What Should A Rational Investor Do Now?

We believe behavioral finance is the most important ingredient in successful investing. When asked what the secret is to Berkshire Hathaway's investment success, Charlie Munger replied, "We have tried to remain sane when others like to go crazy." Having a strategy that keeps you focused on long-term results and out of short-term, tactical and emotion driven reactions is vital to your investment (and possibly mental) health.

The marketplace provided multiple reasons to make one feel discouraged last week. The one week declines in the S&P 500 Index, the Dow Jones Industrial Average, and the Russell 2000 Index were respectively: 1.25%, 1.79% and 2.57%. In addition, the headlines are full of confusing stories regarding interest rates, profit forecasts and geopolitical mayhem. As opposed to the tactical perspective that all of this noise is new information and requires a new response, *our perspective is that there is more continuity than disruption in this and staying on course is the right thing to do.*

Going back to last November, the S&P 500 Index has traded in a fairly narrow range, pivoting around a 3.0% variation from 2050. At this moment, the quote on the S&P 500 Index is 2100, a variance of 2.4% from that 2050 pivot point.

The market has been flat for an appropriate reason, in that earnings have been flat. In 2014 the S&P 500 Index earned just over $118, and the consensus estimate for 2015 is now $119. Earnings are flat due to mostly technical reasons relating to the strong dollar and weak energy prices. The economy and most businesses are plenty healthy. A rising market needs fuel in the form of valuation or earnings. We believe earnings will rise in 2016. We make an unremarkable assumption that valuation will stay on this plateau, and we will get a modestly higher market over the year ahead. The marketplace will continue to provide rewarding opportunities for equities.

Here are our most important takeaways from this market backdrop:

- Do not change your long-term strategy based upon short-term discouragement or emotions;
- Focus on selectivity and unique business merit; do not be a generic investor in the market;
- Stay vigilant about risk management, attuned to the risk of a big, cyclical change in the economic cycle, but do not shift to a more defensive posture now while the data remains so constructive.

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612.340.0181 / 800.345.8745