

U.S. Families' Exposure to Stock Market at Unprecedented Level

by Richard Freeman

In 1989, U.S. families held 27.8% of their financial assets invested in stocks, already a very dangerous proposition, given the speculative bubble which the market had already become. However, by 1998, according to Federal Reserve Board figures, U.S. families had doubled their financial assets invested in stocks, to 53.9% of total financial assets. Given the increasing volatility of the artificially inflated U.S. stock market, those families have put themselves in an extraordinarily vulnerable situation.

Simultaneously, U.S. families disinvested, or kept their holdings flat, in the kinds of financial assets which represent some degree of stability: savings bonds, corporate bonds, certificates of deposit, and bank checking and savings accounts.

The change in the profile of family financial assets is an indication that a clinical, fantasy-ridden obsession, has gripped the American population. One is reminded of the individual, watching from the shore, as a boat is about to plunge over Niagara Falls; his response to impending catastrophe?

He swims out to the boat, to hop on board for the ride.

Table 1 shows the composition of U.S. family financial assets, in dollar terms. Between 1989 and 1998, U.S. families cut, by absolute amounts, the holdings of critical financial assets: Family holdings of certificates of deposit went from \$782 billion to \$595 billion, the holdings of savings bonds went from \$112 billion to \$92 billion, and holdings of bonds—mostly corporate, and state and municipal bonds—went from \$782 billion to \$585 billion. In the same interval, the level of family holdings of transaction accounts, which comprise primarily checking and savings accounts and certificates of deposit held at banks by individuals, and which are insured up to \$100,000 by the Federal Deposit Insurance Corp., rose, but only marginally, from \$1.46 trillion to \$1.56 trillion.

By contrast, the stock market dominated the U.S. family financial asset sheet. Between 1989 and 1998, U.S. family holdings of stocks more than tripled, from \$2.13 trillion to \$7.39 trillion. There are two principal reasons that the value

TABLE 1
Composition of U.S. Family Holdings of Financial Assets, 1989-98

(billions \$)

	1989	1992	1995	1998
Transaction Accounts (checking and savings accounts)	1,462	1,314	1,337	1,560
Certificates of Deposit	782	604	535	595
Savings Bonds	112	86	129	92
Bonds	782	633	594	585
Cash value of life insurance	456	451	693	872
Other*	1,925	1,884	2,427	2,615
Holdings of Stock, direct and indirect	2,125	2,528	3,809	7,388
Total Financial Assets	7,644	7,499	9,524	13,707

*the portion of retirement funds and mutual funds that are not invested in stocks, managed asset accounts, etc.

Sources: U.S. Federal Board of Governors, *Survey of Currency Finances*; EIR.

TABLE 2
Composition of U.S. Family Holdings of Financial Assets, 1989-98

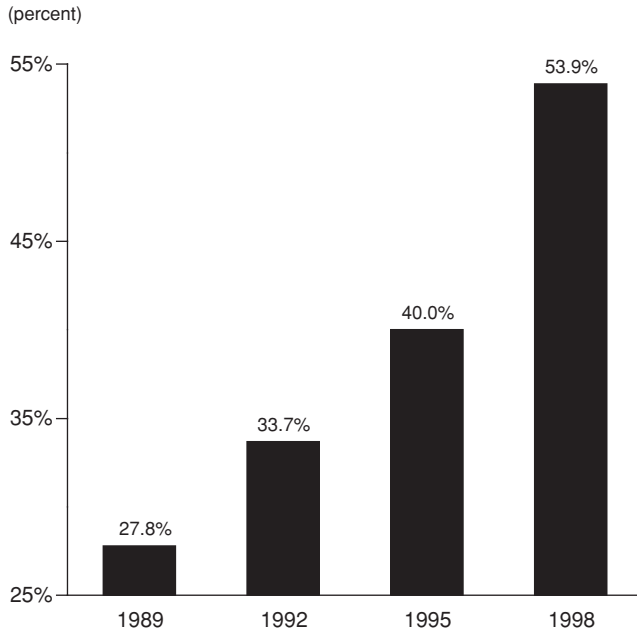
(percent)

	1989	1992	1995	1998
Transaction Accounts (checking and savings accounts)	19.1	17.5	14.0	11.4
Certificates of Deposit	10.2	8.1	5.6	4.3
Savings Bonds	1.5	1.2	1.4	0.7
Bonds	10.2	8.4	6.2	4.3
Cash value of life insurance	6.0	6.0	7.3	6.0
Other*	25.2	25.1	25.5	19.1
Holdings of Stock, direct and indirect	27.8	33.7	40.0	53.9
Total Financial Assets	100.0	100.0	100.0	100.0

*the portion of retirement funds and mutual funds that are not invested in stocks, managed asset accounts, etc.

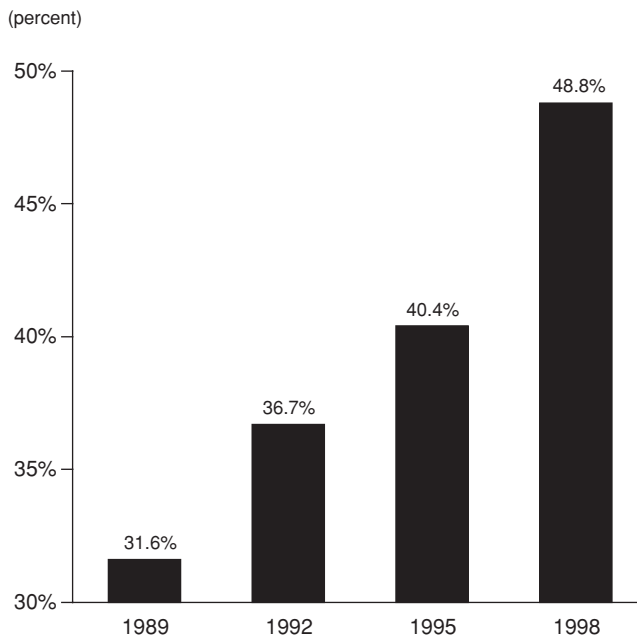
Sources: U.S. Federal Board of Governors, *Survey of Currency Finances*; EIR.

FIGURE 1
Percent of U.S. Family Financial Assets Invested in Stocks, 1989-98



Sources: U.S. Federal Board of Governors, *Survey of Currency Finances*; *EIR*.

FIGURE 2
Percent of U.S. Families That Are Stock-Owners



Sources: U.S. Federal Board of Governors, *Survey of Currency Finances*; *EIR*.

of a family's holding of stocks would increase. First, the value of the stock can appreciate. For example, if a family owns 100 shares of IBM, and the price of IBM rises from \$100 a share to \$150 a share, then the value of the family's stock holding would rise from \$10,000 to \$15,000. This happened to many stocks, and has contributed, in part, to the increase in the value of family stock holdings.

Hidden Margin Debt

Second, families have engaged in a stock-buying spree: In order to play the stock market, families have used their income, and, on numerous occasions, have dipped into their rent or mortgage money, and/or have borrowed from brokers, called margin loans. Between 1989 and 1998, the level of margin lending by brokers, called the official margin debt, rose from \$34.3 billion to \$141.0 billion. But, not satisfied with that, individuals borrowed on their credit cards, from home equity loan lines of credit, from their 401-K retirement plans, etc., to play the stock market. This is called the "hidden margin debt."

Raymond DeVoe, an economist with Legg Mason Wood Walker stockbrokers, who has worked on Wall Street since 1949, estimated that "the actual level of customers' margin could be two to three times the reported level." If the official margin debt at the end of 1998 was \$141.0 billion, then actual margin debt is \$282-423 billion. Thus, driven by the fantasy world of get-rich-quick schemes, families poured money into stocks.¹

Table 2 reports the same process in terms of percent. Between 1989 and 1998, of total family financial assets, the share of U.S. family holdings of most specific financial instruments fell, almost across the board. During this period, the share of American family financial assets that were held in transaction accounts (checking and savings accounts) fell from 19.1% to 11.4% of the total. But the share of family financial assets that were held in stocks grew from 27.8% to 53.9%. Never before in American history, have families held more than half of their financial assets in stocks! (**Figure 1** shows the upward movement.)²

1. Families hold an even larger amount of stocks than stated in this table. The Federal Reserve's *Survey of Consumer Finances* includes a hefty amount of family holding of stocks in pension plans, but it does not include the stock held in defined benefit pension plans, because they are held outside the family household. The *Survey* also does not include family holding of stock of non-publicly traded corporations. But since these two sources of stock holdings are not included as part of family financial assets, in terms of the Federal Reserve Board's *Survey of Consumer Finances*, they are not included in this table, for our purposes here.

2. Families' assets also include non-financial assets, such as homes, cars, businesses, etc. The value of U.S. family non-financial assets for respective years was: 1989, \$17.50 trillion; 1992, \$16.31 trillion; 1995, \$16.57 trillion; and 1998, \$20.05 trillion. The addition of family financial and non-financial assets yields family total assets. For respective years, the value of family total assets was: 1989, \$25.14 trillion; 1992, \$23.81 trillion; 1995, \$26.09 trillion; and 1998, \$33.76 trillion.

Increased Involvement in Stock Ownership

As the stock mania grew, more families jumped into stock-buying. **Figure 2** documents the percent of all U.S. families invested in the stock market. In 1989, either directly or indirectly, 31.6% of families owned stock. By 1998, this had risen to 48.8%.

During this period, two separate, but closely connected processes were going on simultaneously. First, the percent of all U.S. *families* owning stock, increased; second, the percent of all *financial assets* held by families that are invested in stocks, increased.

U.S. family stock ownership has reached an unprecedented level, and cannot be sustained. Built up with several layers of highly geared leverage, the stock market is inflated to a level at least five times its real value. It intersects a world financial system with \$300 trillion of unpayable financial obligations. Those paper values will soon cease to part of the landscape.

U.S. families, which built up their stock portfolios under the delusion that they were making themselves rich for decades to come, will find that trillions of dollars of stock values will evaporate. The dream of easy, eternal wealth will be shattered, replaced by the reality that the crash will have wiped out their financial and other assets.

'Chile-Model' Crazyies Besiege Moscow

by Rachel Douglas

Vladimir Putin, the newly elected President of Russia, will listen to all kinds of advice but take his own decisions. Putin has plenty of options to make an improvement in economic policy, which would require his *not* paying attention to the recommendations of the hordes of neo-liberal economists, both foreign and Russian, now swarming into Moscow. The imposition on Russia, during the 1990s, of the radical liberalism of the Chicago School of economics, of Friedrich von Hayek, Milton Friedman, and the Mont Pelerin Society, has already devastated Russia's physical economy and its population, but the chief international purveyors of that destructive philosophy are at it again. The last week of April saw the arrival in the Russian capital of:

- a group of five agitators for the "Chilean model," led by University of California Prof. Arnold Harberger, the Chicago School's senior case officer for Chile;
- José Pinera, the organizer of Chile's privatized pension funds, which lost billions in the 1997-98 stock market crash;
- Sir Roger Douglas, who, as Finance Minister in the Labour government of New Zealand, launched infrastructure takedown and privatization reforms there in 1984, which became infamous as "Rogernomics" as they ravaged the agriculture, industrial employment, health care, and social fabric of that Pacific nation.

The U.S. Agency for International Development funded the Harberger delegation on its trip to Moscow, according to a report in the Russian publication *Vedomosti*, monitored and reported by RFE/RL Newline on April 27. Shocking, insofar as that is the same USAID, which footed the bill for the infamous Harvard Institute for International Development operations in Moscow (wherein mutual funds were being run out of the back office of an outfit, advising the Russian government on how to organize Russian markets to permit such speculative investment entities), but not surprising! The State Department's USAID and its predecessor, the International Cooperation Administration (ICA), have been funding free-trade dogmas since the 1950s.

In 1956, the ICA co-launched the "Chile Project" with the University of Chicago and Chile's Catholic University. Harberger was involved from near the outset. Cynthia Rush reported in her review of *Pinochet's Economists: The Chicago School in Chile*, by Juan Gabriel Valdés (*EIR*, Feb. 9, 1996), that the project gained complete control over the Catholic University's economics department, in the name of Aus-

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