Greed Is Never Good

The lure of easy money led investors to speculate on the market movement. As a result, they are nursing their losses now

INVESTING has as much to do with emotions as with hard facts. As stocks keep rising, people urge you to purchase stocks. Seeing your friends making easy money makes you envious and this envy becomes your worst sin.

A bull market also causes 'investors' to lose their sense of perspective. In their rush to earn returns, they ignored the fact that while the sensex had moved from 2600 to 6000 in 30 months, the rise from 6000 to 12600 took less than a year. What was the probability that 'investors' who bought at these levels would make money in the short term? Virtually nil. But this did not deter them from buying. Instead of buying large-caps (which are safer), people invested in smaller stocks, which involved lower monetary outlays.

Let's analyse the future course of investors' behaviour. Nothing has drastically changed in the fundamentals to justify the fall from 12600 to 9500. But the sentiments have changed. Everyone was chasing stocks which were expected to rise, but most of them are nursing their losses currently. People were so greedy that they borrowed at high interest rates and built up their stock portfolios. The losses and rising interest costs will soon frustrate them. The lure of the equity market was so much that people also borrowed to invest in MFs. Now, when the market is falling, financiers are pressing redemptions to recover their borrowings. This leads to a flight of MFs. Investors are now trapped. On the one hand, their portfolio of stocks and MFs is declining, and on the other hand, they have to continuously pay margins and interest to financiers. Hence, investors will develop a loss-aversion, which will force them to shun equities and opt for fixed income securities.


Pic: Nalin Solanki

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The charm of equities is definitely punctured. This sentiment cannot be reversed overnight and we will see a subdued stock market for some time to come. The market may rise somewhat, but investors should not be tempted to jump in. On the contrary, they should discard non-liquid stocks and rebalance their portfolio.

I am not predicting an end to equity investing. But we will have to wait for the excesses to be corrected. Till that is not done, we will see a volatile market. I am still bullish on the Indian market and I maintain that equities are the best asset class, but only if you are a long-term investor. The most important lesson from the current carnage is that investment, by definition, should be with your own funds. If you borrow, that is speculation, which is dangerous. I am sure investors will welcome such times, as they will get good investment opportunities.

The sad part is that the financial and banking industries were so greedy that they induced different types of lending innovations like lending money to invest in stocks, portfolio management schemes and even MFs. Although confined within the framework of the law, this was not expected from FIs.

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