

REUTERS

Wall St to struggle despite rescue plan

By Steven C Johnson in New York

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WALL Street's mood will likely remain dark next week as fallout from the credit crisis continues to corrode the US economy and questions linger about the likely effectiveness of the newly passed bailout plan in shoring up the financial system.

On Friday, Wall Street ended its worst week in seven years with another tumble on fears that the \$US700 billion (\$900 billion) financial rescue package may not unblock credit markets and stave off a US recession.

The plan will take bad mortgage debt off banks' hands so they can step up lending to households and businesses.

Aside from the bailout, the start of the corporate earnings season will vie for investor attention. Alcoa Inc will kick off the third-quarter company reports on Tuesday.

But corporate results aside, grim economic data -- topped by a government report showing the economy slashed 159,000 jobs in September in the biggest monthly decline in five and a half years -- confirms that the serious trouble on Wall Street has spread to Main Street.

What's more, lending should remain extremely tight. About the best investors can hope for, analysts said, is a very slow thaw in frozen credit markets, and even that's not a sure bet.

The cost for banks to borrow dollars over a three-month horizon shot up for a fifth straight day on Friday, signaling a widespread lack of confidence.

"The reality is that it's going to take months for credit markets to thaw out, and the stock market will remain very nervous because of the rapid deterioration in the economy," said Fred Dickson, director of retail research at D.A. Davidson & Co in Lake Oswego, Oregon.

And while they say a rescue was necessary, investors also contend it's far from sufficient to grease the gears of the banking system. For one thing, even though US President George W. Bush has signed the bill into law, the plan will take time to kick into action.

"We're still in the thick of this. It's like turning a cruise ship around -- you can't do it on a dime," said Joe Saluzzi, co-manager of trading at Themis Trading in Chatham, New Jersey.

There have been some hopeful signs of late. Markets reacted favorably to news that Wells Fargo, one of the strongest US banks left, had agreed to buy Wachovia, which holds a large portfolio of troubled mortgages -- without government help.

Peter Boockvar, equity strategist at Miller Tabak & Co, said banking sector consolidation should help surviving strong banks while also boost confidence and lending.

Hope that financial services stocks may be nearing a bottom also blossomed as Warren Buffett put \$US3 billion into economic bellwether General Electric this week, a move that comes shortly after his \$US5 billion investment in Goldman Sachs.

Recession fears, rate cut hopes

Still, all three major indexes -- the Dow, Nasdaq and benchmark S&P 500 -- remain down some 20 per cent on the year, and the economic picture continues to look grim.

For the week, the Dow ended down 7.3 per cent, the S&P slumped 9.4 per cent and Nasdaq tumbled 10.8 per cent.

The US economy has shed jobs in every month this year, while the housing market continues to struggle and manufacturing output has fallen sharply.

Recent data "are running well into recession territory," said John Praveen, chief investment strategist at Prudential International Investments Advisers in Newark, New Jersey.

"Even with the passage of the rescue plan, we will probably still have at least a shallow recession," he said. Michael Stahis, managing principal at Apex Venture Advisors in Dallas, said the government rescue "may loosen up overnight credit markets and improve things on a short-term basis."

"I think next week, early on, we're going to see a short-term upside rally, and if we do, you'll see more people go in," he added. "But I think that's just going to be a bear trap. Ultimately the market is going to go lower."

Mr Praveen said the economic and credit woes could prompt the Federal Reserve to cut interest rates from the current 2 per cent before its next scheduled meeting in late October. If the Fed moves in concert with the European Central Bank, which has seen euro-zone growth slow and lending dry up, he said that could help offset some of the bad news for stocks.

Another penitential drag on the market, though, looms with third-quarter earnings season, which begins to heat up next week, first with Alcoa, then Chevron on Thursday and General Electric on Friday.

"Earnings season is going to be dismal," said Hugh Johnson, chief investment officer of Johnson Illington Advisors in Albany, New York.

And while some stocks are starting to register as undervalued, he said the fear in the market is likely to keep a lot of investors sitting on their hands for a while yet.

"To step up to the plate in these markets, it takes a lot of courage and money," Mr Johnson said. "Warren Buffett's got that kind of courage and money, but not too many others."