

NEWS RELEASE

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US STOCKS DROP AS BANK DEVELOPMENTS WEIGH

By PETER A. MCKAY - MarketWatch

Stocks tumbled as more losses and upheaval in the banking sector and dire trade and retail data hinted at an economy at risk of a deflationary spiral.

The Dow Jones Industrial Average, which was already on a five-day losing streak coming into Wednesday's action, recently shed another 266 points, trading 3.2% lower, at 8182.46, hurt by declines in all 30 of its components. The blue-chip measure has fallen about 830 points since the start of its recent losing streak and is about 630 points from its late-November low set as Wall Street's lending mechanisms froze up.

"People always take more risk than they should earlier than they should in search for extra yield and that has come back to roost," said Julius Ridgway, an investment advisor with Medley & Brown.

A series of developments on Wednesday underscored that the financial industry's woes are still not in the rearview mirror. Dow component Citigroup plunged 20% after saying it would sell the majority stake in its brokerage unit for \$2.7 billion to Morgan Stanley. The move is part of what will likely be a broader dismantling of the "financial supermarket" model that has long defined Citi's business strategy.

The banking sector was also hit by a warning from Deutsche Bank that it would post a fourth-quarter loss of about \$6.33 billion. Morgan Stanley analysts said HSBC may have to raise as much as \$30 billion and slice its dividend in half. The losses for Deutsche Bank and HSBC, whose shares fell about 9% and 7% respectively, hit stocks in Europe, setting a downbeat tone that has carried into the U.S. session.

Traders also continued to fret over when the government will release the second phase of its promised \$700 billion in aid to troubled banks, whether lawmakers will approve additional bailout funds as recommended by Federal Reserve Chairman Ben Bernanke, and what conditions might be attached, including possible restrictions on dealmaking.

"There's still a lot we don't know for sure at this point, but we know a few things that are likely - reduced dividends, lack of [mergers and acquisitions], and continued declines in earnings," said Peter McCorry of Keefe, Bruyette & Woods. "None of that is supportive of share prices."

The S&P 500 fell 3.4% to trade near 840. All its sectors traded lower, led by a nearly 6% drop in financials. Insurers also contributed to the category's weakness. Lincoln National fell 12.1%, Prudential Financial fell 9.4%, and Hartford Financial Services Group was down 9.1%.

Among the S&P's other sectors, major decliners included energy, down 4.5%; industrials, down 3.5%; and basic materials, down 3.3%. Bunge, one of the world's largest processors of soybeans, fell almost 13% after lowering its profit forecast, citing lower global demand for its products due to the worldwide economic slowdown.

Competitor Archer Daniels Midland was off nearly 12% in recent action.

In economic news, the Commerce Department said U.S. retail sales

fell 2.7% in December, worse than an expected 1.2% decline. Such a pullback bodes ill for the broader U.S. economy, which has already been in recession for more than a year and leans heavily on consumer spending as a contributor to overall growth.

Strategist Denis Amato, of Ancora Advisors in Cleveland, said weak spending remains a major threat, although his firm has also been cautiously "nibbling" at beaten-down names in the basic-materials sector and elsewhere looking for a safeguard against a possible pop in prices of goods and services throughout the economy if the government's recent bailouts and interest-rate cuts prompt too sudden a rebound in activity, perhaps later this year.

"One of the risks right now is that you don't know which is the greater threat to our standard of living - a continued economic decline or inflation," said Mr. Amato. "In order not to get inflation, it will take a lot of discipline on the government's part to pull back all its stimulus as it becomes apparent that it's accomplished its job. But, politically, that could be hard to do."

On Wednesday, evidence of a slowdown in commercial activity also showed up in trade numbers that showed exports and imports in the U.S. slowing sharply from July to November. Among commodities and industrial stocks, aluminum maker Alcoa and General Electric fell more than 5% each.

Many retail chains have pared their guidance in recent weeks, with the latest being jewelry retailer Tiffany, which again reduced its fiscal-year outlook after holiday sales slumped. Executives expect the tough sledding to continue well into 2009. Tiffany shares were off more than 1%.

And, in a worrisome development for the telecommunications sector, Nortel Networks filed for bankruptcy protection, citing a need to put itself "on a sound financial footing once and for all." Its shares fell nearly 75% in the U.S. before being halted.

The tech-oriented Nasdaq Composite Index fell 3.1% to 1498.87. The smallstock focused Russell 2000 was off 3.4%, trading at 457.87.

Commodity prices fell. Crude oil was off \$1.29, trading at \$36.49 a barrel in New York. Gold contracts fell \$7.10 to 813.60 per ounce. The broad Dow Jones-AIG Index was down almost 2%.

Treasury prices climbed as investors sought safe havens. The two-year note was up 1/32 to yield 0.734%. The 10-year note climbed 30/32 to yield 2.198%. The 30-year bond rose 2-6/32 to yield 2.904%.

The dollar was mixed against major rivals. One euro cost \$1.377, down from \$1.3190 late Tuesday. One dollar fetched 89.11 Japanese yen, down from 89.13 yen.