Exactly the Wrong Thing

When stock prices are cheap, selling is exactly the wrong thing to do, yet this is precisely what everyone is doing. They are also not buying. Of course, that is why stock prices are going down. What we have today is a remarkable case in the irrationality of markets.

The psychology works like this. Prices decline, people panic, they sell. Prices decline more, people panic more, they sell more.

One might argue - doesn't it make sense to protect against declines by getting out? Why call that irrational?

Selling a stock without understanding its worth is irrational. The way to determine what a stock is worth is to assess the company's profits. Selling a stock at a price dramatically lower than its worth is even more irrational. Why would anyone sell a $20 stock for $10? But they are.

Selling because "you know" prices will go lower is also irrational. In our opinion, no one can predict price movements. What about waiting for things to stabilize? This is just a variation on the idea that one can predict prices. Volatile markets generally don't stabilize until after they have recovered. Witness the 22% stock price jump from November 21 to year end. Was it safe to get back in on 12/31? Apparently not. The next time it might jump 30 or 40% in a month. Will it be safe then?

Of course, media pundits will list all kinds of good reasons why stock prices will go down more, just as they listed all kinds of good reasons why stock prices would go up when they were already high. The new administration's policies won't work. The Fed is printing too much money. We are a debtor nation beyond the point of no return. Jobs are being lost left and right.

In the words of Yogi Berra, it's Déjà vu all over again. Democratic and Republican administrations have both implemented damaging policies in the past. Big companies and financial institutions have gone bust. The Fed has printed too much money. Jobs have been lost during recessions and depressions. Throw in a couple of world wars, and there you have the dark side of US economic history. Yet through it all, corporations have continued to make decent profits and pay decent wages. The primary requirement for them to continue doing so: the continued existence of Western Civilization.

I do not want to sound cavalier about the financial imbalances or debts of our nation. The key is to understand that relative to the size of our economy, they are manageable. We are still wealthy and relatively healthy - an assertion based on economic fact rather than idle hope. One must not confuse a severe economic contraction with the demise of Western Civilization. Assuming our continued existence, we will recover from the current contraction, and stocks will adjust in price to their profits as they always have.

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However, for stocks to rise, sellers will have to throw in the towel. I do not know when that will be. I only know we will not be joining them. The profit value of the stocks we own is demonstrably and significantly higher than the market value reported on your statement. What we really have today is the buying opportunity of a lifetime.

Nick Tompras
March 2009

As of November 4, 2022, we have provided this supplement to accompany the commentary and satisfy changing regulations: https://acr-invest.com/commentary-supplement/

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