MarketWatch

Jan 15, 2009

US Stocks Slide On BofA Report; DJIA Dips Below 8000

By Peter A. McKay

U.S. stocks plunged and the Dow Jones Industrial Average fell below 8000 for the first time intraday since Nov. 21, amid fears the banking system may need yet another government rescue.

The biggest loser on the DJIA was Bank of America, off 21% after reportedly entering talks with the U.S. government about another round of assistance. Citigroup, which rushed into the sale of a controlling stake in its brokerage to raise capital, was off 15%.

"The size of the capital shortfall for the banks in the U.S. and for that matter Western Europe is larger than people were willing to believe a few months ago," said Daniel Alpert, a founder of boutique investment bank Westwood Capital. "At this level, I believe the market is saying: 'You know what, guys? You're insolvent; you're selling off the family jewels.'"

Alpert said there was a misapprehension on the stock market that, after writing down the value of residential mortgagebacked securities last year, the banks would return to bull market business as usual. Now, new losses are piling up from investments in commercial real estate, loans for failed leveraged buyouts, corporate bonds and equities.

"All we're doing is plugging holes," Alpert said. "When the government puts in money, it's just covering a bunch of losses. That's not helping the macroeconomy, it's just saving the institution."

The DJIA was recently down 176 points at 8025, on pace to post a seventh straight daily drop. Earlier, it fell more than 200 points to 7995.

JPMorgan shed 16 cents to $25.78 after posting a profit of 7 cents a share for the fourth quarter. Earnings fell 76% from a year ago and Chief Executive Jamie Dimon said loan demand "is dropping rather dramatically."

The last time the blue-chip measure finished below 8000 was Nov. 20, when several major indexes hit their lowest point during the latest bout of crisis on Wall Street. Many veteran traders and analysts believe the market is likely to test those levels again in the coming weeks, though there is some disagreement over whether the old lows will hold, considering the continuing flurry of fourth-quarter profit reports that is likely to contain more nasty surprises.

"A lot of sins were priced in at the lows," said portfolio manager Linda A. Duessel, of Federated Securities in Pittsburgh. She believes the market's November trough is likely to withstand the latest burst of selling, an outlook that has led her to advise clients to put some money to work in beaten-down sectors.

But, she adds: "We don't tell anyone to bet their whole wad. You have to peel back into this market, respecting all the problems that are still out there."

But some participants are more pessimistic. Unless the government steps in again to support the banking sector, the stock market closing lows Nov. 20 of 7552 on the DJIA and 752 on the Standard & Poor's 500 will likely be taken out in the foreseeable future, said Lorenzo Di Mattia, manager of hedge fund Sibilla Global Fund.

Bank of America is reportedly moving closer to getting billions of dollars more in aid to close its acquisition of Merrill Lynch. Analysts increasingly fear that the bank may need to take more steps to bolster its capital as it absorbs Merrill Lynch and its other large acquisition, mortgage giant Countrywide Financial.

"Even with help from the government, we think [Bank of America's] tangible equity levels are low relative to peers," analyst Stuart Plesser said. "It will need to cut its dividend and or raise equity capital in the coming months."

The losses for the big banks infected the broader financial sector, dragging down the stock market. The S&P 500 recently fell 19 points to 823, pulled down by a plunge of 6.4% in its financial sector, which is now down by more than 20% for the year just two full weeks into 2009.

The technology-focused Nasdaq Composite Index was down 20 points, trading at 1469, hurt by a 5% drop in Apple on worry about the health of Chief Executive Steve Jobs. Jobs said late Wednesday he would take a medical leave from the company.

Asian shares crumbled under heavy selling pressure after Wednesday's slide in U.S. markets, with resource and financial stocks hit the hardest. Japan's Nikkei lost 4.9%. Stocks in Europe crumpled as U.S. markets fell, with the U.K.'s FTSE 100 and Germany's DAX moving lower.

Commodity prices fell, hurting the energy and industrial sectors. As demand in economies worldwide seems to weaken with each data point, markets are pricing in a "deflationary" phase, where the prices of all assets decline, reducing incentive for investment and trade.

The Philadelphia Federal Reserve's employment index, based on a survey of factories in the area, showed its second weakest reading since 1968.

Crude-oil futures shed more than $2.80 to trade below $35 a barrel in New York. The broad Dow Jones-AIG Commodity Index fell about 1%.

Treasury prices were mixed. The two-year note slipped 2/32 to yield 0.750%. The 10-year note slipped 3/32 to yield 2.216%. But the 30-year bond rose 17/32 to yield 2.867%.

The dollar strengthened. One euro cost $1.3080, down from $1.3160 late Wednesday. As expected, the European Central Bank cut its main interest rate by half of a point. One dollar fetched Y89.555, up from Y89.06.