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PHILEQUITY CORNER

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Bullish or bearish?

The stock market has always served as a barometer for the overall state of the economy. Many non-economic factors affect this investor perception. A still ongoing war in another time zone or the gyrations of other markets due to the rise and fall of AI interest can affect the local economic outlook, especially for foreign investors.

Other strictly local developments such as the downgrading of the credit rating outlook of the country, the lower GDP forecasts, the devaluation of the peso versus the US outlook and investigations on misallocation of government spending tend to pull down overall investor confidence. Positive numbers like the steady flow of inward remittances from OFWs or the ample GIR level can provide some basis for optimism.

Can fear also be a factor in defining investor confidence?

Charles Kindleberger's "Manias, Panics, and Crashes: A History of Financial Crises" (1978) is often cited as reference for unusual crises in the market, such as severe market downturns experienced in the sub-prime mortgage crisis (2007-2010).

Kindleberger has written a historical analysis of financial crises and how panics and crashes start and fade away. In his analysis of these crises as cyclical, he finds that the market always comes back and recovers, until the next crisis.

Kindleberger, who wrote his book almost fifty years ago with three updates up to the latest edition (1996), cites the famous South Sea Bubble (1711-1720) as an example. The South Sea Company was a British firm doing business in Latin America. The price of the stock rose almost ten times before it crashed. This pulled the whole market down until it recovered again.

The Kindleberger book was much discussed during the 2007-2008 market crash arising from the sub-prime mortgage and the collateralized debt obligations which affected global stocks.

Kindleberger asks, "Are markets so rational that manias (irrational by definition) cannot occur?"

Kindleberger charts 34 financial crises from 1618 to 1990. Clearly, manic cycles seem to pop up routinely and almost on schedule, much like solar eclipses that turn day into night, but only for a while.

In 1996, Allan Greenspan then the Federal reserve Board Chairman, talked of the market's "irrational exuberance" referring to the dotcom bubble of the mid-nineties. This exuberance covered all sorts of listed stocks that used online apps which did not properly reflect the financial prospects of the firms.

On the bullish side, Greenspan followed up that fateful prediction of overvalued stocks with a more bullish assessment of stocks with good prospects that are “rationally justified”. The re-coined phrase of these deserving stock class raised the possibility of “rational exuberance”

History then teaches us lessons on how bubbles start and end. These lessons seem to address both bulls and bears.

A reality TV show (2001-2006) called “Fear Factor” explores reactions of contestants to deep-seated phobias. Surviving their fears, they allow themselves to be subjected to creepy situations like being lowered into a tank full of small rats or snakes crawling all over their bodies or walking a tightrope to pluck flags in a race for time. The winners are those who overcome fear and stay in the race.

In one memorable episode, contestants (none of them Filipinos) were required to eat a fertilized duck egg (balut) with the still feathery body and bill already evident. Does this yucky looking item evoke the same fear and loathing among natives? For us (including myself), balut that is unshelled is just a hearty snack. You can take it with a pinch of salt.

Does the prospect of a volatile market also differ between local investors and their foreign counterparts?

The fear factor should be used constructively as a sixth sense of evaluating risk and rewards. But it should not be the only basis for investor confidence in the market.

Regular analysts of the market can explain a mild rally in a bear market as a case of “bargain hunting”. Is this why buybacks of stocks from current investors are providing a lift in the market?

The fear factor needs to be put in perspective. It is the same investors who turn from bears to bulls. Staying on the sidelines can be a missed opportunity for missing the transition. A long-term investor understands this.