A Tale Of Six Investors

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On Tuesday, November 16th, I had a variety of conversations with clients regarding the recent market activity. I gain tremendous insights from my clients and there are things that all of us can learn from each other. Based on these conversations, I felt compelled to pen this short note this morning.

Backdrop: After a strong September and October, the markets have just corrected for seven days in a row (including yesterday). Tuesday the 16th was particularly harsh with high volume selling across the board. Commodities and Chinese stocks were hit the hardest. There are several different interpretations and reactions to this type of environment, and I think we can say that this type of environment encompasses a somewhat typical short-term correction (although all corrections have their differences).

Investor #1: A conversation this morning about the volatility in the market in the past week certainly didn't phase this investor, who was out enjoying the fresh snowfall of the past few days. They don't pay attention to things on a short-term basis, and tend to glance at their statement once a quarter. The past week's activity has absolutely no effect on their long-term plan.

Investor #2: This client is excited and rubbing their hands together, as they have some cash in their account and are excited about opportunity to buy more of their favourite stocks on sale. They're anxious to put their cash to work, but I recommended caution until some stability is evident before deploying new funds into the market.

Investor #3: After having a tough time watching the market rise so significantly for the past couple of months, with the feeling that they should have owned more stocks and were too defensive, they're no longer feeling regret. Last week they felt regret, but now that the market is falling, they feel relieved that they don't have too many equities. Owing fewer equities means not having to feel too much of the pain around the recent correction. Are they now keen to buy the stocks that they were keen to buy last week at higher levels? No. Less equities for me, please.

Investor #4: These are the hardcore margin investors. Margin investors are investing with borrowed money and don't have the time or ability to keep borrowed money at risk in the face of high volume sell off in the market. The rational thing would be to sell and stand aside. Now they wait for the market to stabilize, while continuing to keep their eye on their buy lists in the event that the market is ready to reverse course in the coming days. As a note, I myself am in this category, and I use a six percent stop loss on my whole margin account on a monthly basis. As soon as I'm down six percent for the month, I sell all my positions and stand aside until the next month. Am I discouraged? No. Is it a setback? Sure, but the market is open every day and I know there will be opportunities to climb my way back next month.

Investor #5: This is an investor who wants to make as much money possible, as quickly as possible, and not lose any of it. After seeing an impressive rise in their account in September and October, the past week took those profits back more quickly than they were earned. Such is the nature of corrections. Unfortunately, the speed with which profits are sought leads to an even faster experience with losses and emotions must be kept in check. After seven down days in a row, this investor wants to start selling in fear that the correction will never end. This investor will likely experience short-term regret if the market rises immediately after selling and will wonder if they made the right decision. This investor is probably investing above their true comfort level.

Investor #6: This is me, in my capacity as an Investment Advisor and Portfolio Manager providing recommendations to my clients and acting in a fiduciary capacity in the management of my discretionary funds. After taking some individual stock profits late last week (obviously not enough!), I have my eye on my buylist and am waiting for my buy signals to get involved. Silver has been one of the strongest leaders of this market, and it just corrected right back to the 20-day moving average and printed a doji (a technical sign of indecision that often signals a turning point) after a sharp correction. Silver is down 13 percent in the past six days and I sense an entry point. Consequently, I acted and introduce silver to my Aggressive Growth fund and ETF Strategies fund. I analyze the trade and it looks rational and wise. Will it be profitable? Time will tell, but I had a plan and followed it.

Corrections come and go, and I can’t stress enough the importance of realizing that emotions affect being rational with your finances. I have said it more than a few times, but most investors are incapable of looking at their accounts values on a frequent basis (e.g. daily or hourly!). Your account value on a given hour means nothing to your long-term set of objectives, so please try to stand back and stay focused on the plan. Which investor are you? Can you recognize yourself or your reaction to the recent market correction in these descriptions? Which investor (#1-#6) is acting most rationally? I would say numbers 2, 4 and 6. Remember, each investor saw the same market behaviour, but each perceived it differently. That is why understanding your motives as an investor is key to feeling confident in your investment strategy.

I always welcome your questions and comments.

Sincerely,

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