Wall Street margin debt surges to record high

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Wall Street's S&P 500 index reached a new record high on Thursday on the back of the decision by the Fed the previous day that its continuous boosting of financial markets, through the injection of more than $1.4 trillion a year in asset purchases, would continue for a "long time."

The commitment came despite indications of increased US economic growth and rising inflation which, in times past, would have set the stage for a tightening of monetary policy. But such is a fear that even the hint of a move in that direction will spark a collapse of the speculative financial boom that Fed chair Jerome Powell took every opportunity at his press conference to rule it out.

The extent of the speculative mania, which goes way beyond anything seen in the past, is indicated by broad financial trends and specific events.

One of the most significant broad indicators is the escalation of margin lending in which investors borrow money from brokers to finance share purchases and trade in financial markets. The collateral for the loan is the financial asset purchased, with the broker able to demand more cash from the investor—a margin call—if its market value falls.

The perils of margin trading were revealed last month with the collapse of the previously little-known family investment firm Archegos Capital as a result of such a call. It had amassed some $50 billion in loans from some of the world's major banks, most notably Credit Suisse, and its demise left the banks with a total loss of $10 billion.

But despite this warning sign, the escalation of margin debt is continuing. The Financial Industry Regulatory Authority, a supposed Wall Street watchdog operating under the supervision of the Securities and Exchange Commission, has reported that margin debt at the end of March was a record $822 billion.

This compares with the figure of $479 billion at the same time last year and more than double the peak of $400 billion in 2007 on the eve of the financial crisis of 2008.

Placing these numbers in context, the *Financial Times* reported calculations by the London-based fund ABP Invest showing that in the 2000 dotcom and 2007 credit booms US margin debt reached a level equivalent to around 3 percent of gross domestic production. It is now equivalent to nearly 4 percent.

But even the figures provided by FINRA are a major underestimation of the total debt involved because, through the use of financial derivatives, banks are able to further finance highly leveraged trading as was revealed in the collapse of Archegos.

The cheap money provided by the Fed is enabling the orgy of speculation which has seen the transfer of trillions of dollars into the hands of the world's richest individuals, while millions of people in the US and around the world confront a return to conditions not seen since the days of the 1930s Great Depression.

There was a revealing exchange which took place during the CBS program "60 Minutes" earlier this month when Fed chair Jerome Powell was questioned on the escalation of margin debt.

The interviewer, Scott Pelley, noted there had been a 49 percent increase in margin debt so far this year and asked: "At what point does the Federal Reserve start to rein in this speculative bidding up of stock prices based on borrowed money?"

Powell replied: "That sounds like margin debt. I don't know that statistic. I really can't react to that statistic."

The assertion by the Fed chief that he is completely ignorant of the level of margin debt, given its significance for the stability of the financial system, simply beggars belief.

Powell chose to answer in the way he did because of fear that any comment on the issue—and even the vaguest hint that margin debt was reaching dangerous levels and might need to be reined in—would set off turbulence on Wall Street, so dependent has it become on the flow of ultra-cheap money from the central bank.

Another broad indicator is the increase in the money raised by special purpose acquisition companies (SPACs). The firms, sometimes described as blank cheque companies, raise money and obtain a stock market listing with the aim of taking over another company which wants to go public and join the share market boom without having to through the often-complex procedure of making an initial public offering.

In the first three months of this year SPACs raised almost $88 billion, more than for the whole of 2020.

There are numerous individual phenomena which express the extent of the speculation. Chief among these is bitcoin, which earlier this month rose to a high of $64,000 before pulling back somewhat.

The rise and rise of Tesla shares is in the same category. The company is also tied in with the bitcoin speculation. On Thursday it announced its net income for the March quarter was $438 million, a record. The company revealed it had sold $1.5 billion worth of bitcoin which contributed $101 million to the bottom line.

As a producer of electric vehicles, Tesla also picked up $518 million in selling regulatory credits to other companies to help them meet emissions mandates. As the *Wall Street Journal* put in a headline “Tesla makes more money trading bitcoin than selling cars.”

The complete divorce of the share market value of the company from underlying real value—a characteristic feature of the stock market boom as a whole—is indicated by the fact that Tesla’s market value of $700 billion is more than five times the combined value of Ford and General Motors. Sales of the former in the US in the first quarter alone were more than double Tesla’s global sales for a year.

Possibly the most egregious expression of the market mania is the case of Hometown International which owns a small deli in Paulsboro, New Jersey. The deli had sales of just $21,772 in 2019 and only $13,976 in 2020 when it was closed for six months due to the COVID-19 pandemic. But recently its share market valuation topped $100 million. As one hedge fund manager commented “the pastrami must be amazing.”

The rise and rise of Hometown’s market value is indicative of a broader process. Shares and other assets, including major industrial commodities such as lumber and copper, are being purchased purely on the basis that other buyers will come in at an even higher price.

While commentators, barely able to see beyond the end of their nose and no doubt dazzled by the rise of their own portfolios, have been hailing the market rise as a resurgence of the US economy out of the pandemic, it is an expression of its deeply diseased character.

It should be recalled that the origins of the present maniacal phase of the stock market boom lie in the massive intervention by the Fed beginning in March 2020 when markets collapsed and the $21 trillion market for US Treasury bonds, the basis of the global financial system, froze.

The Fed’s intervention, amounting to trillions of dollars and supporting all financial markets, including the purchase of stocks for the first time, was an extension and qualitative development of the policies it has pursued ever since the stock market crash of October 1987 when it initiated the program of supplying ever cheaper money to the markets in response to a crisis.

The history of these interventions shows that whatever their effect in short-term stabilisation they prepare the conditions for the resurgence of the underlying crisis in even more virulent form.

All the conditions are now developing for another crisis, going far beyond the scale of the crash of 2008, in which the working class will be directly confronted with the necessary task of taking political power in its own hands in order to begin the reconstruction of the US and global economy on socialist foundations.