Philequity Corner (September 24, 2012)

By Antonio R. Samson

Investible Funds

Economics is subdivided into “macro” dealing with countries and economic zones (GDP, sovereign debt, national budgets, interest rates and money supply) and “micro” dealing with firms and what they produce and how they price their goods, otherwise known as price theory. The emerging discipline of behavioural economics deals with personal economics and what motivates the consumer to spend or save driven by non-economic factors like status, loss aversion, envy, and self-esteem.

A number of local TV programs now feature personal economics, one dealing directly with how to spend your money wisely, say for a wedding (have a cupcake pyramid rather than a wedding cake so that the cake cutting and the giveaways can double up in one cost) and small entrepreneurs with the encouragement of putting up your own business. Featured guests deal with non-intimidating endeavors such as Christmas decors and self-publishing on the Internet (the returns are meager).

There is really no point in giving advice on individual finances if there are no investible funds to begin with.

An individual with a high net worth due to adept management of his savings or retirement pay receives the attention of private bankers. Managing personal wealth is as much a psychological as an economic issue. It is easy enough to compute recurring needs starting with the bottom of the cost pyramid consisting of food, clothing, utilities, and shelter. Still, even these supposedly basic necessities vary in cost. Nutrition is not always the primordial consideration for a meal. Dining in the food court or a five-star restaurant buffet provides a cost gap between haves and have-mores. Clothing is even more obvious, as it goes beyond protection from the elements to a matter of status and a feeling of belonging.

Moving up the pyramid of costs are unnecessary luxuries like travel, art, club memberships, resort homes, and body pampering which includes surgical transformations of one’s looks, more intrusive than the digital alteration of fat celebrities in their billboard alter ego—they don’t even look like twins.

Issues of personal finances affect not just the clerical class or the remittance economy beneficiaries but also those with above average cash flows like successful boxers and entrepreneurs who sell their fast food business. Another Parkinson's Law states that “expenses rise to meet income”. Someone who comes into a cash bonanza or gets promoted to a higher paying job will immediately upgrade his lifestyle and start acquiring durable goods and property beyond even his new income levels. The merely rich also suffer from status anxieties as they get envious of the super-rich.

Problems of personal finances arise from acquired or aspired tastes. Even those in the salaried class who really cannot afford even a small car with its relentless monthly instalment demands, maintenance, repairs, the random accident, parking fees, and gas, long to possess them.

If one does have a significant level of funds to invest, even when entrusting this to fund managers, the saver/investor still needs to know what he's getting into. It's best then to have both personal *and* entrusted investments. The former is best understood by looking into the first-time investor (FTI).

"Buy Low, sell high" is the hoary advice given to first-timers and seems like simplicity itself. After all, one can only make money if the cost of buying is lower than the price for selling. Even discounting the broker's fee and transaction tax this axiom is not easy to implement. High and low are relative concepts. A stock that has been rising in price may still be a good buy if expected to rise even higher. On the other hand, a plummeting stock is not always something to pick up simply because it is getting lower…as it may drop with even increased acceleration like a falling knife.

It is good to have a target return and then sell at that price. In certain situations even buying high and selling low (yes, that's not a typo) can be a rational move to cut losses in a falling market or a stock that has no chance of recovering due to a hit it cannot recover from.

Because the FTI is fond of bragging while doing sit-ups or pole dancing in the gym talking about accumulated paper profits (theoretical gains still unrealized if the stock is unsold), he is especially susceptible to the affliction called seller's remorse. Say, he sells his favorite stock 100% return; does he still continue to track its upward journey to 250%? Sure. Then, his 100% gain now seems puny as the price keeps going up. Remorse, or the feeling of having done something that requires forgiveness, sets in. The opposite of this comes later when he buys the stock back as it rises only to have it correct and go on a dive, right after he buys. Then, his old profit is eaten away along with the principal as he now experiences the opposite "buyer's remorse".

Looking back is dangerous when dealing with the market as is true of most things in life. Get that loss out of the way and proceed to the second round, as they say in basketball. The goal is wealth formation and conservation.

Newcomers like hot tips. On the basis of unconfirmed plans of some pending acquisition, stock buy-back or a follow on offering, a new enterprise in the works, the newbie jumps in and accumulates a particular stock. This corner has discussed the herd mentality and the entry of desperate housewives (not always related) in the irrational exuberance of certain stocks with no fundamentals.

Insider trading, a variation of the hot tip, refers to those involved directly in the company, using unpublished information to gain undue advantage over the uninformed public. This illegal practice is seldom even commented on in the local market but is a serious offense elsewhere.

Nothing is more dangerous for the new stock player as early success. Quick profits from an IPO or a tipped stock with business plans but no cash flow prospects for the next 8 years endows the inexperienced investor with beginner's luck and an unwarranted feeling of invincibility. The danger increases when he outperforms supposedly savvy investors…in the short term.

Low returns from bank placements and even fixed-income securities have driven many savers to the stock market. This is healthy for developing capital formation. The excitement still lies in discovering a company with a small market cap and a good story for the future…without expecting quick bucks.

The best rule to follow is putting priority on conservation of capital before chasing the quick buck. A layup for two points has a higher percentage of success than a three-point shot from half-court. Too much conservatism is not good either. Staying in the sidelines only means you don't get to score.

Investments are personal decisions but should not be taken too personally.

For further stock market research and to view our previous articles, please visit our online trading platform at www.wealthsec.com or call 634-5038. Our archived articles can also be viewed at www.philequity.net.