Spectacular share rally on stimulus speculation

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The Australian share market and dollar have staged spectacular turnarounds, with the All Ordinaries index rising phoenix-like from falls of more than 5 per cent to finish with a 1 per cent gain.

The All Ordinaries ended up picking up 40 points to close at 4,097, after falling as low as 3,829.

The ASX 200 staged an even more spectacular recovery, rising from a fall to 3,766 to end the day up 1.2 per cent at 4,034.

The Australian share market bottomed for the day just after 11:00am (AEST), but did not make steep gains until well after noon.

The Australian dollar bottomed out around 12:15pm at 99.28 US cents, but has since rallied to be worth 101.63 US cents by 5:54pm.

PHOTO: Some fund managers say the rally was also driven by the low valuation of some stocks. (ASX)

VIDEO: Aust traders buy up after mass sale (7pm TV News NSW)

VIDEO: Market uncertainty could threaten surplus (7pm TV News NSW)

AUDIO: Share rally linked to stimulus speculation: fund manager (ABC News)

AUDIO: Local market ends higher after day of volatility (PM)

AUDIO: Banks cut rates as conditions deteriorate (PM)

AUDIO: European markets lose ground despite promising China data (PM)

MAP: Australia

Fund managers say the dramatic mid-afternoon rally was sparked by a rumour that the US Federal Reserve will announce another round of quantitative easing when it meets tonight in a bid to stop the financial market slide turning into an economic slump.

Quantitative easing involves the Fed buying treasury bonds, effectively pumping hundreds of billions more US dollars into the global economy.

RBS Australia head of trading Justin Gallagher says the turnaround on the share market was unprecedented.

"I haven't seen this type of volatility and this extraordinary turnaround... this is getting new levels of volatility, even post-GFC days, so it's been an extraordinary day," he told ABC News.

Justin Gallagher says the turnaround was driven by a combination of commentary out of China that interest rates may not need to rise further, as well as speculation that the US might embark on further quantitative easing.

Funds manager Roger Montgomery says there is likely to be a reversal of some of today's gains if the Federal Reserve rules out quantitative easing when it meets tonight.

"I think if this rally is on the expectations of some sort of monetary intervention on the part of the US Treasury and that doesn't eventuate then, yes, you'd expect further declines," he told ABC News Online.

Some fund managers say the rally was also driven by the low valuation of many stocks.

BlackRock investment strategist James Holt says his firm is starting to use some of the profits it has made from surging gold and bond prices to buy shares.

"Gold and bonds are doing really, really well and we're making profits on them and putting these into the asset classes that are getting cheaper and cheaper, which are definitely equities," he told Reuters in an interview.

"Our global allocation fund still likes equities on the whole, but we tend to have had those equities that are either exposed to Chinese growth, which is more sustainable, or the big multi-national dividend payers, the ones that have the lowest PEs (price-earnings) and highest dividends, and pretty strong cash flows."

Roger Montgomery says his fund has been looking at opportunities in the battered retail and banking sectors.

"There are many cheaper companies trading today than there were a few weeks ago," he added.

"We had only 10 per cent of our funds invested [in equities] as of March or April, that's increased now to about 30 per cent, so we certainly believe there's more value appearing."

However, investment bank Morgan Stanley's global strategist Gerard Minack warns there could be further falls for shares if western economies do slip back into recession.

"If the S&P 500 falls another 20 or 30 per cent, it's hard to see why our market wouldn't fall a similar magnitude," he observed.

How stocks finished

The financial sector led the share market rally, with the major banks bouncing back from falls in the 2-5 per cent range to finish strongly higher.

CBA led the way with a 3.6 per cent rise to $47.28, NAB jumped 2.9 per cent to $21.50 after falling below $20 at one stage, ANZ gained 2.8 per cent, while Westpac was up 2.2 per cent.

Investment bank Macquarie bounced back from falls of around 6 per cent to a 2.8 per cent gain for the day.

The resources sector also surged in the afternoon.

BHP Billiton ended 1.2 per cent higher, Rio Tinto fell 1.6 per cent, Fortescue 2.7 per cent, and OZ Minerals 1.4 per cent.

Energy companies bounced too, with Woodside ending up 3 per cent and Santos up 1.3 per cent to $11.45.

The retail sector also recovered.

JB Hi-Fi remained the market darling retailer after yesterday's profit report, rising 3.4 per cent today to $14.48.

Myer gained 5 cents to $2.19, David Jones rose 2 per cent to $2.72, and Billabong was up 1.2 per cent to $5.12.

However, Harvey Norman continued to underperform its retail rivals, sliding 3.2 per cent to $1.80.

More defensive stocks such as Telstra, Woolworths and blood products maker CSL stayed slightly in the red, despite the afternoon rally.

Gold stocks were some of the only companies gaining consistently throughout the day, with Eldorado closing up 1.9 per cent as spot gold hit a record of just over $US1,772 an ounce, before falling back to around $US1,754 an ounce by 5:52pm.

One month oil futures trading in New York had also fallen below $US80 a barrel, with Tapis trading at $US114.40.

There were no identical Lazarus-like performances on Asian markets, with Tokyo's Nikkei ending down 1.7 per cent, Hong Kong's Hang Seng down 3.7 per cent and Shanghai's main index closing flat.

European markets also rebounded with London closing up 1.89 per cent and Paris up 1.63 per cent, but Frankfurt slipped 0.2 per cent.