

## Insiders' Bearish Sentiment Hits Record Level Despite Stock Gains

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A widely followed indicator of insider sentiment plunged to unprecedented bearish levels during October, indicating pessimism for the fifth-straight month, even as the stock market remained aloft.

With the October data almost completely tabulated, Lon Gerber, Thomson Financial director of insider research, said company insiders sold stock valued at \$59 for every dollar's worth purchased. Mr. Gerber's company considers any reading higher than 20 to 1 bearish. The previous record was 41 to 1, in May 2001.



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"The million-dollar question: Why is that? I wish I had an answer," Mr. Gerber said.

Using a variety of methods of analysis, trackers of insider data began reporting a bearish turn in sentiment in May. According to Thomson's data, the four months since June have been among the five most bearish months during the past five years, yet the Dow Jones Industrial Average has risen more than 9% since July 1.

Michael Painchaud, research director for Market Profile Theorems, said his company first advised caution in mid-June based on insider data. Since then, he said, he has weighed and rejected the argument that insider data no longer foreshadow the market trend.

The tendency to discount the significance of insider sales is a result of the movement of the stock market in recent years. Because the market declined from April 2000 through early this year, some are saying insiders never had a chance to exercise their underwater options, meaning the exercise price was higher than the market price.

The current negative sentiment among insiders, according to this argument, is merely the product of a pent-up supply of insiders' stock and doesn't re-

flect pessimism about the market.

One counterargument is contained in the data from Thomson. Mr. Gerber said the unprecedented sales-to-purchases ratio isn't primarily the result of heightened sales. "Buying is extremely below normal," he said.

Mr. Painchaud said he continues to trust the bearish message from the insider data because it is backed by other indicators, including his company's proprietary measure of market sentiment.

Market Profile Theorems tracks data on newsletter writers, professional investors and small investors, and the extreme recent bullishness among these investors is a strong negative sign for the market, Mr. Painchaud said. "If everyone is bullish, everyone can't win," he said. "That to me is confirmation that you should take insider behavior at its word right now."

Jonathan Moreland, director of research for Insiderinsights.com, said he believes insider sentiment is best used as an indicator of the fundamental soundness of a stock or the market—and the current market rally isn't based on fundamentals.

Unsustainable economic growth, combined with "outrageously accommodative" Federal Reserve policy, has sent stocks higher and confounded insiders' expectations, Mr. Moreland said. Something has to give: Either the Fed will acknowledge the strength of the economy and raise rates, or the economy will pull back. Either outcome would validate insiders' concerns, he said.

Mr. Moreland's answer, in part, is that he and other analysts of insider transactions aren't advocating that investors short the market. Even in a market on the verge of a downturn, he said, insiders still can steer investors to stocks worth buying, and he remains net long because he continues to rely on the signals sent by the rare insider buyers.

But he has recently increased the amount of his short positions based on insiders' continued negativity: "It's a warning light on the dashboard as we're zooming down the highway to recovery."