Intel report sends stocks plunging around the world

Barry Gray
6 March 1998

When Intel Corporation, the world's largest producer of microprocessors, announced Wednesday after the closing bell on Wall Street that it was revising downward its projections for sales and profits, a palpable shudder ran through financial markets from one end of the globe to the other.

The price of Intel shares on the Nasdaq market in the US plunged more than 9 points, or 11 percent, in after-hours trading. Other major technology stocks tumbled as well.

The shock wave moved into Asia, where investors were already nervous over the impasse between the Suharto regime in Indonesia and the International Monetary Fund, doubts about the new South Korean government's ability to impose mass layoffs and austerity measures, and reports of serious problems at two of Malaysia's biggest banks.

On Thursday Tokyo's Nikkei Index fell 247 points, or 1.45 percent, with Japanese chip makers and other high-tech issues, such as Sony Corporation, leading the decline. The Heng Sang Index in Hong Kong slipped 547 points, or 4.8 percent. The markets in Seoul took a turn for the worse, with the stock market dropping 6.5 percent and the Korean won weakening by 2 percent. The All Ordinaries average in Australia registered a decline of 53 points, or 2 percent.

From Asia the sell-off moved to Europe. The Financial Times index in London dropped 37.5 points and stocks fell in Frankfurt by 86 points.

When the markets opened Thursday morning in the US the sell-off continued. At the end of the day the Dow Jones average was down 94 points, the Standard & Poor's 500 index was off by 12 points, and the technology-laden Nasdaq exchange had lost 2.7 percent of its value, falling 48 points.

The fact that Intel had lowered its projections by 10 percent, a substantial amount, was in itself alarming news for the big Wall Street investors, who have brushed aside concerns over the financial crisis in Asia and all but ignored repeated warnings from Federal Reserve Board Chairman Alan Greenspan that the bull market is headed for a sharp reversal. Indeed, stock prices have become so inflated that even the *Wall Street Journal* felt obliged to publish a cautionary article March 4 headlined "Stocks are in Stratosphere."

The article began with the question: "Have stock-market investors gone crazy?" It went on to explain that stocks in the Standard & Poor's 500-stock index are now trading at 26.1 times their operating earnings, up from a price/earnings ratio of 15.9 just three years ago.

Under these conditions, any indication of a slowdown in profit growth can quickly undermine investor confidence. But Intel's report was particularly alarming because the company attributed its downward trend to a fall in global demand for personal computers. Intel has been banking on a growth in the under-$1,000 PC market to sustain its sales and profits. But instead, it finds demand slumping. This is not, moreover, in the East Asian countries where such a turn of events is to be expected, but in the major markets of the US, Europe and Japan. Indeed, the biggest decline was in the US itself.

Company officials spoke as though they were stunned by their own report. Intel's problems "became apparent literally in the last few days," said spokesman Howard High. "I don't think we [understand] it completely."

In fact, Intel's report is only the most dramatic in a series of developments which point to a significant slowdown in corporate profits, particularly in the high-tech sector that has played such a central role in the stock bonanza of the 1990s. IBM was among the first to issue a warning about the first quarter of 1998, noting in January that its profits would be below the level of a year earlier, in large part because of the events in Asia.

But the profit slowdown is more general. Last month sneaker giant Nike said weakness in Asian markets and glutted markets in the US and Japan would push profits below expectations and precipitate the biggest layoffs in its 30-year history.

The impact of saturated markets, exacerbated by the collapse of the East Asian economies, is beginning to be felt in virtually every sector, from high-tech to clothing to automobiles. *BusinessWeek* has published a feature on the collapse of car sales throughout East Asia, where units sold have declined by 51 percent in Thailand and Malaysia, 49 percent in Indonesia, and 16 percent in South Korea. In Japan auto sales have dropped by 22 percent since last year.

Notwithstanding the continued exuberance, at least up until now, on Wall Street, these trends are beginning to seriously affect US-based corporations. The estimated annual earnings growth for companies listed in the S&P 500-stock index has dropped to 4 percent from 10 percent at the beginning of the year, the largest such drop since at least 1992.

Thus the reaction to Intel's announcement reflects well-grounded fears that what is emerging is a crisis of capitalist overproduction, which could lead to a deflationary spiral of historic proportions. The Industrial Bank of Japan released a report this week warning of such a danger. It said an influx of cheap Asian imports from countries whose currencies have virtually collapsed has driven down average import prices by 8 percent. In another report, the chief economist at Sanwa Bank warned, "There's even the possibility this will become the biggest bout of deflation since the end of World War II."

In a recent interview Japan's Vice Minister of Finance for International Affairs, Eisuke Sakakibara, suggested that the capitalist powers were in need of a new world financial structure to replace the Bretton Woods system of the post-World War II period. Insisting that the current crisis is global in character, and not simply an Asian problem, he bluntly stated a basic truth: "This just shows how unstable current world capitalism is."