Panic grips global financial markets

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The financial crisis, used to justify the $700 billion Wall Street bailout approved by Congress and signed into law by President Bush on Friday, deepened dramatically Monday, as stock markets around the world registered massive losses in panic selling.

It was the biggest global stock market crash since "Black Monday," October 19, 1987, when exchanges around the world collapsed and the Dow Jones Industrial Average registered a loss of 22.6 percent, its largest ever single-day decline in percentage terms.

On Monday, Europe suffered its worst-ever one-day drop in share prices, with the pan-European Stoxx 600 index falling 7.6 percent. (See: "European stock markets in freefall following Paris financial summit"). Trading was halted either completely or partially in Iceland and Russia. The latter saw a 20 percent decline in share values.

European bank stocks suffered massive losses. Britain's HBOS dropped 19.8 percent, Lloyds lost 10.8 percent, the Royal Bank of Scotland plummeted by 20.5 percent, Switzerland's UBS fell 12 percent, Belgium's Dexia declined 20 percent, Germany's Commerzbank lost 12.5 percent, Deutsche Bank was off 8.4 percent, France's Societe Generale gave up 9.5 percent and Italy's UniCredit shares plunged 9 percent before trading in its stock was suspended.

Shares of European industrial firms were also hammered. EADS, the parent of Airbus, fell 7.5 percent, ArcelorMittal, the world's biggest steel maker, dropped 8.6 percent, German auto maker Daimler was down 5.8 percent and British Airways slid 10.3 percent.

The sense of panic was reflected in gallows humor, such as the quip from a senior trader at ETX Capital, who said, "Black Mondays used to be a once-in-a-lifetime event. Now they're coming along more regularly than a London bus."

Peter Dixon, a strategist at Commerzbank, said, "This is markets in pure panic mode. The financial system is seizing up…"

"The banking system doesn't work any more," said Robert Quinn, European stock analyst at Standard & Poor's. "It's just broken."

Share prices also fell heavily across Asia. China's benchmark Shanghai Composite Index dropped 5.2 percent, Hong Kong's Hang Seng Index fell 5 percent and Tokyo's Nikkei Stock Average declined 4.3 percent to its lowest level since February 2004. Benchmark indexes in Singapore, Seoul and Mumbai fell, respectively, 5.6 percent, 4.3 percent and 5.8 percent. Shares in Indonesia plunged 10 percent.

In South America, exchanges were shut down in Brazil and Peru because of massive selling.

The Toronto Stock Exchange's principal index fell more than 1,000 points, or 11 per cent, then recovered about half of its losses to close down by 573 points, or 5.3 percent.

In the US, panic selling at one point dropped the Dow by 800 points and brought the index below the 10,000 mark for the first time since 2004. By the end of trading, the market had recovered some of its losses, with the Dow closing with a 370 point (3.6 percent) loss. The Nasdaq Composite Index ended down 84 points (minus 4.3 percent) and the Standard & Poor's 500 Index closed down 42 points (minus 3.9 percent).

The losses added to declines on Friday, when all three indexes fell in the aftermath of the House of Representatives' vote approving the bailout plan for US banks drawn up by Treasury Secretary Henry Paulson. For all of last week, the Dow lost 7.4 percent, the Nasdaq fell 10.8 percent and the S&P 500 declined 9.4 percent.

The plunge on Wall Street came despite new steps by the Federal Reserve Board to unfreeze credit markets by flooding the banks with cheap loans. The Fed announced Monday that it would immediately double the amount of cash available to US banks under a so-called "auction facility" it launched last December. Under this program, the Fed extends low-cost credit to the banks and accepts as collateral virtually worthless assets such as mortgage-backed securities.

The Fed increased its credit line under the program from $150 billion to $300 billion, said it would soon raise that amount to $600 billion, and would bring the total of such loans to $900 billion by the end of the year.

The Fed also announced it would begin paying the banks interest on reserves they keep in the Federal Reserve system, another windfall that will eventually be paid with taxpayer funds. This change is one of the provisions, previously unreported in the media, contained in the bailout package signed into law on Friday.

Another is even more far-reaching. It authorizes the US Treasury to guarantee the Federal Reserve against any losses it incurs in pumping liquidity into the banking system. This could potentially cost US taxpayers hundreds of billions of dollars beyond the purported $700 billion cost of the bailout passed on Friday.

Paulson rushed to put in place the machinery to begin buying securities from the banks with public funds. The Treasury named a high-ranking official, Neel Kashkari, to head a new Office of Financial Stability and began soliciting for Wall Street asset managers to oversee the program.

Bush, attempting to calm the markets, made an appearance in Texas and said getting the bailout program up and running would "take time." This only heightened the panic in financial markets, which are facing a lockdown of virtually all forms of credit.

Notwithstanding the claims of the bailout's backers, particularly Democratic congressional leaders and presidential candidate Barack Obama, that the process would have "transparency" and "oversight" safeguards to prevent conflicts of interest, the appointment of Kashkari already points to a program rife with insider influence, self-dealing and corruption. Kashkari is a former executive at Goldman Sachs and worked under Paulson when Paulson was CEO of the Wall Street firm.

The global market panic has already demonstrated that the bailout, while covering the losses of the most powerful sections of the financial elite, will do little, if anything, to stem the deepening financial crisis and recession. The scale of worthless paper assets within the global banking system is so immense that the banks themselves have no confidence in the credit-worthiness of their counterparts and are refusing to lend.

Monday's sell-off was precipitated by a number of factors. The US jobless report issued Friday showed a large increase in the net job loss in September, increasing fears of a deep and protracted recession. A series of bank failures destabilized the entire banking system in Europe. And the European financial summit held Saturday produced no coordinated plan to head off more bank failures.

All of the financial indices on Monday pointed to a general collapse of confidence in the world credit system, which is increasingly undermining the broader economy. Oil prices continued to fall sharply, gold futures soared, yields on US government bonds fell to nearly zero and inter-bank lending rates rose even higher.

The Conference Board in the US reported that its employment trends index fell 0.8 percent in September, leaving it almost 10 percent below the level a year ago. Many economists are now predicting that unemployment in the US will rise sharply, exceeding 7 percent in early 2009.

The investment bank Morgan Stanley warned: "The recession now threatens to go global, with industrial economies on the brink, and trade and financial shocks threatening the developing world."