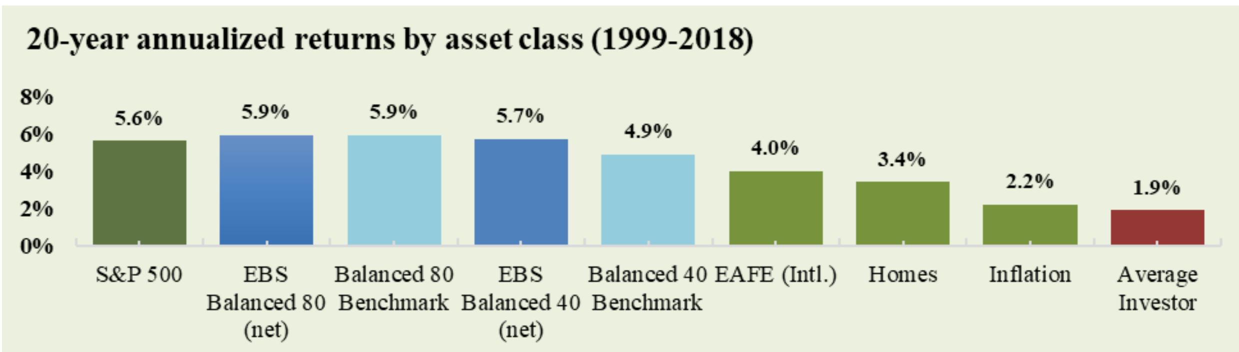
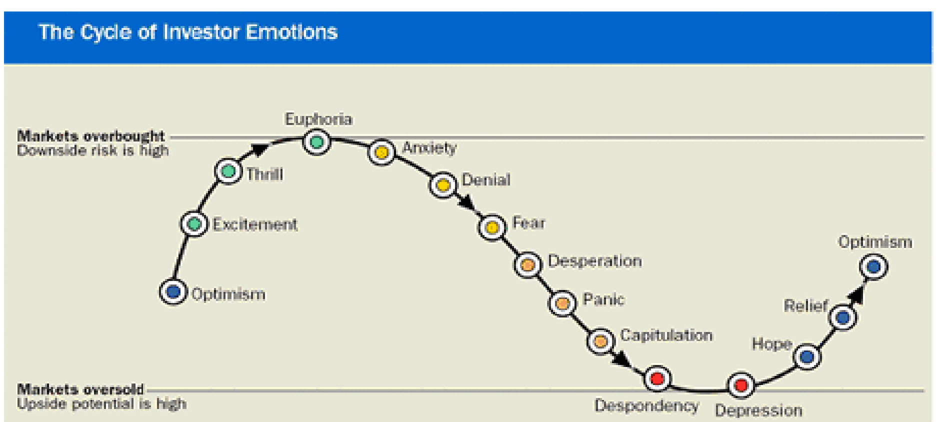
EUBEL BRADY & SUTTMAN
ASSET MANAGEMENT

A Fire Drill for Market Volatility - Will You Self-Inflict Unnecessary Wounds?
Part I: Behavioral Psychology

We start this series by focusing on behavior, specifically the behavior of the average investor.[1] Behavior is arguably one of the top three factors in achieving long-term investment success in publicly traded stock and bond markets. Not convinced? As shown in the following analysis, **the average investor lags even inflation over the last twenty year period** (including the longest bull market in U.S. history).[2]



So how can the "average investor's" poor outcome be explained? Simply stated, blame it on the Amygdala nuclei found in the temporal lobe of the brain. This portion of the brain is known for its role in processing fear. When stimulated, emotions are triggered creating a perceived need to act in the form of fight or flight. For investors, flight takes the form of selling at a time when prices are contracted. Rather than taking advantage of a buying opportunity, the average investor may be locking in a permanent loss of capital at a time the market is becoming less expensive.   Similarly, the average investor's emotions can be triggered to act over a fear of missing out, leading to buying at a time when prices are quite expensive.



Seeking Alpha: The Dangers of Following Celebrity Stock Picks, June 26, 2014

[1] Source: financialsymmetry.com   The average investor is best described as a person attempting to time the market intentionally or unintentionally based on emotional influence.

[2] Source: J.P. Morgan Guide to the Markets - U.S. -3Q 2019 - As of June, 30 2019, Page 64 for all data with the exception of EBS Balanced 80 and EBS Balanced 40 net and benchmark returns. Please see important disclosures attached regarding the EBS Balanced 80 and EBS Balanced 40 composites. Other indices used are as follows: EAFE: MSCI EAFE, Homes: median sale price of existing single family homes, Inflation: CPI, Average asset allocation investor return is based on analysis by Dalbar Inc., which utilizes the net of aggregate mutual fund sales, redemptions and exchanges each month as a measure of investor behavior. Returns are annualized (and total return where applicable) and represents the 20 year period ending 12/31/18 to match Dalbar's most recent analysis.

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Unlike most other financial transactions in one's life, the average investor typically ignores the market when it's having a Black Friday sale. Instead, euphoria and fear cause the average investor to buy when investments are most expensive and sell when investments are at a discount.

We believe an understanding of behavioral tendencies, both of human nature and of the average investor, is vital to investment success.

1. **Be Mindful of Your Natural Behavior:** Some of you have taken a survey we utilize in our business that measures natural behavior and provides insight into how humans formulate decisions. Understanding natural behavior helps us to work collaboratively with our clients to communicate effectively and manage potentially negative emotional reactions. If you would like to take this simple survey and receive feedback, we will be happy to send one to you.

2. **Plan Ahead Based On Your Decision Making Tendencies:** Many investors tend to make decisions more subjectively or emotionally, as opposed to objectively or logically. While emotional intelligence is important, an investor who is prone to react to emotional stimuli like volatile markets may detrimentally follow their gut as opposed to a predetermined strategy based in logic.

3. **Recognize and Avoid Cognitive Biases**[3]

    - **Overconfidence:** Many overestimate their own abilities, knowledge, and skill, tending to place too much belief in what they think they know. This can result in anchoring on an initial uninformed estimate of value.

    - **Representativeness:** Focus on a recent memorable event rather than overall odds. After a stock market correction, people often invest in bonds despite overwhelming historical evidence that stocks significantly outperform bonds over time.

    - **Framing:** How a concept is presented to us matters. An investment is more appealing if framed as if it may double in price versus one that has upside potential but could go to zero.

    - **Confirmation bias:** Seek information that supports our belief. When we want something to be true, we unknowingly spotlight the things that support it, and then draw conclusions.

We invite you to discuss the concepts addressed in this piece with us and to participate in the complimentary survey to gain a deeper understanding of your behavioral tendencies. Through knowledge, education, and support, our goal is to help you avoid self-inflicted wounds and strive to enhance your chances of achieving better long-term investment results than the "Average Investor".

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[3] Behavioral Finance – Jay R. Ritter University of Florida