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The Four (Emotional) Stages of a Market Cycle
Greed, Fear, Patience, Confidence

Intense market volatility, the never-ending downward spiral in stocks, the unsettling global economy, the "gloom and doom" talks about another Great Depression (as if recession is a foregone conclusion). Undoubtedly these are challenging times (and not for the faint of heart). These days, most investors are experiencing some form of the "*five stages of grief*" (often all in the same day).

Denial…Heck no, the market is not overpriced. Each selloff represents a great buying opportunity. Dow 20k, here we come!
Anger…How did my advisor not warn me about this? He/she was taking way too much risk in my portfolio. Those darn greedy Wall Streeters and politicos ruined it for mainstream Main Street folks like me.
Bargaining…If only this market would settle down, I promise not to speculate on securities I don't understand ever again. Yes, I said that after the dot.com meltdown, but I really mean it this time.
Depression…I can't quit staring at my recent brokerage statement and it just makes me sick. I can't work. I can't eat. I can't even participate in my weekly golf game or poker outing. Should I liquidate everything?
Acceptance…OK, it happened and there is nothing we can do about it. No use crying over spilt milk. Moving forward, is my portfolio allocated in the most appropriate manner for me and my family? (By the way, are there any good bargains out there in the market carnage?)

Sometimes one just has to laugh to keep from crying (or worse). Virtually all investors (small and large, institutional and retail) have suffered considerable losses over the past months (except of course, for that colleague in the next cubicle who always "claims" to time the top perfectly and is now waiting for the exact right opportunity to reinvest).

Doing Their Parts…

The Federal Reserve and its counterparts at the world's Central Banks have acted in meaningful ways to inject liquidity into the financial system in an attempt to reignite the credit markets and provide businesses with access to much-needed cash. The coordinated rate cuts proved that "no man is an island" and the central bankers will work together to solve this crisis rather than placing blame on the primary culprits (too many to name). The bailout plans across the globe may seem to interfere with the basic concepts of free market capitalism, but experts agree that they were needed to prevent complete and utter global disaster.

And, yet, many of the moves initially were shrugged off by investors who were afraid to go against the bearish trend. Mass redemptions prompted large scale sales of stocks at mutual funds and hedge funds. Employees stopped making those monthly contributions to their retirement accounts. Even the most experienced and long-term investors looked at those brokerage statements with disgust, turned emotional, and sold into the plummeting market. Around the office water cooler, misery sought company (and plenty was available) as individuals shared horror stories about plunging balances, delayed retirements, and lost college funding. They worried not only about their investments, but also their prospects for continued employment and their ability to afford this holiday season. Day in and day out, investors looked for a silver lining. Day in and day out, the panic grew more severe.

How Did We Get Here???

Investors once again find themselves smack in the middle of the *Four (Emotional) Stages of a Market Cycle.*

Greed: Easy money allowed homeowners to buy beyond their means as mortgage lenders took advantage of lax underwriting standards. Likewise, real estate speculators surveyed the strong housing environment and bought additional properties, confident in their abilities to "flip" them in a short time frame for a tidy profit. Wall Street's appetite for subprime mortgage loans and related securities prompted even more speculative lending as risky derivatives were structured and sold to sophisticated (and not-so-sophisticated) investors in search of high yields.

Fear: When the housing market topped out and began its freefall, many property owners soon found themselves underwater in their loans and unable to afford their mortgage payments. Delinquencies, defaults, and foreclosures ensued as banks and other financial institutions were forced to write-down loans and securities on their books. As balance sheets deteriorated, these institutions struggled to keep up their capital bases and were forced to seek infusions from a variety of sources. Some firms were forced into bankruptcy; others were sold to competitors at bargain basements prices. Bear Stearns was the first "beneficiary" of a government bailout, only to be followed by Fannie Mae, Freddie Mac, and insurance giant AIG. When Lehman Brothers went under and Merrill Lynch was merged into Bank of America, the entire financial landscape had changed forever. The credit markets dried up as businesses found few funding sources and worried about making payroll and continue operations. Likewise, employees grew concerned about their jobs. Investors surveyed the landscape and panicked as many long-term industry staples were no longer around. They sold equities of all shapes, sizes, and country markets, and moved to only the safest and shortest of treasury securities. The government bailout plan and other Fed liquidity moves were perceived as mere band-aids as investors entered full-scale capitulation and began comparing the times to The Great Depression.

Patience: Amid the widespread fear and panic, calmer heads must prevail as investors attempt to remove the emotion out of the equation, realize that the Central Bankers are working together to tackle the giant economic and financial mess, and not make rash trading decisions that may regret in the days, weeks, months to come. They must realize that these stimulus moves will not correct these situations overnight, but over time, the global economy and markets will be primed to rebound. Investors should review their asset allocations to make sure their portfolios are structured in the most appropriate manner and ensure that cash positions are sufficient for the challenging times that may be ahead. A few simple budgetary adjustments also may be in order. However, they must also have the common sense and patience to know that they cannot time the markets. When possible, they should try to avoid touching those investments earmarked for five plus years in the future and realize that once they are sold, the losses may not ever be recouped. While many believe a recession is inevitable, the markets are often leading indicators and decline is anticipation of such a slowdown. Further, stocks often rebound while in the midst of a recession as, once again, investors try to anticipate the next market move.

Confidence: To reverse the course of the panic selling, investors must gain some semblance of confidence that allows them to stay the course and await better times ahead. Perhaps they realize that the Central Bankers are working hard to limit the negative ramifications on the global economy. Perhaps they witness someone smarter than themselves (an officemate, Warren Buffett) who decides to stick their toes back into the equity pond and seek out values in the market carnage. Perhaps a political leader is elected who the people believe is better able to manage and oversee the financial system. Regardless of the catalyst, history has proven that investors ultimately overcome their vast fears, develop a little patience, and find renewed confidence in the economy and markets.

A Call to Action

When panic sets in, investors should turn to their trusted advisors to explain the economic and market issues, help them evaluate their portfolios, and suggest any allocation changes necessary to weather the storm.