In midst of recession, multi-billion-dollar paydays for US hedge fund managers

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A survey of the 2007 income of American hedge fund managers published Wednesday sheds light on the ugly reality of American capitalism.

The annual ranking of top hedge fund earners compiled by *Alpha*, a magazine that caters to wealthy and institutional investors, reports that the top money-maker, John Paulson, took home $3.7 billion last year, probably the richest single-year haul in Wall Street history.

Paulson, the founder of Paulson & Company, was not the only multi-billion-dollar hedge fund winner. He was followed by George Soros, who took in $2.9 billion, and James H. Simons, who netted $2.8 billion.

The top 50 hedge fund managers took in a combined sum of $29 billion.

To place these astronomical figures in some perspective, the combined take of these 50 individuals is about the same as the annual gross domestic product of Kenya, a country of 32.5 million people, and a billion dollars less than the GDP of Sri Lanka, the home of 20 million people.

Paulson's $3.7 billion income alone would cover most of the $4.2 billion shortfall projected by New York Mayor Michael Bloomberg, himself a multi-billionaire, in his preliminary budget for 2009—a deficit that is to be closed by a new round of budget cuts and layoffs.

For the most part, the top money-makers of the US hedge fund world amassed their windfalls by betting correctly that the US housing market would collapse or speculating on the soaring price of basic commodities such as oil and foodstuffs. They benefited handsomely from the housing and credit crises that are driving millions in the US and other countries into foreclosure and threatening millions more with hunger or outright starvation.

The *New York Times* noted on Wednesday that Paulson began betting that complex mortgage-backed securities known as collateralized debt obligations, which played a key role in the housing and credit bubbles that fueled record banking profits until they collapsed last year, would decline in value. One fund that he established achieved a return of 590 percent last year and another gained 353 percent. By the end of 2007, Paulson presided over $28 billion in assets, up from $6 billion 12 months earlier.

Forbes magazine, which published its own survey of hedge fund and private equity CEOs, headlined its story "Wall Street's Top Earners: Your Pain, Their Gain." The article begins:

"Problems paying the mortgage, filling the gas tank and feeding the family have eroded living standards for millions of Americans during the past several months. Not so for people who manage big piles of money: many of them made a fortune betting correctly on the housing debacle and rising commodity prices last year."

Forbes' survey of the top 20 hedge fund and private equity managers concluded that their combined income for 2007 was 43 percent higher than in 2006. "To even make the list," the magazine wrote, "you needed minimum earnings of $350 million, which is $90 million higher than the year before."

The magazine reported that hedge funds increased their assets by 14 percent to $2.2 trillion, while private equity funds raised a record $300 billion to reach $2 trillion in assets.

Hedge funds and private equity funds are virtually unregulated companies that cater to wealthy investors, pension funds, university endowments and the like. Hedge funds promise their moneyed investors super-high returns from speculation in stocks, bonds, derivatives and commodities. The managers usually collect a fee of 2 percent on the total investment of their clients plus a 20 percent cut of any gains realized.

Last year, the Democratic Congress quietly dropped a proposal to end a tax windfall for hedge fund managers, whose income is taxed at the 15 percent capital gains rate, rather than higher income tax rates.

Characterizing the operations of hedge funds, Gary Burtless, an economist at the Brookings Institution, said, "To some degree it's a very gigantic version of Las Vegas."

Alpha noted that the top 25 hedge fund managers on its list earned an average of $892 million, up from $532 million in 2006.

It wrote: "He [Paulson], Soros, Simons and the others who earned more than $1 billion—Philip Falcone and Kenneth Griffen—led what may well prove to be the greatest display of individual wealth creation in any year in the modern history of finance...

“Five of the managers on this year’s list each made more in 2007 that the $1.2 billion that JPMorgan Chase & Co. agreed to pay for the almost failed 85-year-old Bear Stearns Cos.

“When we published our inaugural list, in 2002, Soros led the way with $700 million, a showing that this year would have put him at No. 9. Back then it took $30 million to crack the top 25; this year, $360 million.

“The grand total earned by the top 25 in our 2003 ranking, almost $2.8 billion, was less than what any of the top three managers made this year and less than one fifth of what the top ten made altogether ($16.1 billion).”

It said that minimum required to make it into this year’s top 50 list was $210 million.

What do these gargantuan incomes say about the parasitism of American capitalism and the social inequities it engenders? If one takes Paulson’s income for all of 2007 and divides it by 365, one arrives at a daily take of $10, 137,000. This breaks down to $422,374 an hour, $7,040 a minute, and $117 per second.

The wage of the average American worker is about $17.50. If one were to assume that Paulson worked a 40-hour per week, 52-week schedule, his hourly “wage” would be 24,136 times that of the average worker in the US.

Every hour, Paulson took in a sum nearly equal to the median yearly income ($60,500) of seven American families. The combined $29 billion that went to the top 50 hedge fund managers is equivalent to the median annual income of 479,000 US families.

The sums raked in by the most successful (and lucky) hedge fund managers are only the most spectacular expressions of a far broader phenomenon in corporate America. A survey of CEO pay published Monday by the *Wall Street Journal* noted that the median salary and bonus for CEOs of 200 US firms with annual revenue over $5 billion rose 4.7 percent last year to $2,939,000. Total direct compensation, including stock options and other incentives, rose to a median of $8,848,000.

Another study estimated that the average top US corporate executive received total compensation of $18.8 million as of February 2008, up from $15.6 million a year earlier.

For the most part, CEOs who have presided over financial disasters and plummeting share prices, including those at major banks and investment houses, continue to award themselves multi-million-dollar salaries and bonuses, and even those who have been forced to resign or retire at companies like Citigroup and Merrill Lynch have gotten severance packages worth tens of millions of dollars.

The concentration of wealth at the top and pervasive social inequality are greater in the US today than at any time since the Great Depression. A study released last week by the Economic Policy Institute and the Center on Budget and Policy Priorities reported that economic inequality has continued to grow rapidly this decade.

The study concluded that the nation’s wealthiest 5 percent of families were paid, on average, more than 12 times as much as the poorest fifth in 2004-2006, compared with nearly nine times as much in 1987-89. Since 1998-2000, the income of the poorest fifth has fallen by 2.5 percent, while the wealthiest fifth saw income rise by 9.1 percent. The Income of the middle fifth of families has grown since the late 1990s by just 1.3 percent.

These figures, in fact, significantly underestimate the growth of inequality because they do not take into account income from capital gains, the vast bulk of which goes to the richest layers of society.

On average, the report notes, real wages for low- and middle-income families are now the same or lower than they were in 2001.

Jared Bernstein, a senior fellow at the Economic Policy Institute, said that since 1913, the United States witnessed only one other year of such unequal wealth distribution—1928, the year before the stock market crash.

As the *New York Times* detailed in an April 14 article headlined “Even When Times Get Tough, the Ultra-rich Keep Spending,” the addiction of the uppermost social layers to lavish spending and a life style that harkens back to the decadence and debauchery of the French Ancien Régime continues unabated, despite the slide of the US into recession and the growing social misery of tens of millions of people.

The *Times* notes that the crisis on Wall Street has begun to impact the “merely rich,” under conditions where New York’s Independent Budget Office has warned that the city could lose up to 20,000 financial sector jobs by the end of 2009, but has not had a perceptible affect on the habits of the most privileged layers of the financial elite.

The newspaper writes: “Many businesses that cater to the superrich report that clients—many of them traders and private equity investors whose work is tied to Wall Street—are still splurging on multimillion-dollar Manhattan apartments, custom-built yachts, contemporary art and lavish parties.

“Buyers this year have already closed on 71 Manhattan apartments that each cost more than $10 million, compared with 17 apartments in that price range during all of 2007... And the GoodBar, a downtown lounge, reports that bankers continue to order $3,000 bottles of Rémy Martin Louis XIII cognac.”

The article describes a party planned for May 10 at the exclusive Plaza Hotel. “It will feature a dozen female string musicians made up to look like statues and clothed in dresses of fresh flowers, like roses and gardenias. There will be caviar and cognac bars, as well as a buffet designed to visually replicate 17th-century Dutch paintings from the recent Metropolitan Museum of Art exhibit, ‘The Age of Rembrandt.’”