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View from inside often is different

Bill Barnhart | Market report

As the fourth-quarter financial reporting season winds down, the results and outlooks, as well as analysts' reactions to what companies are saying, do not make you want to rush to buy stocks.

But before you head for the sidelines, it's useful to consider who else is playing.

Company insiders, through public reports they must file with the Securities and Exchange Commission when they buy and sell shares of their companies, frequently offer a perspective that differs from official company statements and Wall Street analysis.

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As for the fourth quarter, which ended Dec. 31 for most companies, corporate profits were the worst in six years.

Earnings of the Standard & Poor's 500 companies, weighted by their size in the index, are expected to be down 20 percent, largely because of losses in financial companies.
Twenty-six percent of S&P 500 companies failed to at least match the average earnings-per-share estimate of analysts, up from a normal rate of 20 percent. The miss rate for financial-services companies was 57 percent.

Retailers whose fiscal years end Jan. 31 have yet to report, but could be a source of more trouble.

Looking forward, the number of companies issuing positive forecasts is at the lowest level of the decade, according to Bespoke Investment Group. Analysts are following suit, by lowering their estimates of results for the first and second quarters of 2008.

"We're seeing pretty significant cuts for the first two quarters," said John Butters, an earnings analyst at Thomson Financial Research. The S&P 500 earnings growth rate is expected to be just 0.8 percent, down from an estimate of 5.7 percent on Jan. 1, Butters said.

This time, it's not just the big bad banks that are getting hit in analysts' growth forecasts of earnings per share. With the exception of utilities, all major stock market sectors are getting the ax, according to Bloomberg News.

Michael Painchaud, research director of Seattle-based Market Profile Theorems, tracks insider trading as a contrary indicator to Wall Street analysts' earnings projections. (You can see more on this stock picking method at http://www.mptonline.com.)

"It is a consistent theme where a company will get hit [by analysts] in terms of earnings," Painchaud said. "Either it fails to beat estimates or the analysts downgrade estimates. It leads to a stock price weakness, and who steps up [to buy shares]? Insiders."

For example, in the last four weeks analysts have turned sour on the outlook for first-quarter profits in the semiconductor industry, according to Bloomberg data. Earnings-per-share estimates for the group have dropped 5 percent.

Yet, on a scale of optimism from 1 to 10, insider buying in the semiconductor industry scores a 10 this month, a sharp turnaround from recent months.

Semiconductor-makers such as Intel, National Semiconductor and RF Micro Devices have seen the analysts' forecasts of their profits decline, while insider buying has turned upbeat.

On the flip side, insiders at utilities generally are not impressed by Wall Street's positive outlook.

"The analysts are too bullish, and the insiders are concerned about the aggressive positive attitude of analysts," Painchaud said. "The market is enamored of this group, but the insiders are not."

Two examples are FPL Group and Energen. On the other hand, the comparison varies widely among utilities. Chicago-based Exelon appears to have robust insider support despite weakening analyst optimism toward the company's coming results.

Buy/sell factors that motivate top company officers and directors and others regarded as insiders are complex. In some cases the ability of insiders correctly to buy low and sell high is no better than the average investor. Taken at large, however, optimism or pessimism by insiders to a company's stock can be a useful tool in making stock selections.

In that regard, it's worth noting that one of the most enthusiastic buyers among corporate insiders, according to Painchaud's analysis, can be found in what is currently the worst-regarded sector of the market: financial services.

For example, Citigroup scores a 9 on the insider buying scale and a 1 on the earnings scale.