

The Markets

We're only three weeks into the New Year and already some very interesting trends have developed in the markets. Consider these four:

1. **The worst performing stocks in 2011 have been the best performing in 2012.** The 50 worst performing stocks in the S&P 500 in 2011 were up a whopping 11.2 percent YTD 2012 as of last Wednesday. By contrast, the 50 best performing stocks in 2011 were up only 2.1 percent so far in 2012. What a difference a "turn of the calendar" makes!
2. **U.S. Treasury securities are off to their worst start in nine years.** With improvements in the employment situation, housing sales hitting an 11-month high and a reprieve in the European debt problem, investors have less need for conservative treasuries and a bigger appetite for riskier stocks, according to Bloomberg and CNBC. At the moment, investors seem to be saying, "risk on."
3. **U.S. stocks rose for the third consecutive week and are near a six-month high.** Despite a decidedly mixed start to the 4th quarter earnings season, stocks are up nicely since their October 2011 low. Of course, too much euphoria could lead to disappointment later.
4. **The CBOE Volatility Index (VIX) declined nearly 22 percent in the first three weeks of this year.** The big decline in the VIX suggests investors are less fearful about near-term market volatility. In fact, the VIX is down to a seven-month low. While the markets may be calm now, we're not complacent.

Trends come and go in the market, but one thing that remains constant is our diligence in helping you achieve financial independence.

WHY IS IT THAT CONSERVATIVES TEND TO WATCH FOX NEWS and those with more liberal leanings tend to watch MSNBC? Psychologists would tell us it's because of what they call "confirmation bias." Confirmation bias is the tendency of humans to seek information that confirms an already held belief or opinion and to avoid or discount information that might contradict an existing belief or opinion.

This concept also applies to investing and it's very important to **avoid** it as much as possible.

For example, let's say we're really bullish on the U.S. stock market. If we let confirmation bias cloud our judgment, then during our research, we would tend to read the reports that support our bullish view of the market and let that reinforce our decision to be bullish. By contrast, we would tend to avoid reading the reports that are bearish, or, if we do read them, we would come up with reasons why they were wrong.

When one is under the spell of confirmation bias, it's easy to miss turning points because of being stuck on a current belief or opinion that won't change even when contradicting evidence presents itself. That, of course, would be bad for your long-term wealth.

How strong is the confirmation bias pull?

A 2009 meta study published by the American Psychological Association reviewed 91 studies in the area of confirmation bias and concluded that **people were nearly two times as likely to seek information which supported their existing view than to seek information which contradicted their current view.** That's a strong pull!

How do we overcome this pull?

Here are two keys that could help:

1. **Acknowledge that confirmation bias exists.** Knowing that it exists helps us try to avoid falling into its trap.

2. **Actively seek contradictory opinions.** This is another way of asking what could go wrong with an investment and then doing our best to ensure we understand the “other side of the coin.”

So, in addition to making a “rational” case for an investment, we have to make sure we avoid letting psychological biases get in the way.

Weekly Focus – Think About It

“If you take emotion – would be, could be, should be – out of it, and look at what is, and quantify it, I think you have a big advantage over most human beings.” --John W. Henry, trading advisor, principal owner of Boston Red Sox

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Notes

The Standard & Poor's 500 (S&P 500) is an unmanaged group of securities considered to be representative of the stock market in general.

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Past performance does not guarantee future results.

You cannot invest directly in an index.

Consult your financial professional before making any investment decisions.