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Markets Dive on Weak Retail Sales

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U.S. stock markets took a dive on Wednesday as retail sales unexpectedly fell in the month of April and helped fuel a debate among investors over the direction of the economy.

The blue chip Dow Jones industrial average was down 1.93 percent, or 163.2 points, while the broader Standard & Poor's 500 index fell 2 percent, or 18.8 points. The tech heavy Nasdaq fell 2.2 percent, or 38 points.

Wall Street has rallied strongly since hitting a low in early March on a series of better-than-expected economic reports and on optimism that the worst of the financial crisis for some of the nation's largest banks may have passed. The S&P 500 has surged about 34 percent since March 9.

This week that exuberance appears to be on hold as investors try and gauge whether stocks have shot up too high, too fast. This morning's retail sales report showered more pessimism on those concerns as the government reported monthly retail sales dropped 0.4 percent.

"Terrible retail numbers compared to what was expected ... that was just enough to set it off," said James Paulsen, chief investment strategist of Wells Capital Management and a self-described bull. "Now you have some economic ammo for the bears ... it is going to fuel the debate over whether this is a new bull market or a bear-market trap."

The figures from the U.S. Commerce Department showed that consumers held off on big-ticket purchases at electronics and appliance stores, sending sales down 2.8 percent in April compared with the previous month, the largest drop of any category. Gasoline stations took a 2.3 percent hit, while food and beverage stores fell 1.1 percent.

"Despite the positive benefits to disposable income from the fiscal stimulus tax reductions and transfers that kicked in during April, consumers are not being induced to go out to the malls and the auto dealers," IHS Global Insight Chief U.S. Financial Economist Brian Bethune wrote in a note to clients this morning. "There is just too much pressure from other areas, including reduced employment levels, prospects of rolling furloughs and virtually no growth in private sector wage and salary compensation."

Yesterday, investors bought up shares of blue-chip stocks in afternoon trading, lifting up the Dow, but broader indexes closed in the red. Today a majority of companies in the blue chip index were down.

The S&P 500 index showed investors selling off shares of companies that produce discretionary consumer goods (those that are not staples) as well as shares of financial firms, industrial companies and information technology companies. Shares of companies in the health care, consumer staples and telecommunications sectors gained.

Michael Farr, president of portfolio-management firm Farr, Miller & Washington, based in Washington, said Wall Street's rally of nearly two months was unsustainable. Despite the economic reports that have fueled optimism on Wall Street, the breadth and depth of the recession was too severe to be overcome so easily, he said.

"We are still declining but the rate of decline is slowing and that seems to be a cause of great celebration for investors," he said. "I am kind of scratching my head, because what they are really desperate for is just an end. The truth is this current level of exuberance is somewhat premature, but investors just can't wait to be done with this mess."

Overseas markets were mixed. London's FTSE was down 1.96 percent, or 86.92 points, while Germany's DAX was down 2.4, or 116.6 points. Japan's Nikkei was up 0.45 percent, or 41.88 points.

Staff writer Ylan Q. Mui contributed to this report.