

Honestly: When Disloyalty Is Going

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WASHINGTON—For some who track insider stock transactions, few qualities are more admired in a company executive than previous acts of disloyalty.

For example, some consider recent insider buying at Activision Inc. particularly auspicious because the buyers are many of the same people who, not long ago, were large-scale sellers of company stock.

Jonathan Moreland, director of research at Insiderinsights.com, says the recent buying is more credible as a signal because Activision insiders have shown they are willing to sell shares

when the price is right. "It's obviously a case where these guys are in it for the money," he says.



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Insider buying, he says, can sometimes be explained by an executive's desire to be loyal to a company rather

than his or her desire to turn a profit—making those transactions less useful as a signal. "Some insiders can be cheerleaders," Mr. Moreland says.

Eight Activision insiders reported buying 539,750 company shares in the final two weeks of 2002—shortly after the company cut its earnings guidance and the stock plummeted. Those insiders included Chief Executive Robert A. Kotick and Chairman Brian G. Kelly, who reported paying a total of nearly \$7.2 million—or an average of \$13.32 a share.

Shares of the Santa Monica, Calif., videogame maker were at \$14.67, down 15 cents, in 4 p.m. trading on the Nasdaq Stock Market. Company officials were unavailable to discuss the transactions.

Five of the insiders who bought in December—including Messrs. Kotick and Kelly—had sold nearly 2.5 million shares previously in 2002, with almost all of those sales concurrent with the exercise of stock options, according to data compiled by Thomson Financial.

Those executives' previous sales took place at \$26.08 a share to \$34.02 a share, according to Thomson Financial, and the concurrent options exercises took place at \$4 to \$16.67 a share.

Michael Painchaud, research director for Market Profile Theorems, says there has been a long history of stock sales at Activision—but almost no buying until December.

"In this case, it's a clear reversal of the pattern in the past," he says. Like Mr. Moreland, Mr. Painchaud says such reversals are "worth more" when assigning importance to the current transactions. "That's why it's important to have a historical perspective on insider behavior," he says.

In selling high and buying low, insiders are imitating the recent behavior of the company itself.

In June, Activision announced it had raised net proceeds of \$247.8 million—about \$33 a share—with the sale of 7.5 million company shares. In October, the company announced it would spend as much as \$150 million to buy back shares. It was unclear how much, if any, of that buyback has taken place.

Mr. Moreland says a company's purchases and sales of stock, like those of insiders, send a signal about how the company views the value of its shares. "Management should only be selling shares if they think they are getting a fair offer for them," he says.

The recent insider purchases began after Dec. 17, when Activision lowered its earnings forecasts, leading to a 19% drop in the stock price the next day, to \$12.71 a share from \$15.73. The company, whose games include the Tony Hawk, Spider-Man, Doom and Quake titles, attributed the revision to weaker-than-expected holiday sales, citing tighter inventory management by retailers and a shift in consumer demand toward well-established brand-name products.

Activision said it now expects to report earnings of 60 cents a share on \$362 million revenue for the quarter ended Dec. 31. The company previously had projected earnings of 82 cents a share on \$435 million revenue.

The company's revision led to a raft of downgrades the next day as the stock plummeted, but one analyst, Morgan Keegan &

Co.'s Bob DeLean, took the opportunity to upgrade the company to "outperform."

"To me, at that point, the bad news was out," says Mr. DeLean.

But Mr. DeLean dissents from the views of Messrs. Moreland and Painchaud, saying he regarded the previous sales as tarnishing the current purchases. "Take the insider buying with a grain of salt," he says, "because these guys unloaded a bunch of stock in the upper 20s and low 30s."