Global markets plunge on US data and European bank fears

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Global stock markets plunged once again Thursday after bad US economic figures compounded new fears of a banking crisis in Europe. The renewed turbulence underscored the disastrous impact of the austerity measures being implemented in Europe and the United States.

In the United States, the Dow Jones Industrial average fell 3.68 percent, the NASDAQ fell 5.22 percent, and the S&P 500 fell 4.46 percent. This followed a similar sell-off in Europe, where the German DAX was down 5.82 percent and the British FTSE fell 4.49 percent.

Investors fled to safe assets, sending the yield on 10-year US government debt below 2 percent Thursday for the first time on Federal Reserve records going back 49 years. Gold, meanwhile, hit a new record of $1,823.70 per ounce.

Stock markets started off the day with a panic in the wake of concerns over European banks, plunging after the release of disastrous US manufacturing, housing, and inflation data.

The Philadelphia Federal Reserve said Thursday that US manufacturing in the US mid-Atlantic region contracted at the sharpest rate since 2009, after the initial financial crash in 2008. Its index of general business conditions fell to -30.7 in August, from 3.2 in July. The index has never hit such a low level without the economy being officially in recession.

The National Association of Realtors also said Thursday that sales of existing homes fell 3.5 percent this month, reaching their lowest level for 2011. Existing home prices continued to tumble, with the median price down 4.4 percent from a year earlier.

Consumer prices, meanwhile, posted their largest monthly increase since March, the Labor Department said Thursday. Prices were up 0.5 percent in August from June after a fall of 0.2 percent from May to June. Rising prices are expected to eat away at consumers' purchasing power, further slowing the economy.

Weekly initial jobless claims meanwhile rose to 408,000 last week, from 399,000 the week before, significantly higher than economists had predicted.

The statistics follow disastrous figures on German economic growth released Tuesday, which showed that the German economy stalled in the second quarter, growing only 0.1 percent, compared to 1.3 percent in the first quarter.

More broadly, the European Union's statistics office reported the same day that the Eurozone's economy grew by only 0.2 percent in the second quarter, compared to a 0.8 percent growth in the first three months of the year.

The US economy has likewise slowed sharply this year, growing at a 1.3 percent rate in the second quarter, and 0.4 percent in the first quarter, amid a global economic slowdown.

Even before Thursday's disastrous US economic figures came out, investors were panicked by developments pointing to a significant weakening of the financial situation of the European banks.

The *Wall Street Journal* quoted an executive at a major European bank as saying that officials at the US Federal Reserve are "very concerned" about the stability of the European banks. The statement comes amid renewed fears that the European debt crisis is likely to spill over into the US banking system.

Investors were likewise panicked when the European Central Bank announced Wednesday that one bank had tapped its emergency dollar pipeline for $500 million. This was the first time that any bank had used the facility in six months.

This news triggered a stock sell-off in the European financial sector, with the French Bank Société Générale down 12 percent and Belgium's Dexia falling 14 percent. Industrial stocks were also hard hit, with Germany's largest steel manufacturers, ThyssenKrupp and Salzgitter, falling by 9.4 and 8.6 percent respectively.

The conditions leading to the sell-off were summarized Thursday by Morgan Stanley in its latest forecast for world economic growth. The bank slashed its growth outlook for 2011 from 4.2 percent to 3.9 percent.

Morgan Stanley said that budget cuts are significantly slowing down growth, while worsening credit conditions are creating a feedback loop of tightening credit.

The bank wrote, "Currently many banks cannot access term funding markets at reasonable rates." It added that, "As a result, commercial banks continue to tighten their credit conditions, albeit marginally, to both their corporate and retail clients. If these term funding stresses continue well into the fall, the risks are rising that a lack of credit availability could dent domestic demand growth further."

The disastrous effects of the austerity measures currently being implemented throughout the United States and Europe were meanwhile summed up by one French hedge fund manager, who told the *Financial Times*: "The simple truth the market is coming to terms with is that a big debt reduction is going to impair growth, which is going to make debt reduction take longer, which impairs growth and so on."

The latest stock sell-off underscores that the world economy is entering another downturn, fueled by worldwide austerity measures and the pervasive financial crisis.