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Fears of global recession send stock markets sliding

Reports that German leaders were preparing for Greece to default on its bonds drove European and U.S. stock markets lower. Investors are worried that a default by Greece could tip the global economy into recession.

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Reporting from New York — Stock markets around the world fell sharply as investors feared that a European debt crisis was coming to a head and threatening to tip the global economy into a recession.

The market declines were driven largely by reports from Germany that its leaders were preparing for Greece to default on its bonds but were struggling to reach a consensus on how to handle it.

The news sent German stock markets down 4.1% on Friday, similar to the declines elsewhere in Europe. Leading U.S. stock indexes followed, with the Dow Jones industrial average experiencing its worst day in more than three weeks, wiping out gains made earlier in the week.

"Now people aren't talking about a recession here in the U.S.," said Anthony Conroy, head equity trader at BNY ConvergeEx Group in New York. "Now we're talking about a global recession."

The Dow finished the day down 303.68 points, or 2.7%, to 10,992.13. The broader Standard & Poor's 500 index fell 31.67 points, or 2.7%, to 1,154.23. Both indexes have fallen five of the last six weeks.

President Obama had hoped to lift some of the economic gloom with his speech to Congress on Thursday night promoting a \$447-billion economic stimulus plan that would cut taxes and increase spending on infrastructure.

The speech, though, was immediately met with questions about whether it could pass a Republican-controlled House of Representatives, and whether it was big enough to have an effect if it did pass.

Investors had also held out hope that Federal Reserve Chairman Ben S. Bernanke would provide some hope for stimulus in a speech he gave Thursday, but he stepped back from making any firm commitments.

"Presumably they have shot their big cannons and what they have left are a few handguns," said Bernie McGinn, president of McGinn Investment Management. "People would like to have cannons now."

By Friday, most eyes had shifted to Europe, where investors were buying Greek bonds at prices that appeared to assume a default was possible.

The European Central Bank has been purchasing Greek bonds in an effort to help support the Greek government as the country implements an austerity program.

On Friday morning, though, the bank announced that its No. 2 official, Jurgen Stark, was resigning, reportedly because of his disagreement with the bond-buying program.

Shortly after that announcement, news reports said that Germany was drawing up a plan to shield its banks in case Greece does default on its bonds.

In July the European Union proposed a \$220-billion plan to help Greece avoid defaulting on the bonds, but political disagreements have thrown into doubt whether the second dose of this aid will be delivered to Greece. The specter of a Greek default is feared because many European banks hold vast stores of sovereign Greek bonds and could face difficulties like those encountered by U.S. banks in 2008 when mortgage backed bonds lost their value.

"This is Europe's 2008," said Kim Caughey Forrest, a portfolio manager at Fort Pitt Capital Group.

Caughey Forrest said that the risk is heightened because European financial leaders do not have the same powers that U.S. government officials had in 2008.

"We have some unholy politicking here, but it's nothing close to the scale of what's going on in Europe at this point," Caughey Forrest said.

Fears about the European economy drove investors to put their money in U.S. Treasury bonds and in the U.S. dollar, which rose 1.6% against the euro.

On Friday, top financial officials from the Group of 7 began two days of meetings in France, hoping to formulate a response to the recent economic problems.

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