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The Financial Panic of 2008 - Lessons from "Groundhog Day"

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Campbell, CA October 30, 2008 — The Stock Market has many characteristics of the '93 movie, Groundhog Day, starring Bill Murray. Bill played a self-centered TV meteorologist named Phil Connors. Phil grudgingly covered the appearance of Punxsutawney Phil, the groundhog, and tried to leave town after the event was over, but was forced to stay due to a blizzard. Phil wakes up the next day only to find that he is reliving February 2nd all over again. Phil relived this same day several times until he learned how to ignore himself and his needs and learn how to love another person. The question we must face is, "Should we keep reliving the 'same day' in terms of our investments or can we learn our lesson as Phil did?"

I have lived through several stock market declines and have seen and heard the same pattern repeated many times. The following shows the general feeling of investors before the "collapse".

> *Many are baffled by the suddenness of the apparent turnaround in the economy. Everything was going up. The job market was great. Housing prices were at an all time high. People were comparing returns on stocks that they had picked. They believe that this is a great period unlike any we've ever gone through before. People had record amounts of equity in their real estate. Everything was great.*

When I begin to hear familiar comments like those above, I get very suspicious. This type of thinking is a "sign of the times" and investor's money should go to the sidelines. And now the "Phils" out there may be forced to learn the market lesson the hard way again.

Investor's concerns are repeated—*Where should I put my money? Maybe I should just hold on until it recovers or until I get back to break even. Then I'll sell!* Let me summarize Benjamin Graham's theory. He was a brilliant analyst, market historian and Warren Buffet's most influential teacher and mentor. He wrote a book about investing in stocks and after personally enduring two market declines, he recommended that his readers shun the stock market entirely and invest in bonds!

Psychological studies have been conducted to analyze investor's decisions during down markets. Recently, Jennifer Whitson of the University of Texas and Adam Galinsky of Northwestern University wrote an article on how the feeling of being overwhelmed changes our perceptions. In one of their experiments, people were first rattled by a computer that gave them unpredictable feedback on their performance at a trivial task, stripping them of their sense of control. These people became much more likely to perceive shapes in a swarm of random dots. "When you sense that you have a lack of control," says Prof. Whitson, "you're much more likely to try twisting and pretzeling explanations and seeing patterns that aren't even there. " In a related experiment, investors who had been stripped of their sense of control by market volatility were convinced that they had read more negative evidence about a company than they had actually seen—and were less willing to buy the company's stock. *In other words, when our sense of control is threatened, we feel the natural urge to pretend that whatever information we do have is more complete and reliable than it is. Imagining that we know what's coming next (even if we think it will be bad) gives us a slight feeling of comfort.*

Now for the practical advice regarding action to take in this kind of volatile market.

First, we have to acknowledge that we don't know the length or depth of this current market decline. These recent events are a historical first for all of us. We have no idea of the long or short term effects of this massive government spending. We do know that this kind of spending is laying the groundwork for future inflation. Government leaders have repeatedly said that taxpayers will have to pay the bill for the billions in rescue money. **Translated that means higher taxes.** We also don't know if the rescue package will work or if more money will be needed. Too much debt triggered our current situation and housing prices are falling. Figures show that we have two years of housing inventory to go through before calm comes to prices in the residential market. A lot of uncertainty exists and that is no friend of the stock market.

An issue that hasn't been addressed amidst all the current turmoil is the looming Social Security deficit and it's impact on the Stock Market. By 2018 [1] Social Security will begin paying out more in benefits than it collects in taxes and will have to begin redeeming bonds from the Social Security Trust Fund ***(IOUs from the government)***. Worse, Medicare is expected to cross that line later this year, resulting in a massive fiscal crisis. The Medicare problem is projected to be 5 times the size of Social Security! On September 30, 2008, the total U.S. federal debt passed the $10 trillion mark for the first time. Adding unfunded Medicaid, Social Security, Medicare, and similar obligations this figure rises to a total of $59.1 trillion.[2]

Many people who come to talk to us have retirement plans, IRAs, and 401(k)s. A decision has to be made. Do you leave the assets where they are and hope that everything gets fixed or should you reposition the assets? If the current world financial crisis is solved, then we have to brace ourselves for spending and printing our way out of the Social Security problems. The reality is that we should expect large financial problems for years to come.

Depending on your personal situation, which you should discuss with your advisor, you might consider moving your stock market assets to a money market/cash position. It makes sense to invest in areas that will benefit from the current problems. You must look at supply and demand factors in today's economy. One clear example would be an increasing demand for apartments due to the following factors:

- Higher down payments and difficulty in obtaining loans will result in a move into apartments for many individuals.
- New construction is down due to lack of construction financing.
- Echo Boomers entering the workforce and increased immigration are expected to swell the number of renters resulting in increased demand.

The result is higher rents and consequently higher apartment values.

There are other areas that now have that same supply and demand factors working in their favor as the above apartment example. You seriously need to look at the stock market and ask yourself if stocks/mutual funds can achieve a similar return. Even if stocks do climb to a higher value, can you get off the roller coaster before the next dip comes? Remember, Phil finally made it past February 2nd!

About AMBAR

AMBAR Financial Group was founded by Barry LeMay in 1976 and is headquartered in Campbell, CA. AMBAR offers §1031 Exchange Replacement Properties, Tenant In

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[1] CATO Institute (2003-03-24)

[2] "Taxpayers on the Hook for $59 trillion", USA Today (2007-05-29)