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“Spooked Investors Seek Safety”

Summary

Since the third quarter proved to be trying and full of uncertainty, many investors are focused on staying safe to make it through the difficult economy. Many investors felt that they were living day to day; trying to make the best decisions in order to stay afloat one day at a time until the market stabilized. These decisions turned many risk takers into safety seekers. Instead of going out and developing risky deals they are choosing to stay inside and focus on creating security. The reasons for this behavior include the unpredictable market that seems to be a repeat of the financial crisis three years ago. Investors are hoping to get out of the tumultuous times in one piece.

In tough times, gold is something people turn to in order to feel secure again. However, even gold suffered a loss during the third quarter. Investors then decided to focus on cash and government bonds even though inflation was higher than the yield; truly a measure of desperate times. The U.S. Treasury 10-year note fell to 1.71% which is the lowest yield since the 1940’s. Inflation is higher than this rate which means investors are incurring a loss either way. The only rationale keeping investors happy is that they will be getting paid “something” in return.

Hedge fund managers are also playing it safe these days. By holding back on using leverage and focusing on cash they are hoping to make it through the long haul. Everyone is turning away from risk while the market is still volatile with memories of 2008 still fresh in their minds. Investors are also turning towards dividends payer in order to keep clients happy.

Finally, since the U.S. almost defaulted, there has been huge uncertainty across the country. With the U.S. and European economies suffering, hope seems hard to find as despair sets in across the globe. Few investors are taking a different approach seeing the market as staying where it is until someone takes a risk to improve it. The current behavior of investors seems only feed the current state of the economy instead of improving it.

Implications of Practice

The downturn of the economy causes many to be losers. Continued job losses and fear about the future are likely to continue to be in the forefront of people’s lives. People who have money in the stock market are most likely losers because the market is turbulent and suffering losses. Investors are losers because despite brokers’ attempts to make good decisions for their clients, they are having trouble making money for their clients. Due to the downturn in the market, investors are more risk averse and making conservative decisions. This could be a reason why the market is not turning around. Other losers are the companies within the market that are actually suffering the losses. They are losing money in their bottom line that is carrying over to losing money for their shareholders.

Potential winners are those who are still willing to take risks to combat the downturn. As most investors become afraid to lose even more money for their clients, they are becoming less risk-oriented. Maybe risks are what need to be taken to put more confidence in the market. I think those who do take risks will be winners in this scenario. Other winners are service-oriented industries. Even though they are incurring losses as well, they are losing less than other industries. This is because consumers would rather spend money to fix appliances and other large items than purchase new ones since they most likely do not have the money for quality products.

Implications for Theory- 3 different implications from the textbook

Stock prices (Brigham 8) are a main issue in this article. Stock prices are continuing to decrease as the market worsens and people are not willing to take the risks they used to which keeps the prices low. The cycle of negativity seems to continue. Prices go down, return on investment is not high, people lose faith in the market, prices go down lower, investors are afraid of risk, and the cycle continues.

Stock market returns (Brigham 46) are another significant point in the article. Investors are not seeing the rates of returns they would like because the market behavior has been dramatic throughout the third quarter. Large increases and decreases provide difficulties to truly understand where the company stands, and if the rate of return will be what is expected. Investors and their clients' main priority is earning a return on what they have given. If there is not a large enough payback or potential payback in the future, they most likely try to get themselves out of the situation.

Risk aversion (Brigham 238) is the primary principle discussed throughout the article. With any investment there comes a level of risk, but the level varies depending on the type of investment and the amount. U.S. Treasury bills typically have a lower rate of risk than purchasing common stock from a company. In today's volatile market, investors are moving away from risk and doing what is a safer bet for their clients. This is a huge reason why the cycle discussed above continues.

Future Direction

In the future, someone will need to take a risk to put confidence back into the market. It will be difficult to make the economy grow if everyone continues to "play it safe." As troublesome as the market was in the third quarter, I would like to hope the fourth quarter made progress as people headed into the holiday season. With great risk could come great reward, or huge loss. However, the trend of playing it safe seems to have little positive effect on the market and peoples' attitudes toward it. I would like to see someone take a risk in order to see the effects. Eventually in the future, the market will turn itself around. Hopefully this will happen soon so that both American and European economies can get back on their feet, and let people breathe a little easier.