

[The confusing investment securities market motion picture](#)

Category : How Stock and Bond Markets Value Investment Securities

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Summary: Securities markets are usually very quick to adjust prices to reflect new information. However, this price adjustment process may take longer and be more volatile, if the new information is ambiguous. At any point in time, market participants will already have used more or less rigorous valuation methods to judge their expected risk-adjusted value of securities. Then, time passes and something new happens. Participants who are aware of the new information must decide whether it will change their perspective and cause them to alter their trading strategy. To most, the result is a very confusing securities market motion picture. (See: [How investment securities are valued -- snapshots in time](#)) This process of reflecting new information in the market prices of securities is known as "impounding" new information. The rate at which information is impounded into prices has increased dramatically in recent years. Only a small portion of potentially interested investors needs to react to change the valuation balance and shift the market price. Significant new information that is generally viewed either positively or negatively will cause some currently active investors to change their trading strategies quickly. Other investors who had been inactive may decide to enter into transactions. If there is a consensus about the meaning of the new information affecting a particular security, its price will change quickly, and that change will tend to persist. Not all opinions are of equal importance to the market. Market participants with more assets will have greater influence on securities pricing. The strength of their willingness to buy or sell has a greater impact on the markets. To execute their transactions, bigger players may absorb all current demand for the other side of the transaction. To execute larger transactions the market price or bid-ask spread may need to shift up or down to induce other participants to trade with them. As other less attentive players subsequently become aware of new information, they too may adjust their valuation. However, because the market price has already adjusted to reflect the change in the information environment, these less attentive players may or may not decide to take action. Because the price has already changed, it may already reflect their revised valuation opinion, and they will remain inactive. Other players may continue to come into the market, but the price may not need to adjust further. The revised price may be sufficient motivation for these investors to take the other side of transactions. In addition, the price could become highly volatile for a time and then will settle down as supply and demand adjust. As the price adjusts, it helps to align the revised supply and demand picture. Eventually, the price will tend to stabilize and fluctuate more narrowly around the newly adjusted price. If the new information is significant, but ambiguous, there could be a more extended period of higher price volatility. The direction and magnitude of the price may fluctuate as participants both sort out what the information means and react to price fluctuations.

These related articles may also be useful to you: [Securities Valuation: ->Introduction to investment valuation and securities risk](#) ->[What is efficient market pricing in the securities markets?](#) [Returns and Risk Premiums: ->Asset class investment risk premiums -- your reward for taking investment risk](#) ->[How stable have common stock equity risk premiums been over time?](#) ->[What explains the recent common stock equity risk premium?](#) ->[How are asset class risk premiums and the risk free](#)

rate of return related? ->What might explain the dramatic rise in common stock equity prices during the 1980s and 1990s? ->How do individual investors' recent portfolio return expectations compare to long-term historical common stock returns and equity risk premiums? ->To estimate the future common stock risk premium, how might individual investors extrapolate from the past? ->What common stock returns might individual investors expect going forward? ->What happens to the expected equity premium, when the common stock P/E ratio reverts toward historical norms?