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Markets Do Not Always Make Sense

Good news is great news and bad news is good news, or so it seems when looking at the stock market these days. **In the financial news, it is difficult to avoid a story discussing how the market has de-coupled from economic and medical reality.** Financial writers, with deadlines to meet, are in a never-ending search for bits of data to support the bullish market momentum. Their readers tend to hang on every word, desperately seeking some logical explanation for something that appears to have no logic. **We have to realize that sometimes, there is no ‘reason’, at least not a reason that is easily discernable at the time.** However, intuitively we desire an explanation or an answer immediately, especially easy answers, and once we grab those answers we tend not to let go.

Easy Answers Can Sound Logical, but Are Often Not Answers at All

One of the items we’ve recently seen used to explain recent market action was the ‘cash on the sidelines’ which will continue to drive equity prices higher. This is one of the most overused excuses for market movements ever conceived. In his recent monthly commentary, John Hussman, President of Hussman Funds writes:

*“As I observed early in the global financial crisis, you’re going to see a lot of chatter about “cash on the sidelines” in the months and years ahead. That’s because the Federal Reserve is creating a mountain of the stuff. The moment the Federal Reserve creates base money (currency and bank reserves) to purchase some asset, the base money it creates must be held by someone in the economy, at every moment in time, until it’s retired. A dollar of base money is just another type of “security.” **A given holder of cash can try to get rid of it by buying other pieces of paper like stock shares or bond certificates, but the seller of the stocks or bonds immediately becomes the new holder of the cash. (our emphasis.)***

So “cash on the sidelines” can certainly change ownership, but it can’t go “into” the stock market, or the bond market, or anywhere else, without coming right back out in someone else’s hands. Once a security is issued, that security has to be held by someone, at every moment in time, exactly in the form it was issued in, until that security is retired. That holds for base money as well.”

The full text (and a worthy read) can be found [here](#).

Cognitive Dissonance and the Pandemic

Our note will be very short this morning, but with the above in mind, we invite you to read an article from The Atlantic, titled “[The Role of Cognitive Dissonance in the Pandemic](#)”. We think this is an excellent article and one with repercussions in many other areas, including investments. **Our view is that to be a successful investor, one needs to be well practiced in promoting cognitive dissonance, as well as avoiding cognitive ease, in their decision-making.**

What is Cognitive Ease?

An example that most of us can relate to is greeting a puppy. If you walk into your yard and see a puppy, it will typically generate cognitive ease. You are familiar with puppies and realize that there is little to fear from a puppy and your brain relaxes. It does not feel threatened. However, if you stepped into your yard and saw a leopard, that would promote cognitive dissonance. That leopard should not be there and it is dangerous. **Cognitive dissonance puts us on guard when something unfamiliar comes along and our brain works harder to protect us from a potential threat. Cognitive ease relaxes our guard when we are faced with the familiar.**

Naturally, we tend to seek things that generate cognitive ease, and cognitive ease can be created by simply hearing the same thing over and over, even if we know it isn't true! This is a very good explanation for the success of “targeted news channels” like CNN and FOX. Our brains naturally desire cognitive ease, so we watch what we agree with! Searching for cognitive ease can be problematic for an investor. When markets are moving up, we experience cognitive ease and we are happy to come up with excuses why it will continue to move up, rather than focus on issues that create cognitive dissonance and may help us make better investment decisions. **Our natural desire for cognitive ease works against being a successful investor, so we need to be cognizant of our bias. This is a reason why it can be extremely helpful to have a second voice at the investment decision table. It can prevent us from believing that there is “money on the sideline”.**

Here is a link to a [short video](#) that explains cognitive ease and cognitive dissonance. We believe you find it both useful and entertaining, but also informative as it relates to investment decision-making.

Last week's market news and activity

My team and I compiled a summary of insights below to help you better understand key aspects of last week's market news, performance and key articles on advanced planning. We hope you find this quick-read format helpful for putting recent news and developments that affect your finances into its proper context. In addition, every Monday we will be updating our charts on our [WEBSITE](#) for you to review. Please feel free to e-mail or call with any questions that you may have.

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