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Markets slide into correction; Europe worries cloud recovery

Europe's debt, increase in unemployment cited

By Kathleen Gallagher of the Journal Sentinel

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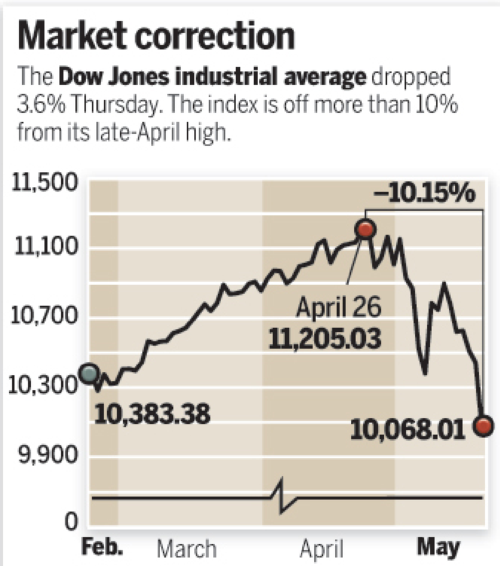

Source: Bloomberg News Journal Sentinel

As major stock indexes plunged Thursday into what market followers call a correction, nervous investors were left to wonder whether much worse was yet to come.

Investment strategist Clare Zempel doesn't think so.

"This is much more likely to be a correction rather than a sustained bear market," said Zempel, principal at investment research firm Zempel Strategic in Fox Point.

His reasoning: Long-lasting market declines typically start when stocks are extremely overvalued. Stock prices had gotten nowhere near that point, Zempel said.

In addition, he noted, interest rates are falling, the Federal Reserve has no plans to raise them, and there's positive economic momentum.

Still, worries over whether the problems of debt-ridden countries in Europe could spill over into the rest of the world continue to tug at global financial markets, which have been extremely jittery lately. Aggravating the situation Thursday was a weekly report from the U.S. Labor Department that new claims for unemployment benefits rose by 25,000 to 471,000, the largest amount in three months and a surprise to analysts who had expected a slight drop.

The Dow Jones industrial average fell 376 points, its biggest one-day point drop since February 2009, and all the major indexes were down well over 3%. All 30 Dow stocks fell, while 497 of the stocks in the Standard & Poor's 500 index closed lower.

Local companies that got hit hard in the decline included Rockwell Automation Inc., which lost $4.54, or 8%, to close at $52.16, and Manpower Inc., down $4.15, or 8.6%, to $44.03.

It's the first market correction - defined as a drop of 10% or more from a recent high - since stock indexes hit 12-year lows in March 2009, and it took less than a month to happen.

The S&P 500, one of the most-used indicators of stock market performance, is down almost 12% from its 2010 closing high of 1217.28, reached April 23. The Dow is off 10.15% from its 2010 closing high of 11,205.03, which it hit on April 26.

Rioting in the streets of Athens and the dramatic recent slide in the euro, the currency shared by 16 European nations, have spooked market participants, particularly those who are short-term traders rather than long-term investors, said Maureen Busby Oster, chief investment officer of Milwaukee-based Cleary Gull Holdings Inc.

Greece has become a symbol of the bigger fiscal problems faced by a number of Mediterranean countries and Ireland, Oster said. But Europeans overall don't have the amount of personal debt Americans do, and the euro-dollar relationship is at about its average level for the past 10 years, she said.

Oster said she believes the market is in a long trading range like the one that occurred from 1968 to 1982 - a range she said she's "reasonably confident" will continue for some time.

Joe Frohna, founding principal and portfolio manager at 1492 Capital Management LLC in Milwaukee, said he would be much more worried about the recovery if China or other parts of the developing world, such as Brazil, started faltering.

"When was the last time we looked to Europe as being a growth part of the world?" Frohna said.

Frohna, who invests mostly in small companies, also questioned the weakness in the government jobs numbers, saying they didn't jibe with what he had learned in meetings with hundreds of small companies in the past few months.

"Almost to a 'T' every one of them is saying they're hiring at least to the level they were at before the recession, so I'm really skeptical of this number, particularly with government hiring for the census," Frohna said.

Some others, however, took a dimmer view, worrying particularly that Europe's problems - and the efforts to resolve them - could ruin the global recovery.

"It's starting to look like one of these tragic stories where one person falls through the ice, then everyone else rushes in to help and ends up drowning," independent market analyst Edward Yardeni told The Associated Press.

Investors appear increasingly convinced that European countries will need to adopt stringent spending cuts to pay down their heavy debt loads, Yardeni said. Such cuts would likely lead to long economic slumps for those countries, a prospect that investors may now be accepting as reality as they sell stocks and the euro, he said.

The euro, a key indicator of confidence in Europe's economy, managed to rise to $1.2491 in afternoon trading Thursday, a day after hitting $1.2146, a four-year low. The euro began the year worth $1.4325.

"The drop in the euro is the initial phase of a long-term, multiyear economic decline in Europe," Yardeni said. "It shows a declining confidence in the workability of the EU (European Union) monetary union, and that's why their stock markets are down."

The Associated Press contributed to this report.