

# 'Indiscriminate panic selling' has taken hold

## NEWS ANALYSIS

Asset prices have been driven to levels lower than justified by fundamentals, writes Stacy-Marie Ishmael

Investor risk aversion in global financial markets has now surpassed levels seen in the turmoil following 9/11 and the collapse of hedge fund Long Term Capital Management in 1998, according to one benchmark.

Sharp falls in shares on uncertainty arising from credit market instability have pushed up the UBS Risk Index to highest point since it started tracking

investor activity in 1998. This is leading to a rush to sell riskier assets and buy into "safe" investments like government bonds.

"What we are seeing now is indiscriminate panic selling, driving asset prices in some cases well below levels that would be justified by fundamentals," said Marco Annunziata, chief economist at UniCredit.

The UBS Risk index takes into account risk indicators such as currency and equity volatility, the performance of gold relative to the euro and dollar, and the spread between JPMorgan's EMBI+ emerging markets index and the US Treasuries.

The index reached 2.53, compared with a level of 2.16 after the collapse of Long Term Capital Management or 2.27 seen in the aftermath

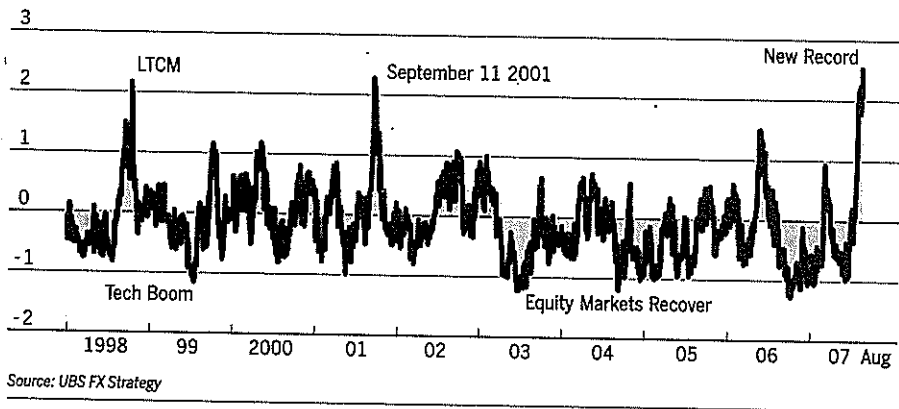
of the September 11 attacks on the US.

While all of the indicators have been flashing red in recent days, "equity volatility is the main source of risk aversion right now", said Manuel Oliveri, a currency strategist at UBS. "But this volatility in equities, which is also spilling over to the foreign exchange market, is a reflection of the problems in credit."

The Chicago Board Options Exchange's Vix index - Wall Street's "fear gauge" - rose to its highest since October 2002, the month when the bull markets in stocks began.

The index measures investor expectations of volatility implied by S&P 500 option prices. Higher readings indicate traders expect bigger share-price swings over the

UBS Risk Index



next 30 days. The Vix entered a new phase this week as it crossed the 30 level, closing at 30.67 on Wednesday.

Yesterday it jumped more than 10 per cent to hit a four year high of 33.86. The Vix is now more than 70 per cent higher than at the start of July.

Jonathan Wilmot, strategist at Credit Suisse, said rising volatility could force selling as models which

measure "value at risk" at investment banks and institutional investors signal a need to reduce risk.

"Actual and implied volatility in asset prices has been in a 'long' trend decline since 2002... But once volatility rises above a certain threshold, it feeds on itself," Mr Wilmot said.

"That is what's happening now, and it feels more dangerous to us than anything we have seen in the current

bull market for riskier assets."

But Mr Oliveri said heightened risk aversion could be seen as a contrarian indicator.

"Historically, the index has never been able to sustain these levels over the longer term," he said. "Usually, right at the point when uncertainty reaches a peak and the market turns very bearish, very negative, the risk index comes down."