Even the U.S. press warns, a market crash is coming

by Marcia Merry Baker

Readers of *EIR* are familiar with what has led up to the financial crisis now breaking out simultaneously at different points around the globe—from the Southeast Asian currency devaluations, to the mid-summer stock market madness in Europe and the United States. Over the last 20-30 years, a gigantic "bubble economy" of financial speculation has grown up, at the expense of the physical economy; and, the "Great Bubble" is beginning to burst.

Warnings and reports on this, with a focus on the looming crash in the stock markets, are now appearing regularly in capital cities around the world. For example, the London *Sunday Times* of July 27, ran the headline, "Brace Yourself for the Crash of '97." The hold-out, is still Washington, D.C.; but even in the United States, the media "money" columns have begun to offer advice on "self-protection" measures for the coming crash.

Paramount to understand, is that there is, and will be, no contained "regional" or "local" run on a currency, or contained bank failure, or contained stock exchange "correction" episode, or any kind of containable blow-out. The era of "managing" such incidents as the Mexico crisis (1994), the Barings Bank crisis (February 1995), and others, is over.

When we see reports of such incidents, we are seeing the process of disintegration of the entire world financial system. You can't even do "trend analysis" in the same way as before—stupid as it was. Take the stock markets. We are in an "ex-research" phase, as was stressed by the *Frankfurter Allgemeine Zeitung,* a leading German daily, in its July 25 coverage of a new report by Morgan Stanley investment bank, predicting a major stock market "correction" over the next 12 months.

It can be clearly stated, says Morgan Stanley, that stock market prices have completely decoupled from economic fundamentals. Stock market prices are now "ex-research," meaning that any assessment of economic perspectives of specific companies is now totally irrelevant for anticipating their future stock prices.

Crisis events of the day

In July, the Thai currency, the baht, fell 23.6% in value; the Philippines peso, 6.9%; the Indonesian rupiah, 5.3%; and the ringgit of Malaysia, 4.1%.

On the major stock markets, European analysts, generally, forecast a collapse in August, or possibly October. The European media project an imminent collapse of 20, 30, or 50% of the values on the New York Stock Exchange. This likelihood arises from the ricochet process that will inevitably ensue, when markets crash anywhere in the world, then cross-connect, then roll back to New York.

The major U.S. and European markets are now in a phase of hysteria, with bettors trying to hog all the profit they think they can get.

The Dow Jones "industrial" average is up by 28% this year to date, exceeding its rise of 26% during 1996. On July 31, it hit 8,254.89.

Germany's DAX index has gone up by 50% this year to date. In the first four months of 1997, more money was invested in German stocks, than in all of 1996. On July 23 alone, the DAX rose 4.15% (with a record 3.5 million transactions); this surge came the day after a TV special give tips on how to get in on the stock boom.

Other markets are wild. In the Netherlands, the homeland of the Tulip Bubble (which burst in 1637), the Amsterdam Exchange index has increased by 52% since January.

Historically, October has been a frequent month for a crash, for reasons of timing, including the fact that the government fiscal year ends on Sept. 30 in many countries; October marks the beginning of the second half of the fiscal year in Japan; it is the time for release of half-year corporate earnings, and so forth.

But beyond all this, there is the Big One—the derivatives markets. These markets represent the second level of the collapse process, an even deeper level of threat to blow out the banking and financial system. Forecasters are discussing whether a derivatives blowout will happen during the period of August through December 1997, or sometime later in 1998. The notional valuation of outstanding derivatives contracts is put at $60 to 100 trillion internationally.

Press coverage of the 'crash of '97'

• On July 23, the *Frankfurter Allgemeine Zeitung*'s lead article was headlined, "Fear Is Spreading Among Emerging Stock Markets; Now Also Latin America Is Facing the Currency Problems of Other Regions. Will There Be a Domino Effect Like the Mexico Crisis of 1995?" The article reported on worries at stock exchanges around the world, "that the present currency crisis in Southeast Asia could create disasters at more and more stock exchanges in the emerging markets by a domino effect." What started in Thailand, Indonesia, and the Philippines, has also weakened currencies in eastern Europe, and, in recent days, Brazil, Argentina, and Mexico were following with heavy stock market upheavals. "The IMF [International Monetary Fund] has already started emergency actions and is advising several countries in their crisis management. Leading analysts are already speaking of a renewal of the 1995 Mexico crisis, and warn investors of a potential crash risk," in particular that the huge capital flows into the emerging markets "could easily be turned around," it said.

Among the "crash prophets" cited, is the super-cautious Deutsche Bank Research agency, which is now expecting many more "Thailands," and giving Greece as an example of a hot candidate in this respect.

• On July 27, the London *Sunday Times* ran the story, "Brace Yourself for the Crash of '97." Writer David Smith predicted, "October is shaping up to be the cruellest month on the world stock markets." Smith began his warning to readers writing as if from the vantage point of January 1998, looking back on the crash that had happened on "Black Tuesday of October 1997." At the very least, the article concluded that, as of August, "Some severe turbulence is overdue."

• On July 26, the *Frankfurter Allgemeine Zeitung* ran a front-page editorial, warning of the crash consequences of current "high-altitude ecstasy" on the stock markets. Written by Jürgen Jeske, the article reported on the recent stock speculation hysteria in Germany, warning, "A stock market plunge always comes suddenly. If you look at the history of the big crash in 1929, there are certain striking similarities: the overall euphoria, the growing wish to buy financial assets, the run-up on new stocks, the utilization of the favorable market climate to issue new stocks, the takeover speculation. . . . Because the present euphoria is driven by huge liquidity, which cannot flow in forever, the danger of a backfire is growing."

• The Aug. 4 issue of *Time* magazine ran a cover headline, "Stocks—Preparing for the Crash." A three-page business section article, by Daniel Kadlec, titled "Wall Street's Doomsday Scenario," reviewed contingency plans by U.S. government and mutual funds "Crashmeisters" to manage the crisis. Kadlec wrote that "even with all the adjustments since the '87 crash, another meltdown is quite possible." The chief Crashmeisters are the members of the President's Working Group on Financial Crisis. But the *Time* review gave the best details on the managers of the mega-mutual funds companies, who are taking precautionary measures that are as insane as the buildup of the stock bubble to begin with. They are staging drills and practice-runs for the crisis ahead.

For example, Fidelity Investments (over $500 billion in investments) says that it can double its phone-line capacity in a crisis, dropping down extra cables now stored in the ceiling of its cafeteria. "During the past year, Fidelity has paid particular attention to crisis planning, 'More dry runs, more computer simulations to make sure equipment is working, information is disseminated quickly, and lines of credit are reconfirmed with our banks,' says Robert Pozen, president of Fidelity Management and Research Co."

Vanguard (managing $300 billion) has a "bear-market task force." Reported *Time,* "To prepare itself, Vanguard has built an off-site 'war-room' loaded with phones, and has a 'Swiss army' of about 1,000 telephone representatives that can be deployed almost instantly, doubling the firm's call capacity." John Brennan, CEO of Vanguard, can activate his war-room whenever an emergency hits, "to field frantic calls."

• *Money* magazine, in its August issue, ran the cover story, "Don't Just Sit There . . . Sell Stock Now!" The cartoon shows a man seated on the crest of a gigantic ocean wave, just about to crash. The magazine, whose July issue said "Sell Now!" advertises on the cover: "Risks are rising. Take profits by cashing in 20% of your shares. Our 24-page special report tells you what to do next."

Inside, a two-page graph shows three lines, the Dow Jones "industrial" average, corporate profits, and equity funds flows. The scenario is that, beginning now, the Dow will fall from a level of 8,000 down to a level of 6,200 by this time in 1998. Why? "Since 1995, strong flows into funds have made the stock market race ahead of corporate profits." So, analyst Michael Sivy, of *Money* magazine, says: Selectively sell your stocks. What about the whole financial system, you ask? Don't worry, Frank Lalli, managing editor of *Money,* says in an editorial, "Check your stocks today, and sell some of your runaway winners, so you'll have plenty of cash to invest the next time the market becomes the screaming bargain it was three years ago."