



MONEY DUE REWARDS:



Greg Southwell

Remembering 1987

As most people are probably aware, the Australian sharemarket has had a sensational run over the last 4 years. There is a real sense of exuberance among some market commentators and participants. Without necessarily saying that we are just about to see a re-run of 1987 (it may not happen that way at all), I do think it might be of interest to recount the events on Wall Street during August, September and October of 1987.

The US stockmarket, as measured by the Dow Jones Industrial Index peaked at 2722.42 on 25 August. At the time, this barely made news, since the market had been setting new records almost daily. The Wall Street Journal published a story about this new all time record but it was buried on page 41. The story included the following quote from one trader: "In a market like this, every story is a positive one. Any news is good news. It's pretty much taken for granted now that the market is going to go up".

But the following day the market didn't go up. It began to fall, and continued to do so for the next four weeks. By 21 September, the Dow Jones index had dropped 8.4% from its high. At this stage, however, most commentators believed that the market's fall was only a "correction" and stocks rebounded strongly over the next fortnight as investors bought into stocks which they regarded as "cheap".

By 2 October, the market had recovered to the extent that it was only 3% below its August peak, but on 6 October the market dropped sharply, losing 3.5% of its value in one day. This continued over the next seven trading days until the Dow Jones index had reached 2,355 – some 367 points or 13.5% below its previous record high.

This was not the end however, and on Friday, 16 October there was a further drop of 4.6%. The market closed for the weekend, but it was on Monday 19 October that panic really set in. As the market opened, there were more sell orders than buy orders for many stocks, which meant that trading was delayed. By the end of the day, the Dow Jones index had plunged some 508 points or 22.6% with huge trading volumes. The Dow Jones index, at 1738.74, was some 36.7% below its peak level, less than two months earlier.

It is perhaps not fair to stop the narrative here, because it wasn't actually the end of the world. The market recovered gradually at first, and then more quickly. Six months after the crash, the Dow Jones had recovered by 15%, and after twelve months the improvement was 22.9%. In fact, it was less than two years and two months after the day of panic, on 1 December 1989, that the market again reached its previous high.

So what are the lessons we should all take away from this? The first one perhaps, is to invest on the basis of the underlying value of a share, rather than on sentiment. Another good idea is to ensure that your level of borrowing is sufficiently modest to allow you to "hang on" during any downturn, rather than being forced to sell out at rock bottom prices.

If it does happen to you, don't panic! On dark days like 19 October 1987, many investors would have been tempted to sell up and give up, but in hindsight this would not have been a wise move. A professional financial advisor can assist you in making the hard decisions in such tumultuous times.

Greg Southwell and Dawson & Partners Financial Services are authorised representatives of Lonsdale Financial Group Ltd, an Australian Financial Services licensee. Greg is also a SMSF SPECIALIST ADVISOR™, a CA – FINANCIAL PLANNING SPECIALIST, and a director of Dawson & Partners, a Cootamundra based accountancy and financial advisory firm, which was established in 1913. Dawsons have a division specialising in self-managed superannuation and sharemarket investing. The information in this article is general advice only and has been prepared without taking into account your objectives, financial situation or needs. It is recommended that you should seek professional advice prior to making a financial decision or acquiring a financial product.

SMSF SPECIALIST ADVISOR™ is a mark owned by the SMSF Professionals' Association of Australia Limited (SPAA), and is awarded to individuals who successfully comply with all the initial and ongoing accreditation requirements of the SPAA Specialist Accreditation Council.