Black Monday revisted

Many lessons to be learned

By RAY NEUMAN

If you're asked in the year 2000 where you were and what you were doing on Mon. Oct. 19, 1987, the chances are good you will give a very precise answer.

On so-called "Black Monday," the Dow Jones Industrial Average plummeted 508 points, and lost 22.6 percent of its value — almost twice the percentage drop of the Crash of '29.

The TSE followed suit by tumbling 621.27 points or about 17.3 percent of its value on Monday and Tuesday of that week. As people gathered around televisions, radios and evening newspapers, the talk was of an economic disaster and the beginning of a possible new depression for North America and the world.

Yet, the sun came up again. The financial market system held together, and investors learned that they would live to fight another day.

Even now, as financial markets continue to search for direction, it is instructive to put "Black Monday" into perspective as to its causes and its lessons for individual investors.

One important fact often overlooked is that the Dow began its five-year bull run in Aug. 1982 at 777 points, peaking in Aug. 1987 at 2,722 — more than a 250 percent gain.

The 22.6 percent, one-day drop was unprecedented, but represented only one eleventh of the five-year gain. Similarly, the gain for the TSE from its 1982 low to its August. 1987 high was 2,781 points or 208%. The two-day decline in October therefore represented only one-twelfth of the five year gain. This means many long-term investors retained substantial gains even after the tumultuous week of Oct. 19.

The second lesson is how different 1987 is from 1929. Today, most economists discount the possibility of a re-run of the financial collapse that followed the 1929 crash.

The basic reasons are stronger and more alert central banks, the separation of the banking system from the market system, tougher restrictions on margin trading (buying stocks on credit) and the "safety net" of bank deposit and securities account insurance. Each is a result of lessons learned from 1929.

The actual cause of "Black Monday" is more difficult to pinpoint. Most experts identify three key factors:

- massive Federal budget and trade deficits, which have turned the U.S. into the world's largest debtor nation;
- sophistication of global financial markets with computerized trading and new instruments, such as stock index trading, that increase market volatility;
- investor psychology that translated the above factors and lack of action from Washington, D.C., into a panicked stampede.

As for the individual investor, the lessons learned from Oct. 19 were many, and sometimes painful. On the most obvious level, many learned the basic reality of the stock market — what goes up may come down. Many first-time investors had never experienced a significant loss.

Even more investors learned the market can be a perilous place without expert advice. Clients of full-service brokerage firms had investment executives backed by up-to-the-instant information to help them make investment decisions.

In a situation where time literally was money, full-service firms cleared client transactions as quickly as possible, often saving several dollars a share in the falling market. Many other firms' clearing time may have been longer since they had to go through third parties for their transactions.

Lastly, individual investors learned first-hand the value of a diversified portfolio. As recently as Oct. 12, many major firms recommended clients keep 25 per cent or more of their assets in cash or equivalents and a similar amount in fixed income bonds, leaving less than half their funds in the stock market. Those who followed this advice had some solace on Oct. 19.

Looking ahead to 1988, you might wonder if there are any good values in today's markets. The answer unquestionably is yes.

However, more than ever, financial success will depend on a clear understanding of investment goals, advice from a qualified investment executive, and a diversified portfolio of investments.

Ray Neuman is an Investment Executive with McLeod Young Weir in Markham.

Markham executive optimistic

A vice-president with a Markham-based company is advising consumers not to worry about last fall's stock market crash and its effect on the economy.

Predictions of a recession have been overdone, according to Nick Mancini, vice-president, strategic planning, American Express Canada, Inc.

"The economy will grow by 2.5 per cent in 1988," he said citing five factors which will sustain economic growth.

"The G-7 countries have orchestrated the sharpest drop in short-term interest rates in years and long-term rates are following suit. This will lend considerable support to the consumer durables industry," Mancini pointed out.

"And 1988 is a presidential election year in the U.S. which will, undoubtedly, help to keep those interest rates low," he added.

Mancini noted that employment and labor income are at all-time highs providing stimulus for further growth next year. "This mitigates stock market losses which affect relatively small numbers of Canadians," he said.

Mancini observed that the U.S. administration also seems ready to assume fiscal leadership and that financial markets will react positively to a combination of tax increases and spending reductions aimed at reducing the U.S. deficit.

"Observers concerned with any action that appears to reinforce recessionary pressures are assuming that looser monetary policy will not offset what tighter fiscal policy takes away," he said.

"Moreover, a depreciated U.S. dollar is stimulating the U.S. economy."

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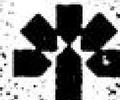

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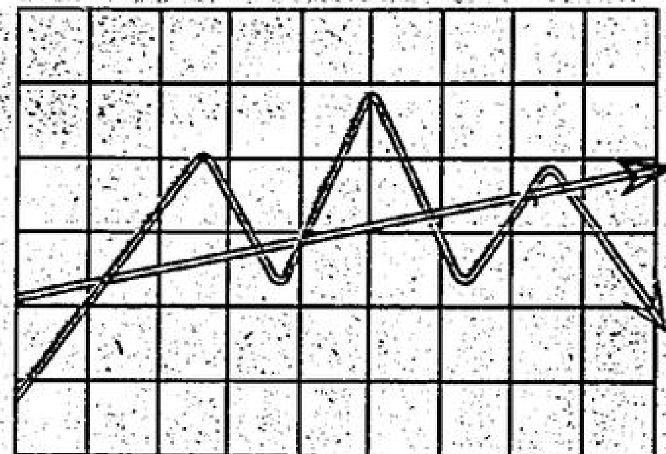

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