

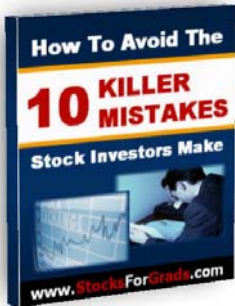
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Case Study - Black Monday (1987)



In the previous post, we gave an introduction of how greed and fear can cause massive havoc in the market.

Today, I'll go in depth, and do a case study on emotions gone wild in the market - and the resulting destructive effect!

Before we touch on that, let me share with you a quote by Sir John Templeton, the legendary investor of Templeton Growth Fund's fame - **"Bull markets are born on pessimism, grow on skepticism, mature on optimism and die on euphoria."**

Wise words indeed!

If you notice, stock market history is a never-ending cycle of boom and busts. And when we speak of busts, few come any bigger than Black Monday 1987.

Monday, 19 October 1987...

That fateful day saw the second largest one-day percentage decline in stock market history. Ever.

The S&P 500 fell 20.5% while Dow plunged by a **monstrous 22.6%**!

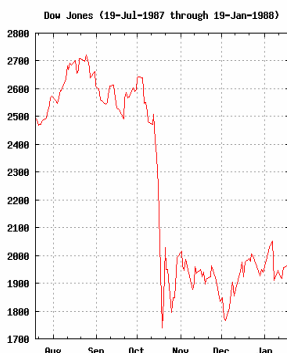
The carnage was not limited to the United States alone. The intense fear and panic was elsewhere, spreading without mercy. Regional markets such as Hong Kong, United Kingdom, Canada and Spain all took crushing losses of an average of 22% by the end of October.

Pandemonium was rampant as fearful investors rushed to exit the market. The huge exodus of cash out of the stock market only served to force the market index down further.

There was chaos everywhere. Traders were spooked. Investors were scared out of their wits. All they could think of was damage control.

Can You See How Deadly Fear Can Be?

It can cause an investor that is usually rational to drop everything in an instance. When market acts irrationally as a whole, there's complete chaos.



The massive sell-off...

If anyone had any sense to stand back from the madness and think calmly for a moment, throughout history, such crashes are usually short-lived.

In such cases where irrational exuberance rear it's ugly head, it is...

The Perfect Opportunity To Make Money!

Look, fundamentals don't disappear overnight. The fact is most crashes are the result of the market acting emotionally as a whole. Sense is thrown out of the window - but for that moment and period only.

Now, if someone just had the presence of mind, to scoop some shares of blue chip companies (think banks with strong government backing) with **rock solid fundamentals at rock bottom price**, how much money will he make when the market recovers?

I bet it will be substantial.

But how many people will actually do that? Very few.

I myself may not do it. After all, I'm also human, and I'm affected by fear just as everyone else is.

All these "long established" theories such as the efficient market hypothesis suddenly don't make sense anymore.

If even professors and high flying managers can make a mistake, where does that leave the average retail investor?

Emotions...

Fear. Greed. Hope. An investor's worst enemies...

When will we ever learn? I guess never, as human nature never changes.

But there will always be someone out there, who is standing calmly outside waiting to make a contrarian move - and profit at the crowd's expense.

The question is - will that be you? Or will you be part of the crowd?

Play It Smart,

Jag Foo

Jag Foo
Chief Editor

StocksForGrads.com



Bottom fishing

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