Wages are also up. Foreclosures are comparatively uncommon.

A generation ago, the steel industry that built Pittsburgh and still dominated its economy entered its death throes. In the early 1980s, the city was being talked about the way Detroit is now. Its



Light Security Across Iraq on a Holy Day for Shiites

By SAM DAGHER

Baghdad — Millions of Iraqis celebrated one of the most important occasions in their religious calendar Wednesday, accompanied by stringent security measures that included a ban on anyone entering the area around Baghdad's holiest shrines after a series of suicide bombings.

They also heard a call from the American Shiite cleric Mokhammad al-Sadr, who is believed to have been killed in Iraq during the war. He urged Iraqis to carry out attacks against American forces in revenge for Israel's military campaign in Gaza.

Ashura, the 10th day of the Islamic month of Muharram, marks the death of Prophet Muhammad's grandson Imam Hussein and his rebellious companions in the year 680 in battle in Karbala against the army of the Umayyad caliph Yazid. Imam Hussein's shrine, which embodies the divide between the Sunni and Shiite sects of Islam, continues to play a central role in defining Shiite identity.

The largest Ashura gathering takes place in the city of Karbala, about 100 miles from Baghdad, where Imam Hussein is entombed within a magnificent golden-domed shrine. On Wednesday, hundreds of thousands of men and women gathered the area around the shrine, beating their chests and heads in mourning. Some men and boys expressed even

greater fervor in more extreme rituals, beating themselves with chains and cutting their scalps and letting the blood flow.

In one of the most spectacular rituals, the Twarj run, thousands dashed two miles to the shrine from an area outside the city center, to symbolize their rush to heed Imam Hussein's last cries for help in battle.

Shiite religious festivals and shrines in Iraq have been the targets of some of the bloodiest attacks of the war. To ward off attacks in Karbala, 28,000 Iraqi soldiers and policemen have been on high alert for days, according to Maj. Gen. Othman al-Ghanemi, who commands operations there. Vehicle traffic was banned for miles from the shrine, and those approaching on foot were subjected to eight separate security checks.

In Najaf, nearly 20,000 security force members were mobilized, while Baghdad's streets were largely deserted as 30,000 soldiers and policemen fanned out.

In the impoverished neighborhood of Shuwader in Sadr City, Ashura was marked with a pageantry-filled play known as Shabih-e-Elam, which recreates the battle of Karbala.

Hundreds of men and women swarmed into a soccer stadium to watch the narrated spectacle, which was sponsored by Mr. Sadr's movement. Fluttering green banners, two camels and women shrouded in black symbolized Imam Hussein's camp. According to Islamic history, Imam Hussein had set out from Mecca with a small band of relatives and companions to the city of Kufa, where he had been promised support in his rebellion against the caliph, who was regarded as a usurper of legitimate Islamic rule.

But the imam was intercepted near Karbala by a force of several thousand men loyal to the Sunni caliph. Despite the overwhelming odds, the imam and his people decided to stand and fight.

To wails from the audience, the battle ends with the dramatic and slow death of Imam Hussein.

"Hussein is a symbol of rebellion against oppression and tyranny," said Salem al-Lu'ibi, the play's assistant director. "We are living under the same conditions in Iraq today. Nothing has improved. Death is everywhere."

China, a Key Lender, Loses Its Taste for U.S. Debt

From Page A1.

American bonds has helped keep interest rates low for borrowers ranging from the federal government to home buyers. Reduced Chinese enthusiasm for buying American bonds will reduce this dampening effect.

For now, of course, there seems to be no shortage of buyers for Treasury bonds and other debt instruments as investors flee global economic uncertainty for the stability of United States government debt. This is why Treasury yields have plummeted to record lows. (The more investors want notes and bonds, the lower the yield, and short-term rates are close to zero.) The long-term effects of China's using its money to increase its people's standard of living, and the United States' becoming less dependent on one lender, could even be positive. But that rebalancing must happen gradually to not hurt the value of American bonds or of China's huge holdings.

Another danger is that investors will demand higher returns for holding Treasury securities, which will put pressure on the United States government to increase the interest rates those securities pay. As those interest rates increase, they will put pressure on the interest rates that other borrowers pay.

When and how all that will happen is unknowable. What is clear

China's demand for American bonds has helped reduce rates for other borrowers.

now is that the impact of the global downturn on China's finances has been striking, and it is having an effect on what the Chinese government does with its money.

The central government's tax revenue soared 32 percent in 2007, as factories across China ran at full speed. But by November, government revenue had dropped 3 percent from a year earlier. That prompted Finance Minister Xie Xuren to warn on Monday that 2009 would be "a difficult fiscal year."

A senior central bank official,

Cai Qiusheng, mentioned just before Christmas that China's \$1.9 trillion foreign exchange reserves had actually begun to shrink. The reserves — mainly bonds issued by the Treasury, Fannie Mae and Freddie Mac — had for the most part been rising quickly ever since the Asian financial crisis in 1998.

The strength of the dollar against the euro in the fourth quarter of last year contributed to slower growth in China's foreign reserves, said Fan Gang, an academic adviser to China's central bank, at a conference in Beijing on Tuesday. The central bank keeps track of the total value of its reserves in dollars, so a weaker euro means that euro-denominated assets are worth less in dollars, decreasing the total value of the reserves.

But the pace of China's accumulation of reserves began slowing in the third quarter along with the slowing of the Chinese economy, and appeared to reflect much broader shifts.

China manages its reserves with considerable secrecy. But economists believe about 70 percent is denominated in dollars and most of the rest in euros.

China has bankrolled its huge reserves by effectively requiring the country's entire banking sector, which is state-controlled, to take nearly one-fifth of its deposits and hand them to the central bank. The central bank, in turn, has used the money to buy foreign bonds.

Now the central bank is rapidly reducing this requirement and pushing banks to lend more money in China instead.

At the same time, three new trends mean that fewer dollars are pouring into China — so the government has fewer dollars to buy American bonds.

The first, little-noticed trend is that the monthly pace of foreign direct investment in China has fallen by more than a third since the summer. Multinationals are hoarding their cash and cutting back on construction of new factories.

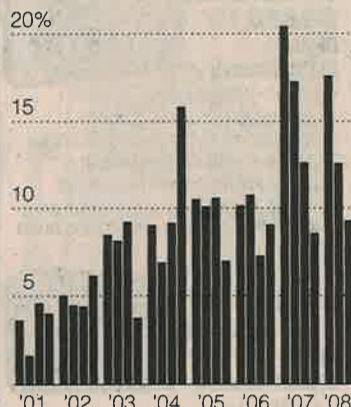
The second trend is that the combination of a housing bust and a two-thirds fall in the Chinese stock market over the last year has led many overseas investors — and even some Chinese — to begin quietly to move money out of the country, despite stringent currency controls.

So much Chinese money has

Buying Fewer Bonds

China has slowed its purchases of Treasury bonds, mortgage-backed securities and other overseas investments.

Percentage of Chinese G.D.P. spent on expanding foreign reserves



Sources: Calculated from data from National Bureau of Statistics and People's Bank of China, via CEIC Data THE NEW YORK TIMES

The nation's finance minister has warned of 'a difficult fiscal year.'

poured into Hong Kong, which has its own internationally convertible currency, that the territory announced Wednesday that it had issued a record \$16.6 billion worth of extra currency last month to meet demand.

A third trend that may further slow the flow of dollars into China is the reduction of its huge trade surpluses.

China's trade surplus set another record in November, \$40.1 billion. But because prices of Chinese imports like oil are starting to recover while demand remains weak for Chinese exports like consumer electronics, most economists expect China to run average trade surpluses this year of less than \$20 billion a month.

That would give China considerably less to spend abroad than the \$50 billion a month that it poured into international financial markets — mainly American bond markets — during the first half of 2008.

"The pace of foreign currency flows into China has to slow," and therefore the pace of China's re-

investment of that foreign currency in overseas bonds will also slow, said Dariusz Kowalczyk, the chief investment officer at SJS Markets Ltd., a Hong Kong securities firm.

Two officials of the People's Bank of China, the nation's central bank, said in separate interviews that the government still had enough money available to buy dollars to prevent China's currency, the yuan, from rising. A stronger yuan would make Chinese exports less competitive.

For a combination of financial and political reasons, the decline in China's purchases of dollar-denominated assets may be less steep than the overall decline in its purchases of foreign assets.

Many Chinese companies are keeping more of their dollar revenue overseas instead of bringing it home and converting it into yuan to deposit in Chinese banks.

Treasury data from Washington also suggests the Chinese government might be allocating a higher proportion of its foreign currency reserves to the dollar in recent weeks and less to the euro. The Treasury data suggests China is buying more Treasuries and fewer bonds from Fannie Mae or Freddie Mac, with a sharp increase in Treasuries in October.

But specialists in international money flows caution against relying too heavily on these statistics. The statistics mostly count bonds that the Chinese government has bought directly, and exclude purchases made through banks in London and Hong Kong; with the financial crisis weakening many banks, the Chinese government has a strong incentive to buy more of its bonds directly than in the past.

The overall pace of foreign reserve accumulation in China seems to have slowed so much that even if all the remaining purchases were Treasuries, the Chinese government's overall purchases of dollar-denominated assets will have fallen, economists said.

China's leadership is likely to avoid any complete halt to purchases of Treasuries for fear of appearing to be torpedoing American chances for an economic recovery at a vulnerable time, said Paul Tang, the chief economist at the Bank of East Asia here.

"This is a political decision," he said. "This is not purely an investment decision."

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