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**Single Stock Risk:**  
Implications for Individuals and Markets

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**Single Stock Risk**

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“Why Company Stock is a Burden for Many -  
And Less So for a Few”

*Wall Street Journal*, November 27, 2001

## Single Stock Risk - Background

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- ❖ Companies (especially large ones) tend to match 401k contributions in company stock
- ❖ Individuals often purchase company stock with their own 401k distributions
- ❖ SO WHAT! Markets only go up and everybody wins!!!! WHOOPS.....

## Single Stock Risk - Issues

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- ❖ What can (should) an individual in a highly concentrated 401 portfolio do?
- ❖ What implications do these actions have for the market at large?

## **Single Stock Risk - Implications**

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- ❖ Executives with large portfolios have more flexibility and more tools at their disposal
  - ❖ May not be locked up
  - ❖ Above \$2M, custom hedge packages
- ❖ Other employees face difficult challenge
  - ❖ Buying puts is expensive
  - ❖ Single stock futures
  - ❖ Relaxation of restrictions

## **Single Stock Risk - Implications**

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- ❖ Large, publicly-traded companies tend to match 401k contributions in company stock
  - ❖ Concentrations over 80 percent not uncommon
- ❖ Throughout the 1990s, these firms enjoyed high P/E multiples so stock matching was “cheap”
  - ❖ Fewer shares need to hit a certain dollar target; also saves cash
- ❖ Selling pressures on high P/E stocks the other side of the coin

## Single Stock Risk - Implications

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- ❖ Admitted crude analogy
  - ❖ Expiration of “lockups” on Initial Public Offerings (IPOs)
- ❖ Price pressure on firms with largest concentrations of shares in defined contribution plans
  - ❖ Unlike IPOs, however, these companies tend to have very large public floats
- ❖ Do employees rebalance with “similar” firms thus offsetting the pressure?

## Summary

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- ❖ Some relief from trading restrictions is likely
  - ❖ Companies will balance costs and benefits of having employees worried about concentrated portfolios
  - ❖ Threat of regulation
- ❖ Employees flooding out of concentrated portfolios will keep selling pressure on large-cap firms
  - ❖ Large cap P/E ratios still very high
  - ❖ Rebalance with diversifying assets