

# focus



## Investing or speculating?

Overnight we saw the largest drop in equity markets since 13 March. Investors' pursuit of safety has pushed up the price of defensive assets. The yield on United States 10-year Treasury bonds has tightened from 0.95% to 0.65% over the last week (remember, when bond prices rise, the yield on offer falls).

“Although it’s easy to forget sometimes, a share is not a lottery ticket... it’s part ownership of a business.”

PETER LYNCH, FORMER  
FUND MANAGER, AUTHOR

## ...a more plausible explanation is the surge in speculative “investing”...



Media always look for a headline explanation to explain such moves. Today the pullback is being attributed to yesterday's pessimistic economic outlook from the United States Federal Reserve. Others are pointing to the continued spread of COVID-19 throughout the United States, and surges of cases in places such as Texas and Arizona.

The likely reality is though, there isn't a lot of new news in either of these headlines. Certainly not enough to warrant a 6% plunge in the S&P500 index. We believe a more plausible explanation is the surge in speculative “investing” we've seen in markets. Many of these speculators are betting on very short-term (in some cases, hourly!) moves in share prices. Speculative trading has helped the strong recovery in markets off the March lows and can exacerbate market volatility.

Much of this speculation has come from retail investors (rather than professional fund managers). A noteworthy feature of markets in recent months has been the wave of retail trading. We've seen this in New Zealand and overseas. Some people

have been bored and looking for entertainment in lockdown. With casinos closed and no sports to bet on, some have turned to markets to get their “punting fix”. Others are (understandably) seeking an alternative to the near-zero interest rates they're getting in the bank.

### NEW ZEALAND: A SURGE IN TRADING FROM RETAIL BROKERS ASB SECURITIES AND SHARESIES



Source: Iress, Forsyth Barr analysis



...American Airlines has seen an average of 101 million shares traded each day... 23 times the average last year...

Much of this retail interest has focused on the sectors and stocks we'd describe as among the more speculative and higher risk, particularly in a COVID-impacted world. In the United States, Robinhood is a discount broker favoured by retail traders. The ten stocks that have seen the greatest interest from Robinhood clients over the past month include airlines (American Airlines, Delta, Spirit Airlines, United Airlines and Boeing), hotels (MGM resorts), cruise ship operators (Carnival, Norwegian Cruise Lines), and rental cars (Hertz, which has actually filed for bankruptcy protection). Interestingly, Robinhood's demographic – 80% male, average age 31 – is also the segment most likely to bet on sports.

And to highlight the huge volumes of trading – over the past month American Airlines has seen an average of 101 million shares traded each day. That is 23 times the average last year, and with 423 million American Airlines shares on issue it means the full market value of the company is turned over nearly every four days!

UNITED STATES: GOOGLE SEARCH INDEX FOR "DAY TRADING"



Source: Google, Forsyth Barr analysis

Unsurprisingly, these higher risk stocks were amongst the largest decliners overnight.

We believe it's very important to distinguish between investing and speculating. When investing in stocks we think about buying part of a company (ideally at a favourable price). Over time an investor will benefit as the company

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grows profits and pays dividends. A speculator's mindset is different. As legendary investor Benjamin Graham described it: "A speculator gambles that a stock will go up in price because somebody else will pay even more for it".

We do not suggest that investors shouldn't invest in higher-risk sectors. There are good businesses whose earnings do fluctuate with the economic cycle. At times, particularly when the economic outlook appears bleak, the stock prices of these businesses can be attractive. However, resilient investment in these stocks requires thoughtful consideration of a business's prospects and risks, not just hope that someone else will buy it at a higher price tomorrow.



**Matt Henry**  
Head of Wealth  
Management Research

**Understanding that sudden changes in financial markets can cause concern or indicate opportunity, your Forsyth Barr Investment Adviser is available to provide you with advice and assistance at any time.**



*We have begun producing short videos to provide snapshots of key market topics. These will include regular market updates, along with analysis of individual stocks and sectors.*

*You can find these video updates in the Research Video insights section of the website here: [forsythbarr.co.nz/research-library/research-video-insights/](https://forsythbarr.co.nz/research-library/research-video-insights/)*

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