Portugal banking crisis sparks global stock selloff

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Stocks plunged in Europe and the US Thursday amid a sell-off in the Portuguese banking sector, prompting fears of a resurgence of the European debt crisis.

Shares of Banco Espírito Santo, Portugal's largest bank, plunged by 17 percent Thursday, prompting a temporary suspension of trading in the stock. The bank's stock price has fallen by a third over the past week.

The selloff comes amidst growing concerns that the global stock market is massively overvalued, as years of zero-interest rate monetary policies by central banks have inflated stock prices out of all proportion with the underlying economic reality. "A stock market correction has been an ongoing concern and maybe this is the catalyst," Andrew Wilkinson, the chief market analyst at Interactive Brokers told the *Financial Times* .

The selloff has upended the relative quiescence of the European financial system in recent months, raising concerns of a reemergence of the financial and debt crisis that has been burning at various levels of intensity since the 2008 financial crash. Over the past year, the Portuguese stock market has increased nearly thirty percent, but has fallen by more than 11 percent over the past ten days. The country received a €78 billion bailout from the IMF and EU in 2011.

"There is worry about contagion...The theory is that it could lead to bank failures and throw us back into recession," Thomas Roth of Mitsubishi UFJ Securities told the *Wall Street Journal*. Riccardo Barbieri Hermitte of Mizuho International PLC told the *Journal* that the selloff "shows that assumptions that the market was making were incorrect."

Portugal's PSI 20 stock index fell 4.2 percent Thursday, in its largest fall in over a year. Every other major stock index in Europe fell as well, led by large drops in Italy and Spain. A number of Italian banks likewise suspended trading in their stocks, and the main Italian stock index fell by nearly three percent in intraday trading.

Greece was forced to scale back a government debt issuance, while a bank and construction company in Spain called off its bond sale.

Supposedly safe assets, such as gold and US and German government bonds, shot up in value as investors fled riskier assets. The price of gold climbed 1.1 percent, to $1,338.90 per ounce, its highest level since March.

Fears about the Portuguese banking sector compounded a string of negative data on the European real economy. Industrial production shrank in May in Italy and France, while Germany's imports, exports and industrial production fell that month, according to figures released by the German Central bank this week.

Fitch Ratings has likewise warned of an "increasing anxiety among investors that valuations reflect too much money chasing too few income-producing assets." The rating agency added, "Investors feel they have little choice but to invest in whatever comes to market, despite the continuing fall in yields and coupons."

The *Financial Times* commented this week in a piece, entitled "Thirst for yield drives investors deep into European 'junk' bonds," that "historically low interest rates have compelled fund managers to seek out riskier assets."

The piece noted, "The first half of this year saw 15 companies raise bonds that were rated at the CCC to C level, says Dealogic, a rating described as 'extremely speculative' or carrying 'substantial risks.'… This was three times the number of companies that raised such bonds in the same period last year. The amount raised has also more than tripled, to $7.5bn."

The *New York Times* made similar warnings earlier this week, referring to an “Everything Bubble” in which “there are very few unambiguously cheap assets.” The piece noted that “Global central banks have been on an unprecedented campaign of trying to stimulate growth through low interest rates and of buying assets with newly created money.”

The Federal Reserve has kept interest rates near zero for nearly six years, and has more than tripled its asset holdings since 2008, and other global central banks have followed suit. Last month, the European Central Bank (ECB) slashed one of its interest rates to negative territory, and lowered its main lending rate to a historic low of 0.15 percent.

These actions, however, have only succeeded in guaranteeing the wealth of the financial aristocracy while blowing an enormous financial bubble, totally out of keeping with the moribund state of the real economy.