One Up On Wall Street – Peter Lynch – Lesson 2 – The 1987 Stock Market Crash Explained and 4 Lessons From It

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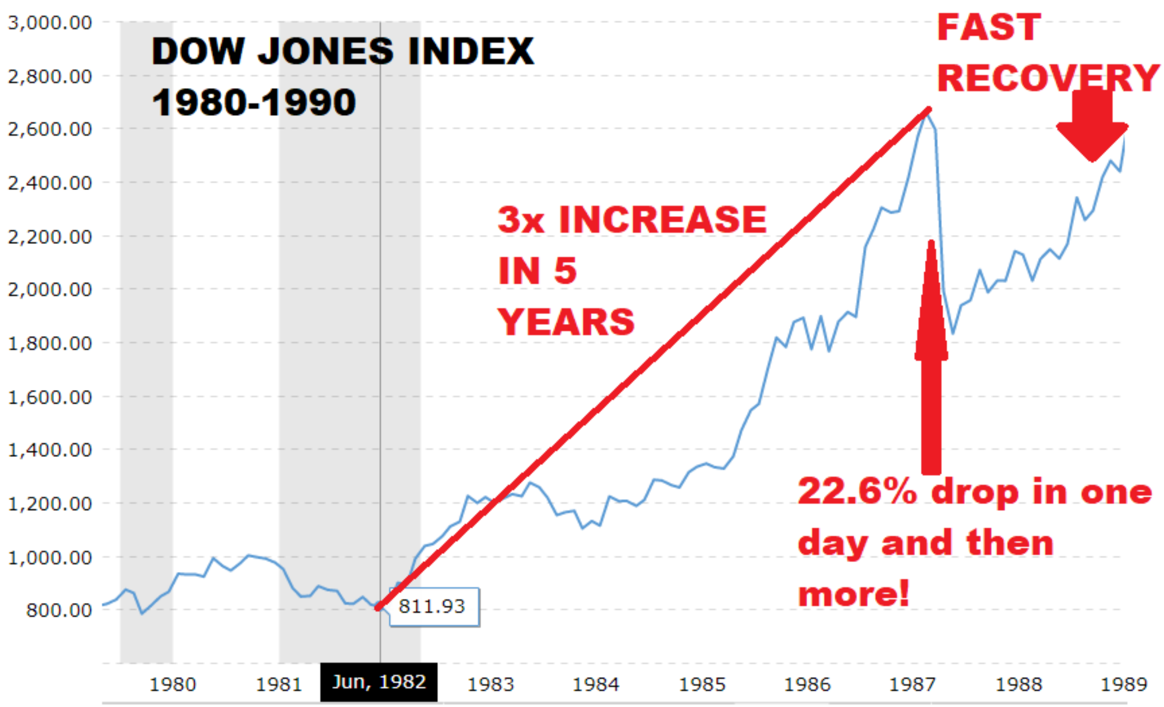
How to invest through stock market crashes

The stock market crash of 1987 happened on black Monday, October 19, 1987 when the Dow plunged 508 points in one day. From 1982 to 1987 the Dow Index jumped from 2,000 points to 6,000 points and when October 1987 came, market panic created a selling spiral that sent the Dow down 508 points in one day.



Dow Jones Index 1987 Crash - [Macrotrends]

The news related to the crash was all about panic, comparing the 1987 crash to the 1929 crash and further putting pressure on the rout.

Peter Lynch's reaction to the 1987 Stock Market Crash

The first funny thing is that Lynch was on holiday while his investors lost $2 billion dollars in one day😊. He was in Ireland visiting Blarney Castle, kissing the Blarney Stone and playing golf.

Later, he was well more on the phone when it started to happen as they had to sell to cater to the 3% redemptions that people asked for. This is interesting because is shows how funds work. In a crash, people panic and funds have to sell to cater for that panic. Therefore, it is not about how great an investor is, it is about how great are the investors in the fund. Only Buffett is protected by this as you can't force him to sell anything withing Berkshire.

4 Peter Lynch's stock market crash lessons

His lessons are the following:

- **"Ignore the ups and downs of the market"**

Something extremely hard to do because we are bombarded with constant news about stock prices and market moves. But, you only have to focus on business fundamentals.

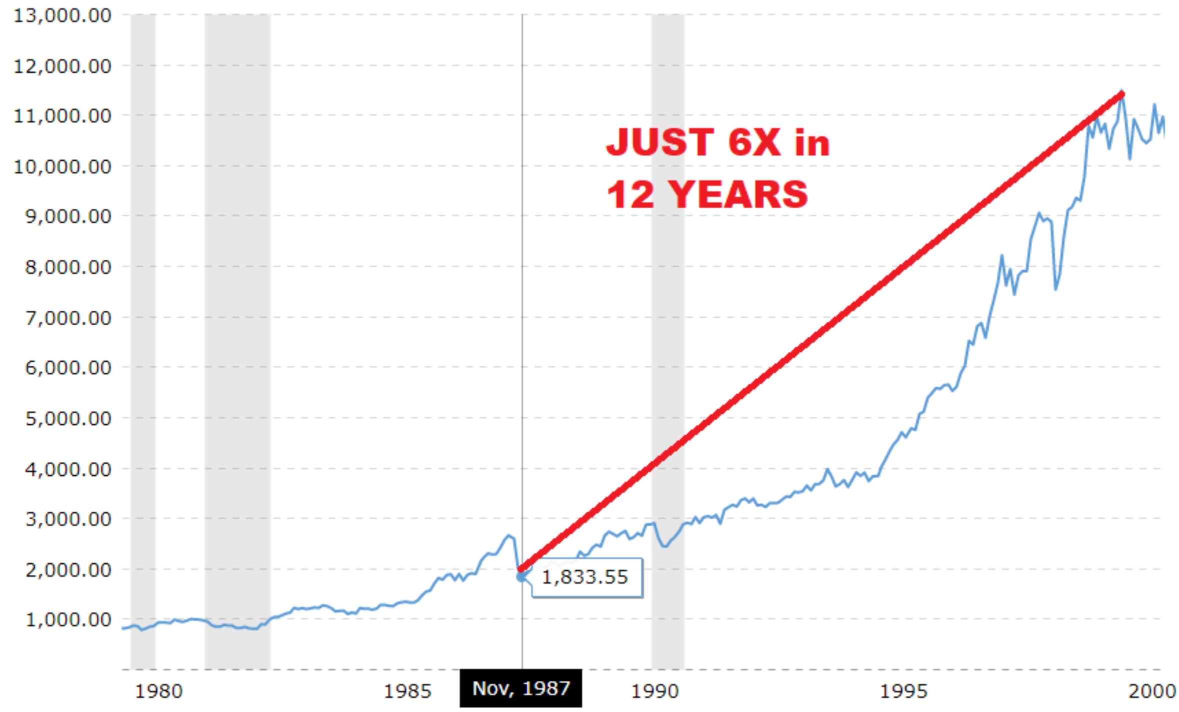
In order to forget about the market and focus on investing in businesses, you should also forget about stock prices.

A funny note from Lynch is that in the 1970s stock market news was hard to find while now, stock market news is hard to avoid. However, market news constantly discusses stock prices and therefore our focus easily shifts from what matters, i.e. fundamentals, to what the market thinks.

To quote Peter Lynch: "When you sell in desperation, you always sell cheap"

- **Stocks go up over the long-term**

The funny thing about the great panic in 1987 is that pretty soon, stocks recovered, passed through the previous high and never looked back. The Dow Jones index went from the 1833 points bottom of the 1987 stock market crash to 10,000 points by 1999.



- **Don't let nuisances ruin a good portfolio**

This is perhaps the most important thing to understand. When investing, you can't predict crashes, but what you can do is to own good businesses that will survive crashes and be better afterwards as the competition gets crushed. Investing is about doing better over cycles, not betting on when the cycle is going to happen.

"Superior companies will succeed, mediocre companies will fail" Peter Lynch

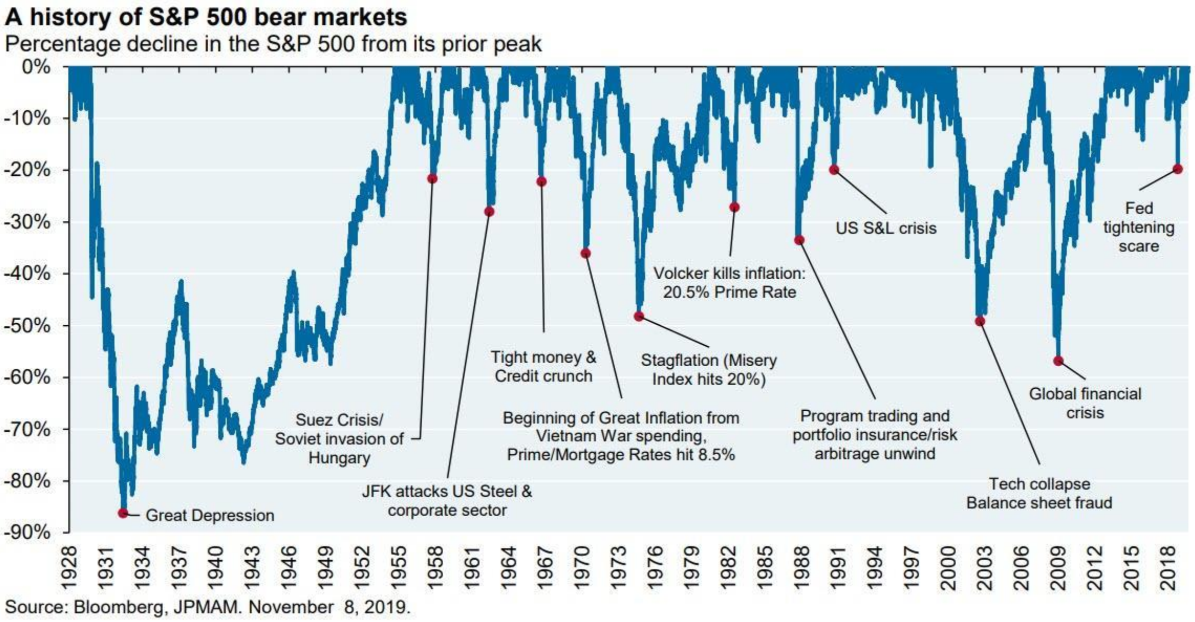
People often sell the stocks that went up most in order to protect themselves from a possible crash, but often the stocks that go up the most are the best stocks in a portfolio.

- **"Both Bull And Bear Markets Don't Last Forever" Peter Lynch**

Stock market crash and stock price

A great fact to know when it comes to investing is the following:

- There is a 10% or more stock market decline every couple of years
- There is a 20% or more stock market decline every 6 years
- There is a 30% or more big stock market crash every decade or so



Source: [Zerohedge]

When you know the above, you can expect that to happen and not do the mistake most investors make which is selling in panic. Don’t try to time the market.

If you have bought a good business, it can crash 30% or more starting tomorrow. But, you need to be patient and, if you bought a good business, not a speculative one, the bear market will be over, and the businesses’ earnings will deliver your investment returns.

Lynch also mentions an interesting thing, as companies prefer buybacks to dividends, investors miss the security a dividend offers in bad times. Plus, in order to make a return, they need to sell the stock, which is again taxed and is not really long-term investing. Just a psychological aspect but very interesting.

All in all, it is about investing in businesses and let those earnings deliver your investment returns.

We will continue with the summary of the book One up on Wall Street and you will learn the following as the book is structured in 3 parts:

- PART 1 – PREPARING TO INVEST
- PART 2 – HOW TO PICK WINNERS
- PART 3 – THE LONG-TERM VIEW