A dangerous point in the cycle

Bear markets ignore good news and bull markets ignore bad news, but what do highly volatile markets do? They punish any profit shortfall or disappointment by slashing and burning the share price. It has been a harsh pattern of market behaviour, which has been regularly repeated over the past quarter.

The latest to join the list of casualties is online estate agency Purplebricks, which warned on 21 February that its full-year revenues would be £35m lower than expected – between £130m and £140m against previous guidance of £165m and £175m. And the market's response? It marked the shares down severely: 40p – or 24% – to 125p. In March 2018, the management had sold stock to German publishing giant Axel Springer at 360p per share – nearly three times more than the currently prevailing share price. Hell hath no fury like Mr Market when blue-sky expectations turn into a flood of red ink...

Elsewhere, McBride, the own-label cleaning products company, issued an unexpected profit warning on 19 February, just a day ahead of its scheduled interim results, saying profits would be down by between 10% and 15%. The market reacted ruthlessly, marking the shares down by 32% – or 41p – to 89p, harshly discounting in the share price nearly three times as much as the likely profit shortfall.

Plus500, the spread-betting company, sold off heavily when it issued an unexpected profit warning on 12 February and referred to a 'drafting error' in its annual report. It had stated that the company did not generate gains or losses from client trading positions but had lost $103m in 2017 and made $172m in 2018. The shares collapsed by 31%, or 503p, to 1133p. The founders had sold stock worth £256.8m over the past year and the market dubbed Plus500 Minus500.

On 23 January, Metro Bank also issued a profit warning and revealed a mistake in its loan book that knocked its capital ratio. The shares crashed by 39%, or 857p, to 1345p, as the market speculated that Metro may need to raise more capital. It had tapped shareholders for £303m last July and £278m a year earlier, and Mr Market never rates a continuous printing machine.

To no-one's surprise, shares in UK regional airline Flybe collapsed 83%, to 2.9p, on 11 January, after the board recommended a bid at 1p per share from a consortium led by Richard Branson's Virgin Atlantic. This valued Flybe at just £2.2m, a far cry from its IPO valuation of £215m in 2010, but the alternative was certain bankruptcy and wasted fees to lawyers and accountants.

On 17 December last year, stock market darling Asos, the online fashion retailer, plunged 40% – from £41.86 to £25.51 – when it warned of a 'significant deterioration' in trading during November. This sent shock waves through the retail sector – if online champions were suffering, what hope for 'bricks and mortar' operators? Less than three months earlier, major shareholder Aktieselskabet offloaded 2m shares at £56.85 per share, more than twice the price post-warning.

One of the hottest summers on record did nothing to help tour operator Thomas Cook, the shares of which crashed 30%, from 48p to 33p on 27 November, when it issued its second profit warning in as many months. It said profits would be £30m lower than expected and the dividend would be suspended for the year. Hedge funds Marshall Wace and TT International had led the charge of the short sellers, with discloseable short positions well in advance of the profit warnings.

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Mr Market is not in the mood for surprises and none has been greater than that served by cake chain Patisserie Valerie on 10 October, when it warned of 'significant, and potentially fraudulent, accounting irregularities and... potential material misstatement of the company's accounts'. By 22 January, the company had collapsed into administration. In July 2018, the former CEO and CFO had exercised options and immediately sold shares worth a combined £5.26m. They are now under investigation by the Serious Fraud Office.

The moral of this sorry tale? Caveat emptor – 'buyer beware'. It is late in the cycle after 10 years of 'free' money, Mr Market is in a viciously intolerant mood and insiders have been sellers – do not buy.