



Stocks tumble after government bailout of AIG

By TIM PARADIS, AP Business Writer

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Wall Street stumbled again Wednesday, with anxieties about the financial system still running high after the government bailed out insurer American International Group Inc. The Dow Jones industrial average dropped about 280 points.

The Federal Reserve is giving a two-year, \$85 billion loan to AIG in exchange for a nearly 80 percent stake in the company after it lost billions in the risky business of insuring against bond defaults. Wall Street had feared that the conglomerate, which has its tentacles in various financial services industries around the world, would follow the investment bank Lehman Brothers Holdings Inc. into bankruptcy. The ramifications of the world's largest insurer going under likely would have far surpassed the demise of Lehman.

"People are scared to death," said Bill Stone, chief investment strategist for PNC Wealth Management. "Who would have imagined that AIG would have gotten into this position?" He said the fear gripping the market reflects investors' concerns that AIG wasn't able to find a lifeline in the private sector and that Wall Street is now fretting about what other institutions could falter.

The two independent Wall Street investment banks left standing — Goldman Sachs Group Inc. and Morgan Stanley — remain under scrutiny, as does Washington Mutual Inc., the country's largest thrift bank. Morgan Stanley revealed its quarterly earnings early late Tuesday, posting a better-than-expected 7 percent slide in fiscal third-quarter profit. It insisted that it is surviving the credit crisis that has ravaged many of its peers.

Lehman filed for bankruptcy protection on Monday, and by late Tuesday had sold its North American investment banking and trading operations to Barclays, Britain's third-largest bank, for the bargain price of \$250 million. Over the weekend, Merrill Lynch, the world's largest brokerage, sold itself in a last-ditch effort to avoid failure to Bank of America Corp.

In early afternoon trading, the Dow fell 283.50, or 2.56 percent, to 10,775.52 after being down nearly 400 points. After a nosedive Monday the index is down more than 5 percent on the week, and has fallen more than 23 percent since reaching a record close of 14,164.53 on Oct. 9 last year.

Broader stock indicators also plunged. The Standard & Poor's 500 index dropped 37.26, or 3.07 percent, to 1,176.34, while the Nasdaq composite index fell 72.25, or 3.27 percent, to 2,135.65. The stock market is likely to see heavy back-and-forth movement as traders continue to assess the flood of news that has poured in over the past several days.

On Monday, the Dow lost 504 points, the largest tumble since its drop following the September 2001 terror attacks. On Tuesday, it rose 141 points, after the Fed decided to leave interest rates unchanged.

"It's still uncertain ground we're treading. We just have to move on a daily basis," said Jack A. Ablin, chief investment officer at Harris Private Bank.

The government took other measures Tuesday to help alleviate the turmoil in the markets. The Treasury said it will start selling bonds for the Fed to aid it with its lending efforts, while the Securities and Exchange Commission said it will strictly prohibit naked short-selling starting Thursday.

Short-selling is when traders borrow shares of a stock they expect to fall and sell them — if the stock does indeed fall, the traders buy the cheaper shares to cover the borrowed ones and profit from the difference. Naked short-selling occurs when sellers don't actually borrow the shares before selling them; it's a practice some say is partially responsible for the huge drop in the shares of investment banks like Lehman, Merrill Lynch and Bear Stearns Cos., which JPMorgan Chase & Co. bought earlier this year.

Bond prices wavered Wednesday. The yield on the benchmark 10-year Treasury note, which moves opposite its price, slipped to 3.40 percent from 3.43 percent late Tuesday. The dollar was lower against other major currencies.

Gold prices surged as nervous traders sought safe investments. Gold jumped \$64.50, or 8.25 percent, to \$845 an ounce on the New York Mercantile Exchange — the highest level since Aug. 29.

Crude oil rebounded \$1.87 to \$93.02 a barrel on the New York Mercantile Exchange. Crude dropped by about \$10 a barrel on Monday and Tuesday amid concerns that economic weakness will hurt demand.

Among financial names getting hit, Goldman Sachs fell \$31.98, or 24 percent, to \$101.03 and Morgan Stanley fell \$9.18, or 32 percent, to \$19.52.

"People are afraid of the unknown and they don't know what's on the books of these companies," said **Joe Saluzzi**, co-head of equity trading at **Themis Trading**. "The first reaction in a situation like this is to sell."

Saluzzi noted that surging gold prices and other measures of investors jitters indicate that fear is building.

"There is a lot more fear today than there was on Monday and Tuesday," he said. Indeed, the Chicago Board Options Exchange's volatility index, known as the VIX, and often referred to as the "fear index," jumped 8 percent Wednesday.

Saluzzi is somewhat optimistic that the nervousness could be nearing a crescendo, which could squeeze out more investors and then clear the way for a snapback rally.

But the woes of the financial sector could also exacerbate problems facing other parts of the economy, given that individuals and businesses rely on the nation's money centers.

The Commerce Department reported Wednesday that home construction fell by 6.2 percent in August to 895,000 units, the slowest pace since January 1991. Slumping demand for houses, sinking home prices and mortgage defaults have been the catalysts behind Wall Street's turmoil — and the risky mortgage-backed assets held by the nation's banks are not apt to regain in value until the housing market turns around.

Less than 200 stocks rose on the New York Stock Exchange, while nearly 3,000 fell. Volume on the exchange came to a heavy 913.6 million shares.

Overseas, Japan's Nikkei stock average rose 1.2 percent after AIG's rescue, but Hong Kong's Hang Seng index lost 3.6 percent. Britain's FTSE 100 fell 2.25 percent, Germany's DAX index fell 1.75 percent, and France's CAC-40 fell 2.14 percent.