MARKETS

Wall Street Slammed: Dow Sees Worst First Day of the Year Since '08

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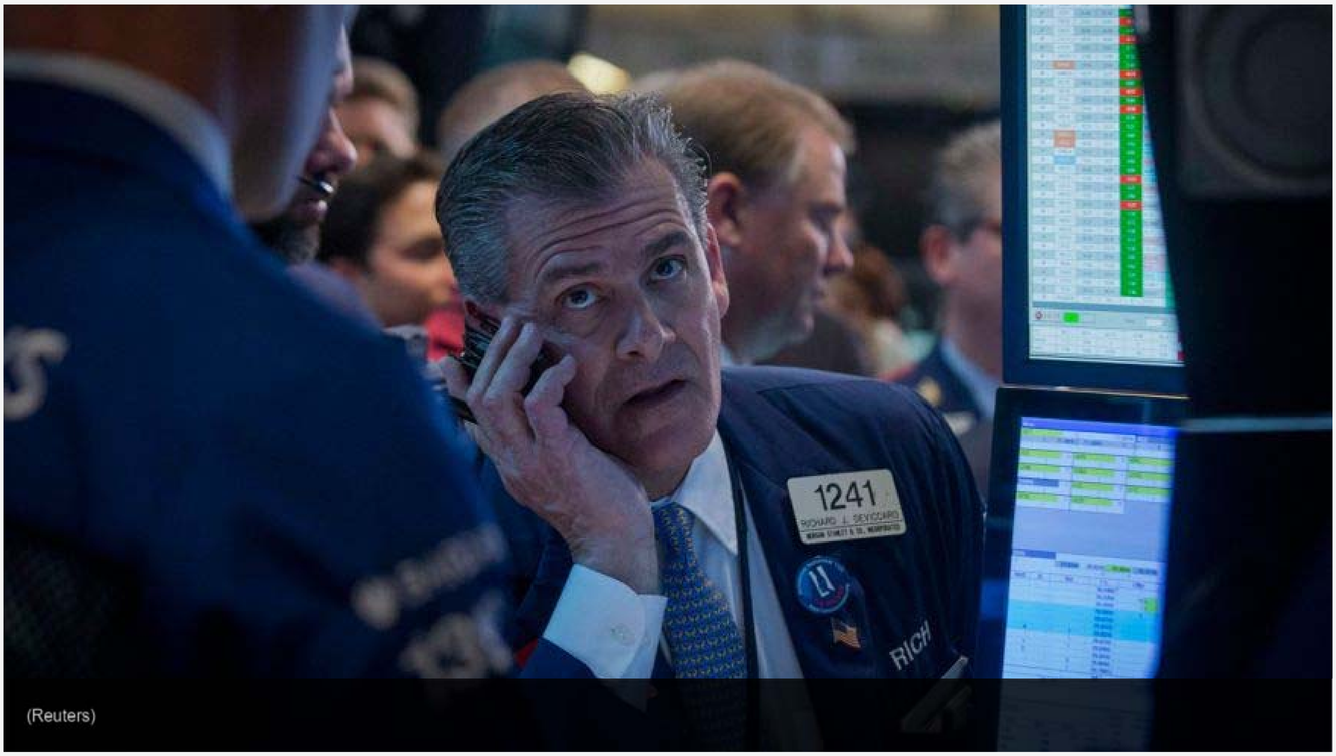

(Reuters)

Investors who thought global markets turned the page on 2015's investment themes got a rude awakening on Monday as last summer's concerns over China's economy resurfaced, though Wall Street ended well off session lows.

The Dow Jones Industrial Average plunged 274 points, or 1.58% to 17150. The S&P 500 declined 31 points, or 1.52% to 2012, while the Nasdaq Composite shed 104 points, or 2.08% to 4903.

All 10 S&P 500 sectors were in negative territory, as financials and health care led the way down, while energy was the best performer, bouncing between gains and losses.

Today's Markets

Just hours into the first session of 2016, China kicked off the New Year with a trading halt as concerns flared again about economic growth in the nation. Jitters spread to global equity markets, hitting U.S. stocks hard. The Dow saw its worst first day of the year since 2008.

The Shanghai Composite index, China's benchmark average, plunged 6.9%, hitting a brand new circuit breaker safety measure – announced late last year and put into action Monday-- halting trading twice during the session, first for 15 minutes and finally closing the session 90 minutes early.

The catalyst for the selloff was twofold.

First was a fresh round of weak factory data out of China. The nation's purchasing manager's index tumbled again, coming in at a reading of 49.7 for the month. That was slightly above November's reading, but below the line of 50 that separates expansion from contraction. The latest figures bring the count to ten-consecutive months of contraction in the manufacturing sector.

But Jason Pride, director of investment strategy at Glenmede, said the bigger part of the anxiety puzzle was nervousness about an impeding reprieve on a ban of large-scale asset purchases by large stakeholders in China. The ban was imposed after a sharp move lower in equity markets last summer, which ignited a global selloff, as the world began to take note of China's slowing economic growth.

Pride said while many cite the PMI data as the primary reason for the selloff, other changes are more significant.

"The actual catalyst is weakened investor sentiment driven by regulatory changes including the introduction of new circuit breakers and the end of the six-month ban on large-scale sales. Those are more of a near-term phenomenon," he explained. "The circuit breakers mean equity investors have limited liquidity during declines, and for anyone seeing equity portfolios are somewhat liquid, [limits] can cause them to pare some positions back on the margin."

The Shanghai Composite ended down 6.9%, while Hong Kong's Hang Seng dropped 2.7%, and Japan's Nikkei plunged 3%.

The sudden and dramatic declines also weighed on European averages. The Euro Stoxx 50, which tracks large-cap companies in the eurozone, dropped 3.21%, while the German Dax tumbled 4.25%, the French CAC 40 gapped 2.71% lower, and the UK's FTSE 100 shed 2.30%.

Aaron Jett, vice president of global equity research at Bel Air Investment Advisors, said while the reaction was extreme, the narrative is a story the markets have seen before – and you don't' have to look back very far to replay it.

"It should be no secret now that China is trying to move from a manufacturing to a consumer economy. That's been in the news for a while. This is a huge overreaction," he said. "The consumer economy continues to improve in China. On such a big base now, it just can't grow at 10% forever."

Jett said selling at such a dramatic pace is likely to be only temporary as there was no shortage of headlines for investors to digest.

After a steep selloff at the opening bell, U.S. investors parsed data on their own manufacturing sector, which came in weaker than expected and showed activity remained firmly in contraction territory.

The Institute for Supply Management reported its gauge of factory activity unexpectedly fell in December to 48.2, the lowest reading since June 2009, from 48.6 in November. Economists expected a slight move higher to 49, still below the reading of 50 that separates contraction from expansion.

Jett said whether manufacturing in the U.S. continues to weaken, or shows some signs of life depends a fair amount on what happens with the U.S. dollar and the Fed's tightening cycle.

"Most of the currency effect, which hurts manufacturing in the U.S., has been felt already. It depends on how many times the Fed moves this year, though. If it moves too fast, it could strengthen the dollar quickly, which would hurt our markets, and would obviously make U.S. manufacturing less attractive globally," he explained.

Still, he expects slow movement from the Fed given 2016 is an election year, and data that hasn't been, in his view, strong enough to support many more hikes from the central bank in the near term.

Oil Changes its Tune…Temporarily

Global oil markets saw a shift in sentiment on Monday as tension in the Middle East helped boost prices. But the commodity couldn't hold onto gains of more than 4% as oversupply continued to plague the market.

On Sunday, Saudi Arabia cut diplomatic ties with Iran, giving Iran's ambassador 48 hours to leave the country, after protests in Tehran, the nation's largest city, resulted in a fire after the execution of a Saudi cleric. Just a day later, Reuters reported that the Saudi foreign minister said the country will cut all commercial ties, put a stop to air traffic between the two nations, and ban its citizens from traveling to Iran.

"This is definitely more of a supply store than a demand story," Jett explained. "Demand has been pretty decent and continued to grow, and it should continue at a decent clip. But will it be enough to soak up enough supply in the U.S. market? Probably not," he said.

He added that for prices to move higher on Middle East tension alone, the status of the conflict would have to escalate substantially.

"It would have to be something a lot more serious as far as military action compared to cutting ties between Iran and Saudi Arabia," he explained. "The oil market is paying more attention to the supply side than the demand side. Because the U.S. is not in the Middle East and producing more than ever, it's trumping the power of OPEC."

In recent action, West Texas Intermediate crude prices slipped 0.76% to $36.76 a barrel, while Brent, the international benchmark, declined 0.16% to $37.22 a barrel.

Pride added that energy-related equities are beginning to pique his interest as valuations are becoming more attractive for buyers across the board.

"They've just been hit so hard that they're getting closer to the point where valuation becomes more attractive enough to ignore the near-term fundamentals. But we're not quite there yet," he said.

Elsewhere in commodities, gold prices gained 1.40% to $1,075 a troy ounce, while silver paced 0.30% higher to $13.82 an ounce. Copper dropped 2.59% to $2.07 a pound on the back of China's disappointing economic data.

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