



A Look at NYSE Margin Debt and the Market

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of Advisor Perspectives

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The New York Stock Exchange publishes end-of-month data for margin debt on the NYX data website, where we can also find historical data back to 1959. Let's examine the numbers and study the relationship between margin debt and the market, using the S&P 500 as the surrogate for the latter.

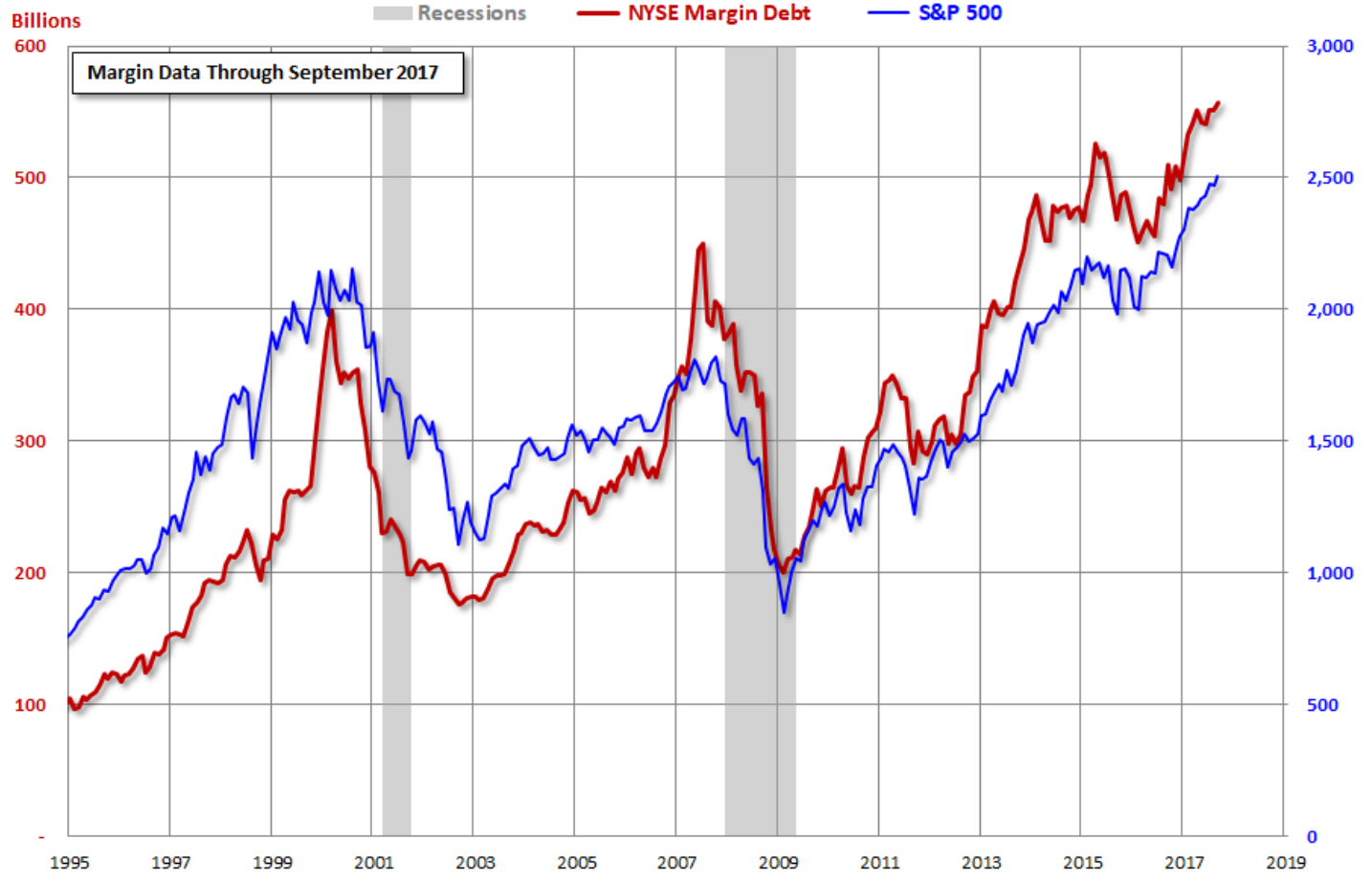
The first chart shows the two series in real terms — adjusted for inflation to today's dollar using the Consumer Price Index as the deflator. At the 1995 start date, we were well into the Boomer Bull Market that began in 1982 and approaching the start of the Tech Bubble that shaped investor sentiment during the second half of the decade. The astonishing surge in leverage in late 1999 peaked in March 2000, the same month that the S&P 500 hit its all-time daily high, although the highest monthly close for that year was five months later in August. A similar surge began in 2006, peaking in July 2007, three months before the market peak.

Debt hit a trough in February 2009, a month before the March market bottom. It then began another major cycle of increase.

The Latest Margin Data

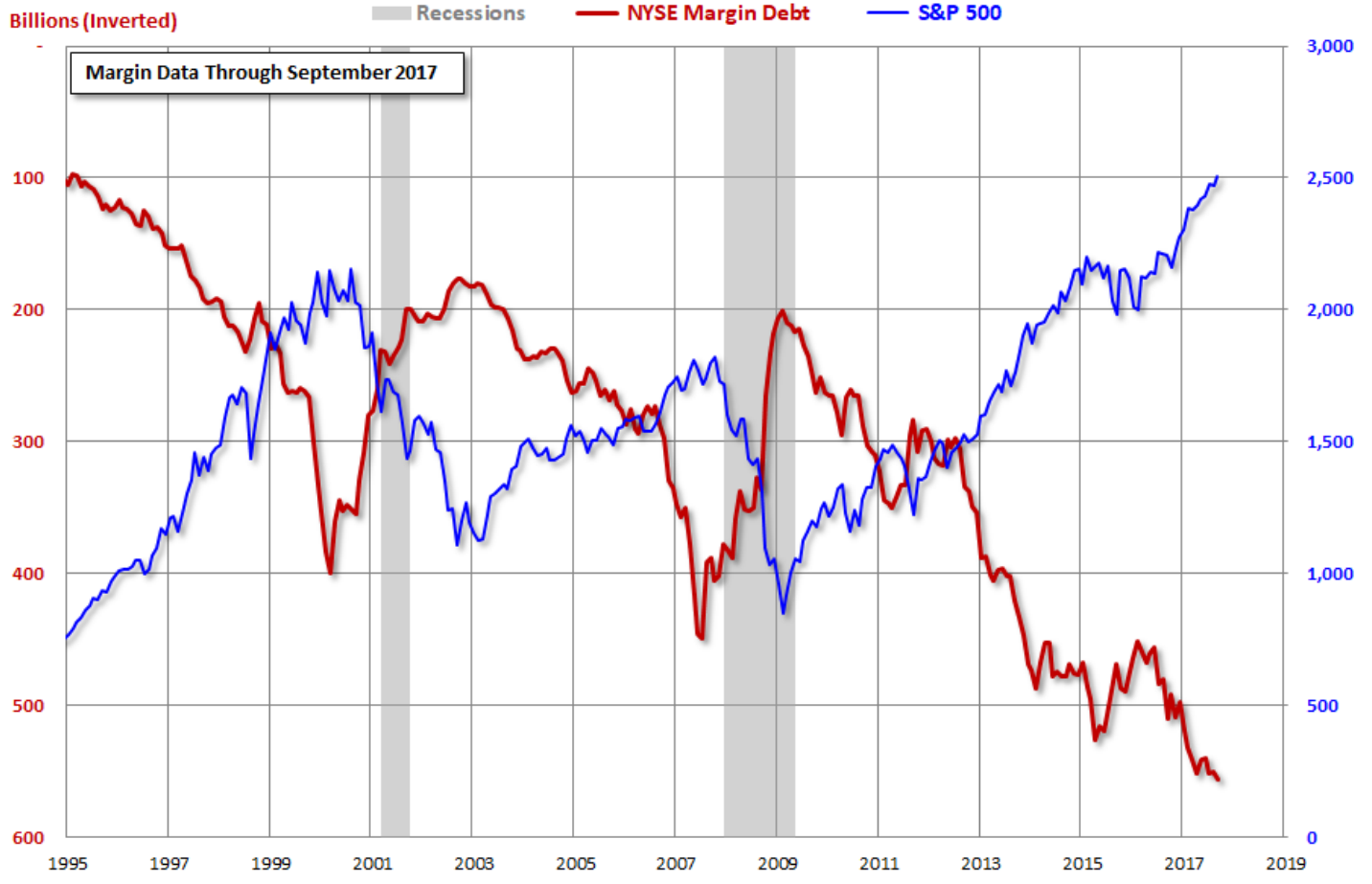
The NYSE has released new data for margin debt, now available through September. The latest debt level is up 1.6% month-over-month. The September data gives us an additional sense of recent investor behavior.

NYSE Margin Debt and the S&P 500 Real Values (Adjusted to Present-Day Dollars)



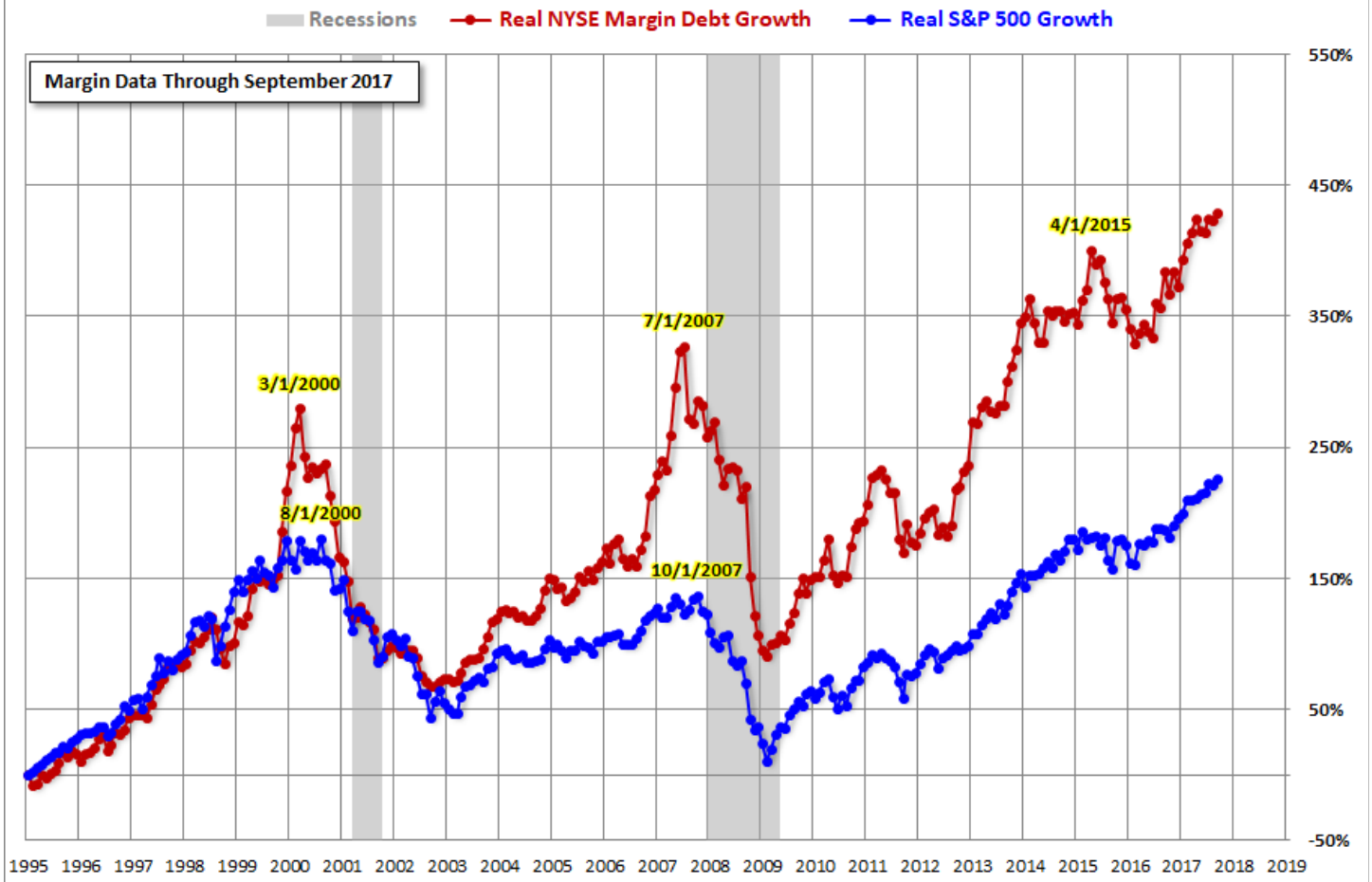
At the suggestion of Mark Schofield, Managing Director at Strategic Value Capital Management, LLC, we've created the same chart with margin debt inverted so that we see the relationship between the two as a divergence.

NYSE Margin Debt and the S&P 500 Real Values (Adjusted to Present-Day Dollars)



The next chart shows the percentage growth of the two data series from the same 1995 starting date, again based on real (inflation-adjusted) data. We've added markers to show the precise monthly values and added callouts to show the month. Margin debt grew at a rate comparable to the market from 1995 to late summer of 2000 before soaring into the stratosphere. The two synchronized in their rate of contraction in early 2001. But with recovery after the Tech Crash, margin debt gradually returned to a growth rate closer to its former self in the second half of the 1990s rather than the more restrained real growth of the S&P 500. But by September of 2006, margin again went ballistic. It finally peaked in the summer of 2007, about three months before the market.

NYSE Margin Debt and the S&P 500 Real Growth Since 1995

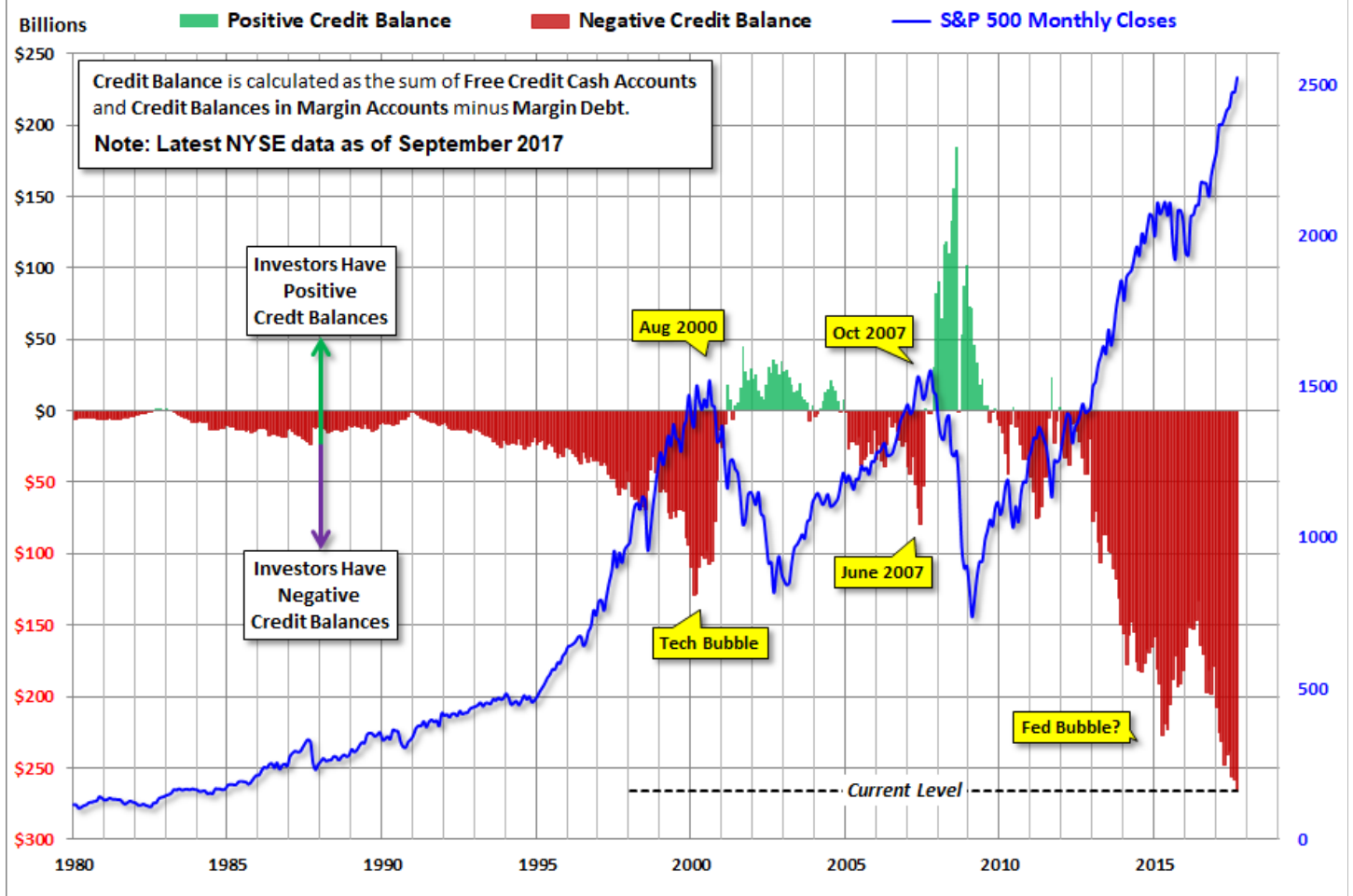


After the market low of 2009, margin debt again went on a tear until the contraction in late spring of 2010. The summer doldrums promptly ended when Chairman Bernanke hinted of more quantitative easing in his August 2010 Jackson Hole speech. The appetite for margin instantly returned, and the Fed periodically increased the easing. Even with QE now history, margin debt has reached another record high. The latest peak may not be a Fed-induced, easy-money bubble due to QE, but perhaps a response to the latest equity market rallies. It remains in high gear, as evidenced by the S&P 500 having logged over twenty record closes since the presidential election. For reference, last summer saw ten record closes and in November of 2014, there were twelve. As of this posting, the index is less than 1% below its latest record close.

NYSE Investor Credit

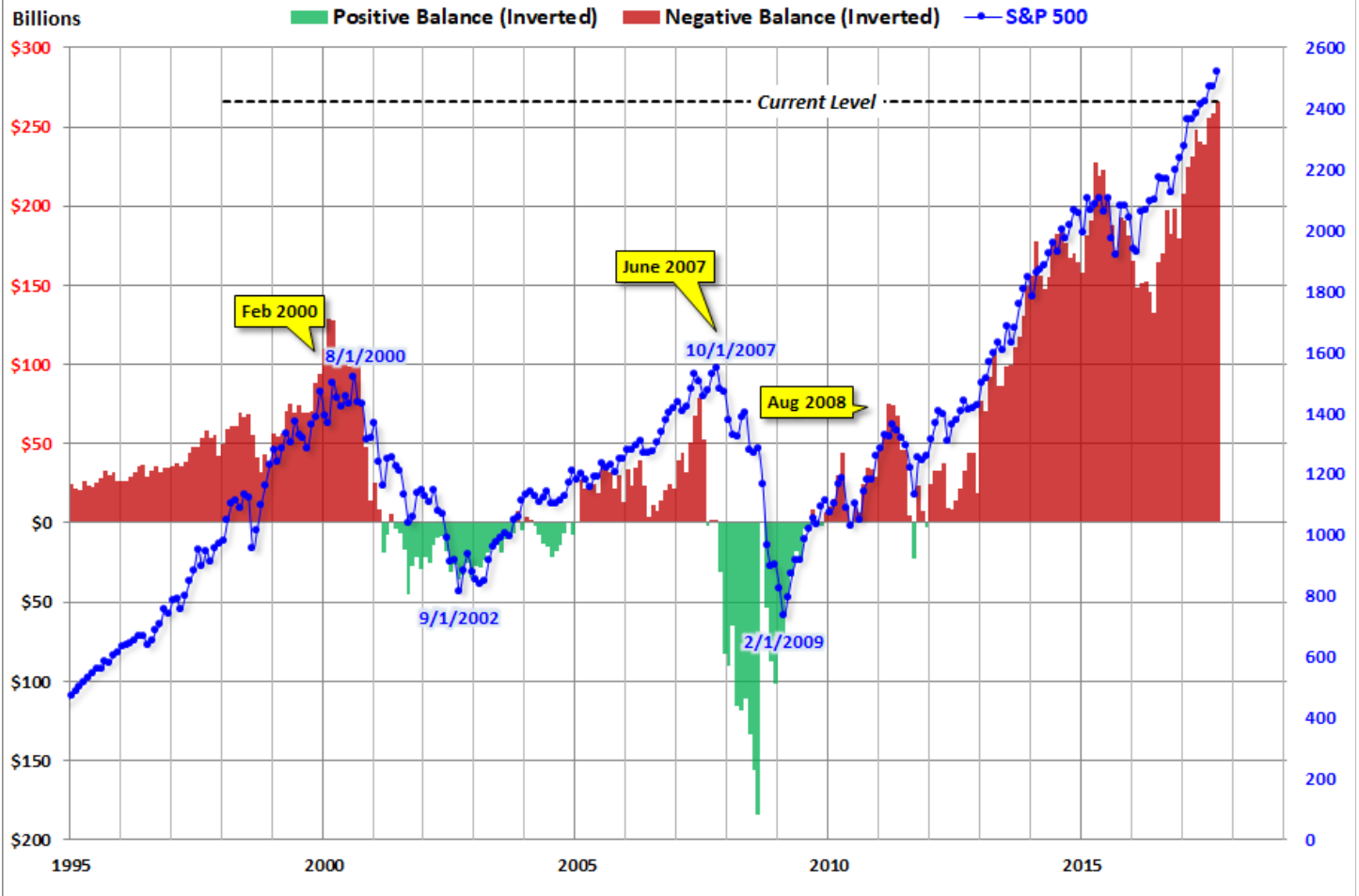
Lance Roberts of Real Investment Advice analyzes margin debt in the larger context that includes free cash accounts and credit balances in margin accounts. Essentially, he calculates the *Credit Balance* as the sum of *Free Credit Cash Accounts* and *Credit Balances in Margin Accounts* minus *Margin Debt*. The chart below illustrates the mathematics of Credit Balance with an overlay of the S&P 500. Note that the chart below is based on nominal data, not adjusted for inflation.

NYSE Investor Credit and the Market



Here's a slightly closer look at the data, starting with 1995. Also, we've inverted the investor credit monthly data and used markers to pinpoint key turning points.

NYSE Investor Credit and the Market



As we pointed out above, the NYSE margin debt data is several weeks old when it is published. Thus, even though it may, in theory, be a leading indicator, a major shift in margin debt isn't immediately evident. Nevertheless, we see that the troughs in the monthly net credit balance preceded peaks in the monthly S&P 500 closes by six months in 2000 and four months in 2007. The most recent S&P 500 correction greater than 15% was the 19.39% selloff in 2011 from April 29th to October 3rd. Investor Credit hit a negative extreme in March 2011.

Conclusions

There are too few peak/trough episodes in this overlay series to take the latest credit balance data as a leading indicator of a major selloff in U.S. equities. This has been an interesting indicator to watch and will certainly continue to bear close watching in the months ahead.

Note on the data: The NYSE website only posts the Free Credit Cash Accounts data back to 2003. The Free Credit Cash Accounts data back to 1980 is available on a fee basis from Haver Analytics.