TABELL'S MARKET LETTER

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Since figures have been available, debit balances of margin accounts in aggregate terms have generally moved in the same direction as stock prices, but more sharply. The chart on the opposide page shows this to be true, until the Dow Jones Industrial Average from its 1976 high declined to its February 1978 low. Uncharacteristically during this time, margin debt increased uninterrupted to new high through September of this year. Two important influences both hard to quantify for this spectacular increase would seem to be clients' borrowing money for non-stock purposes from the margin account and the convenient use of the margin account for the next-day settlement of option trades, the new game in town.

Margin credit has been singled out for selective control ever since the Securities and Exchange Act of 1934, which directed the Federal Reserve to "prevent the excessive use of credit in the purchase and carrying of securities." It is important to note this concept of excessive credit use relates not to the level of margin debt but rather to the actual or potential effect of such credit on the stock market. Initial margin requirements are not aimed at restricting the total amount of margin debt to some predetermined level. Instead, the Federal Reserve's purpose, it would seem, is first in rising markets to limit the magnitude of credit-based buying pressure generated by rising loan values and second in declining markets to provide a buffer between customers' initial equity and the minimum maintenance levels that would initiate wide spread margin calls. The changes in the level of these initial margins affect relative rates or credit expansion or contraction as compared with stock price changes over the same period.

Much attention has been given in recent week to the Federal Reserves' responsibilities in a declining market. The closer the borrowers' initial margin is to the minimum maintenance margin requirements of the New York Stock Exchange, the greater the possibility that price declines will lead to margin calls. This forced selling exerts downward pressure on an already falling market. New declines then trigger more margin calls causing a perpetualizing spiral of selling pressure, price decline, etc. This scenerio is not necessarily meant to explain or simplify the behavior of our recent stock market. However, it is interesting to look at the action of the stock market since the short-term oversold selling climax occurred last October. Since then, the market has rallied over 35 points in one day, unsuccessfully tested the selling climax low, returned to a more normalized, albiet volitile, condition, and rallied to date over twenty points from its November 14th low of 785.26.

This oversold condition was triggered in part by the declining quality of credit in margin accounts in an environment of short-term falling prices and high interest rates. Since statistics have been available, similarities can be seen between recent figures on the quality of margin debt and the figures registered at the 1974 low. In September, 1974, the quality of margin debt deteriorated seriously as 22% of customers' margin accounts were under 40% equity compared to 21% in October, 1978. Additionally, in September 1974, this represented 58% of the total margin debt under 40% compared to 47% in October, 1978. We are, of course, familiar with the two-year perfromance of the market since the 1974 low (October 4, 1975, DJIA 584.56 - September 21, 1976, DJIA 1014.76 = 73.60%). It must be noted, however, en route to this spectacular advance an initial short-term rally of 90.19 points occured posting a high on November 5 or 674.75 which was followed immediately by a decline of 97.15 points to a low of 577.60 penetrating the selling climax low by a slight margin. Selling climaxes of this type are not unprecedented (October 1957, May 1962, May 1970) and the behavior of margin debt statistics at or near major market bottoms can be instructive. As previously pointed out in this letter, climax lows are not always the actual lows in averages but rather tend to reflect an effective market bottom. The market action at the end of last October fits the criteria of a short-term selling climax. Historically, these conditions have occurred at significant market bottoms -- this possibility should not be discounted.

Dow-Jones Industrials (12:00 p.m.)	806.65
S&P Composite (12:00 p.m.)	55.39
Cumulative Index (11/22/78)	672.79

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