Growing warnings of a stock market bubble

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Concerns are starting to be voiced in the financial elites about how long the bull run in stock markets, which has delivered hundreds of billions of dollars to them in additional wealth, can continue.

Last Monday the S&P 500 index went past the record high it reached in early August marking the second longest-running bull market in US history, eclipsing the 1949-56 upsurge. It has risen by around 268 percent since the market low of March 2009, recorded in the wake of the 2008 global financial crisis. The longest bull run was from 1987 to 2000, which ended with the collapse of the dotcom bubble.

With the coming to power of the Trump administration, markets experienced a surge and have risen by about 16 percent. Initially this was fuelled by the belief that with its program of tax cuts for corporations, deregulation and promises of infrastructure spending it would be good for the bottom line. But even as doubts have arisen over how much Trump will be able to deliver the market rise has continued.

Now there is some degree of nervousness about how long the present upsurge can go on, which was voiced on Tuesday at a hedge fund conference in New York organised by the business channel CNBC.

The clearest warning came from long-time hedge fund operator Julian Robertson who said “we are creating a bubble” in the stock market. Stock market prices are too high because the low interest rate regimes established by the world’s central banks meant that investors are taking on too much risk.

“It’s the Federal Reserve’s fault and the Federal Reserves all over the world,” he told the conference. With interest rates at record historical lows there was “no real competition” for stocks, pointing out that until recently negative interest rates in the German government bond market meant that investors had to pay to hold its debt.

Leon Cooperman, the head of the hedge fund Omega Advisors, said while he did not expect a bear market, a 5 to 8 percent correction could happen at “any time” and bonds, where interest rates are at near all-time lows, “look like they’re in a bubble.”

Others are not so much concerned with the low interest rate policies of the central banks but with geopolitical risks, the most prominent of which is the threat of war on the Korean Peninsula.

The CEO of Blackstone Group, Stephen Scwarzmman said the issue was not so much economic or even the policies of the central banks. “It’s geopolitical and there’s some bad things going on in the world and conventional analysis says things will be fine.”

But whether it was North Korea or trade “there are a number of issues that people don’t want to focus on because the outcome would be really bad,” he said.

One of the indicators of the emergence of financial bubble conditions has been the rise and rise in the value of the cryptocurrency bitcoin, which has jumped by 335 percent this year to a price of more than $4,000. The astronomical increase in its value has attracted some attention from investors, prompting remarks by JPMorgan Chase CEO Jamie Dimon at a Barclays Investment conference this week.

He said the currency was a “fraud” and that he would fire anyone at the bank who traded in it “in a second,” likening its rise to the Dutch tulip mania of the 17th century. “It won’t end well,” he said, adding that it would eventually “blow up.”

But the speculation in bitcoin is only a very graphic expression of the forces at work in financial markets as a whole. This can be seen by contrasting the latest bull run with that the run up of the markets in the period 1949-56. In the earlier period, the market was sustained by the growth of US industry in the past war period. By contrast, the present bull run takes place under conditions of low growth—the US economy has been growing at only 2 percent or less, well below that of any previous "recovery"—coupled with falling productivity and stagnant or falling wages.

The present period also compares unfavourably with the record run from 1987-2000. While market growth in that period contained a large element of speculation—even the former chairman of the Federal Reserve Board Alan Greenspan had occasion in 1996 to refer to "irrational exuberance"—it was based, at least to some extent, on real developments.

These were the lowering of the cost structure of industry provided by the development of globalised production and the increased use of information technology. The present upsurge, however, has been virtually entirely driven by the ultra-cheap money policies of the Fed and other major central banks.

In fact the rise of the market is itself a reflection of the lack of investment opportunities in the real economy. Consequently, the share price bubble has been driven largely by financial manipulations such as the use of borrowed funds at low rates to finance share buybacks.

Evidence of the way in which the underlying weakness in the real economy has led to an increasing turn to financial operations was provided in an investigation by the *Financial Times* published this week.

It reported that Apple, Microsoft and Alphabet (the parent company of Google) are among a list of top US firms which have become a force in the global bond market. Some 30 major US corporations now hold more than $800 billion worth of fixed income investments and have become "asset managers in their own right" according to the head of JPMorgan's corporate finance advisory group Ramaswamy Variankaval.

Overall the cash holdings of US corporations have risen to more than $2 trillion, an increase of 50 percent over the past decade and more than double their holdings at the turn of the century.

The *Financial Times* found that the 30 major companies which were the subject of its investigation, including firms such as Ford, Coca Cola and Boeing, hold more than $1.2 trillion in cash, cash equivalents and marketable securities.

These figures, which indicate the lack of investment opportunities because of low growth levels, point to the growing divergence between the rise of the stock market, and the real economy on which it ultimately depends.