Finance professor in interview

Thorsten Hens: "I still buy shares".

Finance professor Thorsten Hens has learned something from the stock market crises: You have to rebalance stocks. This is now possible again, as it was during the financial crisis of 2007/08, says Hens in an interview with cash.

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Thorsten Hens teaches as a full professor at the University of Zurich and is a member of the Board of Directors of the Institute for Banking and Finance.

cash.ch: **Mr. Hens, the markets have been extremely nervous since the beginning of the year and even six months after the outbreak of war in Ukraine. How do you assess the situation?**

Prof. Thorsten Hens: The market always gets particularly nervous when something comes along that it doesn't know. That was the case with the pandemic, and it is now the case with the Ukraine war. The markets are down 20 to 25 percent, which means that by definition we are in a bear market.

The next, also by definition, would be a 'mega meltdown', i.e. a kind of market meltdown or collapse with declines of 40 percent or more. How likely is that?

Statistically, this is rather unlikely. A 'mega meltdown' has a 25 percent probability of occurring in a bear market. But as I said, that's the statistics. And you can't rely on that, of course.

Turnover on the stock markets has fallen massively. It gives the impression of a 'shock freeze' on the stock markets.

That's right. Which would actually be a sign that we're at the bottom. Shock rigidity is a typical sign of that.

Is there any hope that the tide will turn on the stock markets by the end of the year?

My forecast at the beginning of the year for 2022 was minus 10 percent. Now we are at around minus 20 percent. So I think the market will recover by another 10 percent. Then I would be right on target with my forecast.

As an investor, you could have predicted a number of things for this year, such as the cycle of interest rate hikes, even to this extent.

This is the so-called hindsight bias. Or, to put it more simply, hindsight is always wiser. It was clear that interest rates would rise at some point. The trigger for the rate hikes was certainly commodity prices. Enough liquidity was accumulated during the Corona crisis, and then it needed a spark.

You said in an interview that you were still buying shares at the beginning of February, shortly before the outbreak of the war....

I still buy stocks. I am a rebalancer. I know it's difficult, and you have to go through it at the bottom. But I've been through a lot of stock market crises. In the dotcom bubble, it kept going down year after year. At some point, you're 'out of the game' because you can't buy more. Over three years of buying shares in falling markets - that was very painful, but it paid off. The Corona crisis was almost too quick for that. Many investors missed out on re-buying because the markets went up again very quickly. But now we have a typical crisis like the 2007/08 financial crisis, where rebalancing is good.

Rebalancing, which is mainly done by institutional investors such as pension funds that have to stick to their predefined quotas in equities or other asset classes and then act on market changes.

Yes - that is their typical strategy. But pension funds always have to look at regulation as well. In a bear market, the funding ratio drops, and at some point the regulator could intervene and say that a funding ratio of below 90 percent requires restructuring measures. To avoid that, they also have to protect themselves with appropriate financial instruments, such as out-of-the-money puts. Otherwise, they lose their freedom of action.

Rebalancing a portfolio requires a lot of discipline. Is such a strategy really also suitable for private investors?

Discipline is something you learn with age. When you have gone through several crises, you acquire it.

Many investors blindly buy stocks that have lost 70 percent or more. To what do you attribute this behavior?

We call this the 'anchoring bias'. You know the high price of the share and then think after the decline that this is a bargain. But you have to be careful: At the index level, you can of course invest countercyclically, as in rebalancing, because an index is well diversified. But individual stocks can unravel. I myself once had Air Berlin in my portfolio, as well as Wirecard, and I bought some more. That taught me something: You have to rebalance with indices like pension funds, and not with individual stocks.

Now is also the time again for people who call the stock exchanges casinos. How do you respond?

The stock exchanges are not casinos. The stock exchanges have an economic function. They have to finance the companies, and as an investor you participate in the value creation of the national economy. In the long term, investors get a share premium of between 5 and 6 percent. At best, the short-term fluctuations can be described as a casino. As an investor, however, you must not let them drive you crazy and keep an eye on long-term developments.

A study by a Swiss asset manager claims to have found that women have invested much more boldly and riskily than men this year. If this is the case, do you have an explanation?

A long time ago, we conducted a study with the Zürcher Kantonalbank on this topic. We found out that women who do the housework are much more risk-averse than women who have another job. And these women were, on average, more risk averse than the working men. In other words, the women who are invested in the stock market do not represent the 'average' woman. My wife doesn't invest in stocks either, she invests in real estate, gold, antiques and jewelry, real assets. I can't say that she is worse invested than I am.

By your own admission, you only make four to five trades a year. Isn't that a bit low?

Maybe it's even a little too much, I don't know. It depends on how you are invested. I hold a few passive products, and what is there to trade much?

You describe yourself as a big fan of exchange traded funds, or ETFs for short.

ETFs are a low-cost way to participate. Equity ETFs are suitable for investors who want to diversify their investments. Personally, I think you should use the S&P 500 and not the MSCI World. This always gets me into discussions with many ETF disciples. I just think that the good companies can be listed in the USA, and then you don't have to have the whole world. But I am also a core-satellite investor. So I have a core investment and a few satellites where I think I know more than the others. Hope dies last (*grins)*.

So there is a bit of the trader gene in Professor Hens after all?

Sure. But that's also down to personality. There are people who see it soberly and just want to earn money. But I myself am already too strong in the subject matter from a professional point of view. And that's why I try it once in a while. But only with satellites.

Thorsten Hens is a behavioral economist. He is a professor of financial economics and deputy head of the Institute for Banking and Finance at the University of Zurich. Hens studied at the University of Bonn and at the Département et Laboratoire d'Économie Théorique Appliquée in Paris. His research areas include financial economics and evolutionary finance.
The interview with Thorsten Hens took place this week on the sidelines of the International Structured Products Forum in Lucerne, where Hens was a speaker.