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# Stock Markets Implode Worldwide—What's Next?

By Dr. Jack Rasmus
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*Today, February 5, 2018 the main US stock market, the DOW, fell another 1,175 points, the largest drop in its history. That followed a major decline of 665 points the preceding Friday. The total two day decline amounts to 7.5%. The other major US stock markets, the Nasdaq and S&P 500 also registered significant declines of similar percentages. Markets in Japan and Europe followed suit over the weekend in response to Friday's US drop; and are expected to fall comparably to the US when they open for Tuesday, February 6. What's going on? More important still, what will go on—in the next few days and in the weeks to come?*

The business press and media trotted out all the experts today. The 'spin' and message was "don't panic" folks. This is to be expected, they say, given the bubble price run-up through 2017, and especially since last November 2017, after which the bubble accelerated still faster. In the month of January alone, the DOW rose nearly 7%. That's considered a good 'year's gain' in ordinary times. Yet mainstream economists say it hasn't been a bubble, while they give no definition of what a bubble exactly is—because they don't know. But certainly a DOW run-up from around 16,000 lows in 2016 to more than 26,000 in little more than a year constitutes as a bubble.

But the media talking heads parading in front of cameras today sing the same song, "don't panic". It comes in various keys: "It's a welcome pullback", a "constructive sell off", an "opportunity to buy on the dip" and other such nonsense. But when asked why now the collapse, they have nothing to add.

What it represents, however, is professional institutional investors decided to 'take their money and run', leaving the small investors to take the losses. And more are coming. The professionals realize that the central bank, the Fed, is going to raise interest rates 3-4 times this year. That has already begun to send the bond markets into a tailspin. And now stocks are following suit. The stock markets have risen to bubble territory for several reasons:

One is the 9 year massive injection of free money by the Fed and other central banks. More than necessary to invest in real production, so it flows into financial markets in the US and worldwide. Corporate profits since 2010 have nearly tripled, and capital gains taxes have been steadily reduced by trillions of dollars since 2010 as well. Corporations have kept a steady flow of money capital to their shareholders with 7 years of stock buybacks and dividend payouts—averaging a trillion dollars a year for seven years! Profits, dividends, buybacks, capital gains tax cuts resulted in trillions flowing into financial markets. Add to that record levels of margin buying of stocks by small investors (always a sign of bubbles) and that's the source of the record price appreciation of stock markets. And, of course, let's not forget the Trump business-investor tax cuts of more than $4 trillion (not $1.5) that are coming on top of it all—that will subsidize profits with an immediate 10%-31% profits boost, on top of the record profits that US corporations had already attained. Massive money capital injections surging into stock and other financial markets. That's why the bubble.

But what of the bust? Why now—not before or later? It's because of changes in the markets themselves: the advent of what's called 'momentum trading' by big institutions like quant hedge funds and others; by the shift to passive investing and what's called index funds; by derivatives like ETFs driving stock prices as well. All the above result in rising prices sucking in more money capital just because prices are rising….which results in still more prices rising.

Until of course the central bank convinces them that the 'punchbowl of free money' is being drained. Then the professionals take their money and run, leaving the 'herd' of small investors holding the empty bag.

What's most interesting is that the Fed's interest rates haven't even reached 2% and the system has cracked. In 2007, Fed rates had to exceed 5% before the credit crash was set in slow motion. But this writer predicted that would be the case, i.e. that the Fed rates could not rise above 2-2.25% (and the 10 year Treasury bond much above 3%) without precipitating another credit crisis.

But the stock crash of February 2 and 5 is not the beginning nor the end of what's coming. There may be a further decline in coming days but it will stabilize. There will be a recovery or sorts. But it will be a 'dead cat bounce', as is always the case in such events. Some weeks, or even months later, the real contraction will begin. And that will be the real one.

To recall events of 2008, it was the collapse of Countrywide Mortgage and Bear Stearns investment bank in early 2008 that were the warning signs. Recovery temporarily followed, until Fannie Mae and then Lehman Brothers set the real forces in motion. The precipitating events may not even originate in the US but outside. Japan and Emerging Market economy stock markets are especially vulnerable. But financial markets are global and tightly integrated in today's capitalist system. Contagion is built into the system globally. And investors move their money around worldwide in an instant. They will eventually pull back, wait and see, and the markets temporarily restabilize. Is it an opportunity to scoop up the losses of the smaller herd investors that will have lost trillions this week? That's what the professional investors, the big institutional investors, the hedge funds, private equity, the big capitalists will now be asking themselves. Or is it the real contraction that will drive the markets down at least 20% in coming days and weeks? They will also ask themselves will the Fed hold to its plan to continue to raise rates? If it does, the they'll decide the great stock bull run of 2010-18 and its bubble is over and they'll move to the sidelines for the foreseeable future, not temporarily. They'll take their trillions of dollars and run. And when they do, the real contraction will begin….and the road to the next recession.

In the meantime, watch the dead cat as it bounces. How high. And when it lands will it flop over dead or get up and run again?

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*Dr. Jack Rasmus is author of the 2017 book, 'Central Bankers at the End of Their Ropes: Monetary Policy and the Coming Depression', Clarity Press, August 2017, and Systemic Fragility in the Global Economy, Clarity Press, 2016*

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