

Back to the Future

*“The market had been a full runaway bull market to date, with wild gyrations in the prices of the more speculative issues. The basic financial problem soon became apparent and settled down to one dark stormy area: call loans. Call loans were time-restricted demand loans made payable by banks to brokerage houses. The cash from these loans was in turn put up for margin by the brokerage houses for their customers. The loans were the fuel for the fire that drove the market – the margin was essential. These loans were made everyday, as the bankers appeared on the stock market floor ready to loan money to the brokers. The problem was simple. The banks did not have enough cash available for the brokers to cover their margin requirements. The money that was available was between 100% and 150% interest rates. The banks, which usually fought to lend this high yield money, were not interested in extending any further loans to brokerage houses, at any interest rate. It was a credit crunch to the most dire proportions – stocks plummeted. Then, that fateful day, it was chaos on the floor of the exchange. Hundreds of brokers gathered around the money post, screaming out their demands for short term loans, but there was no money available, no money at all. This meant that the brokers must sell their stock positions on the open market to cover their margins, but there were no buyers for stock, all the buying had dried up. So it was a situation where all of a sudden there was no cash, and no buyers. **It was the market’s worst nightmare, and it happened quickly. Pure, abject, unadulterated, raw fear swept over the brokers and the bankers. Wall Street was simply out of cash. The panic was on.**”**

Fast forward to 2007. Substitute “mortgage” for “margin.” Or better yet, combine the current mortgage default problem with the margin problem, and you have a disaster waiting to happen. A disaster fueled by the fact that Americans have over-extended their debt. By the way, the above excerpt actually happened on October 24, 1907, nearly one-hundred years ago. Don’t think it can’t ever happen again, because perhaps, it’s already started.

Till next time,

Bill

*The Amazing Life of Jesse Livermore

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