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## World Markets Dive as Investors Retreat to Safety

By GRAHAM BOWLEY

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The financial aftershocks from the earthquake in Japan gathered force on Tuesday as investors fled from riskier assets like stocks, oil and gold amid growing worries that the crisis could slow a global economy that only recently seemed to be getting back on its feet.

Unnerved by a 16 percent drop in Japanese shares in the first two trading days of the week, stock markets slumped as investors sought havens like United States dollars and Treasury bonds, pushing interest rates lower. By the close of trading in New York, however, shares of United States companies recovered some of their losses after the Federal Reserve said it would keep its accommodative monetary policy in place to stimulate the United States economy.

The Fed's announcement brought calm on a day of market turmoil that raised painful memories for some of 2008, when the financial crisis froze capital markets and precipitated a similar rush for safety. "This was a very scary day for global stock markets," said Carl B. Weinberg, chief economist at High Frequency Economics. After the roller-coaster session, the Standard & Poor's 500-stock index, which at one point had been down 35 points, closed down 14.52 points, or 1.12 percent, at 1,281.87. The Dow Jones industrial average fell 137.74 points, or 1.15 percent, to 11,855.42. The Nasdaq fell 33.64 points, or 1.25 percent, to 2,667.33.

On Wednesday in Tokyo, markets regained some lost ground, with the Nikkei 225 rising 3.97 percent in afternoon trading. But on Tuesday, the uncertainty extended to energy markets, as analysts warned that diminished growth in Japan could prompt a sharp decrease in oil demand.

"We don't know the extent to which the post-tsunami Japan is going to grow, and whether or not there will be consequences for other countries as well," said Chris Lafakis, an energy economist for Moody's Analytics.

Amid the flight to safety, oil prices fell \$4.01 to settle at \$97.18 a barrel, while gold dropped \$30.70 to \$1,395.70 an ounce. The 10-year Treasury note, meanwhile, rose 14/32, to 102 22/32. The yield fell to 3.30 percent, from 3.36 percent late Monday.

The central fear is that the disaster — especially the danger of increased radiation exposure from stricken Japanese nuclear reactors — could rip a big hole in the supply lines of the world's third largest economy and set back the global recovery. Some of the first ripples reached the United States on Tuesday as Subaru said it was canceling all overtime at its plant in Lafayette, Ind., which builds the Outback, Legacy and Tribeca models, to reduce the chance that it will run out of some parts from Japan. "The main economic shock is not the direct loss of business, but spillover effects in terms of damage to the power and transportation industries and disruptions to the supply chain," said Ethan S. Harris, an economist at Bank of America Merrill Lynch. "Specifically, many auto and electronics firms rely on the affected region for parts."

As a result of the volatility, several debt offerings were postponed, while Toys "R" Us was forced to delay a planned syndicated loan.

The ultimate impact on world growth is likely to be small, however. "The quake-ravaged economy, the world's third largest, could lower economic activity in Japan as much as one percentage point, and shave off worldwide growth 0.2 percentage point in 2011," said **Bernard Baumohl**, an economist at the Economic Outlook Group.

The region affected by the quake accounts for only about 6 percent of Japanese gross domestic product, and economists calculate that the short-term effects might be eventually offset as Japan spends hundreds of billions to rebuild.

Closer to home, a temporary reduction in American exports to Japan might trim 0.1 to 0.2 of a percentage point from United States economic growth in 2011, according to Stuart Hoffman, chief economist at PNC.

One major exporter, General Electric, which designed the reactors at the Fukushima nuclear plant, fell for the second day in a row, closing down 1.6 percent at \$19.61. G.E. has either built or licensed 92 nuclear reactors now operating worldwide — about 20 percent of the global total, according to Michael Tetuan, a spokesman for General Electric.

But nuclear power development remains a small part of the company's overall operation; it produces reactors in partnership with Hitachi. The business accounted for just \$1 billion in revenues in 2010 — a tiny fraction of the \$85 billion generated by its industrial supply business.

"Nuclear is not a major piece of the puzzle for G.E.," said Daniel Holland, an analyst with the investment research firm Morningstar. "This doesn't move the needle a whole bunch."

Despite the problems in Japan, the Japanese yen strengthened, as speculation increased that big Japanese investors like pension funds and banks — Japan is the second-largest holder of United States Treasuries — would dump their overseas holdings and buy yen to return cash home.

At the same time, there were signs that investors were unwinding other trading positions. With interest rates near zero at home, Japanese investors used yen to buy Australian and

Canadian dollars, as well as the Brazilian real, to invest in higher-yielding assets there. Other foreign investors placed similar bets, bullish on those countries' growth prospects. But as demand for the yen picks up, those currencies have weakened. The Canadian dollar fell 1.5 percent on Tuesday morning, while the Australian dollar fell around 2 percent. The Brazilian real has fallen nearly 4 percent since Friday.

Across Wall Street, traders said the initial reaction among many hedge funds and institutional investors to the Japanese crisis was to sell first and ask questions later. "It's definitely been risk-off since Friday," said Ward McCarthy, chief financial economist with Wall Street investment bank Jefferies & Company. "Uncertainty tends to breed a desire for safety. As it becomes easier to assess what all of the ramifications are, I suspect that will recede."

For instance, Robin Thorn, who oversees the \$1.3 billion PineBridge Global Equities mutual fund, decided on Sunday evening to cut the fund's 9 percent position in Japanese stocks in half.

With the help of his team of more than two dozen analysts in Tokyo — many who have been sleeping in their offices — Mr. Thorn sold off companies that had exposure to nuclear-plant construction. "That turned out to be the right thing in the shorter term," Mr. Thorn said.

But Mr. Thorn said he and his team were also looking for buying opportunities, saying he had increased the fund's stake in companies that will play a role in Japan's rebuilding. And on Tuesday afternoon as Japanese American Depositary Receipts and exchange-traded funds rebounded sharply from early lows, Mr. Thorn said he expected Japanese markets to rally.

"We feel a lot of the emotional selling has been done," Mr. Thorn said. "And it's clear through the action of U.S.-based investors today that people are now trying to look for bargains."

*Reporting was contributed by Tom Zeller Jr., Julie Creswell, Eric Dash and Nick Bunkley.*