Swaggers turn to shudders a year after market high

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SAN FRANCISCO -- Just a year ago, investors were swaggering as the stock market surged to an all-time high. Now, almost everyone on Wall Street and Main Street seems to be shuddering amid a frightening reversal of fortune that has erased $8.3 trillion in shareholder wealth in the past 366 days.

"We aren't dealing with a fundamental economic issue any longer," said James Paulsen, chief investment strategist for Wells Capital Management. "We are dealing with fear. And that doesn't respond to economic medicine."

That hasn't stopped the U.S. government from trying to find a remedy.

In a series of moves aimed at avoiding the mistakes that culminated in the Great Depression nearly 80 years ago, the government already has committed to spend more than $1 trillion to prop up ailing banks and other lenders during the past month of turmoil.

But none of it seems to be working, which only seems to be scaring people even more, especially after the nation's leaders spent nearly two weeks painting a gloomy picture of the economic outlook to persuade Congress to approve a $700 billion bailout of the banks.

"I think right now there are just some very powerful negative images that are alive in many people's minds - images of the Depression, images of people selling apples," said George Loewenstein, a behavioral economist at Carnegie Mellon University. "The images of the downside are just so salient in people's minds, and nobody has presented an upside image yet."

Some investors, like software engineer Sandeep Bhanote, are trying their best not to be spooked.

"Fear is the most dangerous emotion. It can really do the market a lot of harm when maybe it is not necessary to be afraid," Bhanote said Thursday at a coffee shop near the New York Stock Exchange.

The quarterly 401(k) statements that are starting to arrive in the mail will only serve as another grim reminder of the financial carnage. And it has gotten worse since the quarter ended in September, with the Dow Jones industrial average tumbling every day so far this month.

In this week alone, the Dow Jones has plummeted by 17 percent, bringing the total decline to 39 percent since the stock market's most famous bellwether peaked at 14,164.53 on Oct. 9 a year ago.

The downturn translates into a paper loss of $8.3 trillion, based on figures measured by the Dow Jones Wilshire 5000 Composite Index, which tracks 5,000 U.S.-based companies' stocks and represents almost all stocks traded in America.

There are some logical reasons why stocks aren't worth as much as they were a year ago.

For starters, the U.S. economy appears to be in a recession for the first time since 2001. To make matters worse, this contraction looks like it could be particularly painful, with home prices in their steepest slide since the Great Depression and banks in their shakiest condition since the savings-and-loan crisis of the 1980s and early 1990s wiped out thousands of federally insured institutions.

"It's not just psychology," Santa Clara University finance professor Meir Statman said of the stock market sell-off. "There are some things happening in the world that are pretty scary. We have every right to be scared."

And some economic doomsayers still think it could get a lot worse.

"The economy has been in terrible shape for a long time. It was built on an illusion before this," said Mike Stathis, an investment consultant who wrote a book called "America's Financial Apocalypse." "I think people are starting to recognize what's coming, so why wait around for it to get worse?"

Major mutual fund companies like The Vanguard Group, Fidelity Investments and T. Rowe Price all reported sharp increases in phone calls this week as some individual investors bailed out of the market and others sought words of reassurance.

"It's consistent with the climate we're in. Obviously in times of significant market volatility, investors are interested in our thoughts about what they should be doing," Fidelity spokesman Vin Loporchio said. "We try to reinforce our message about long-term investing."

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