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Jack Sirard: Close-up on insider trading

By Jack Sirard -- Bee Staff Writer

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Insider trading -- the legal kind -- has been quietly but assuredly gaining strength on Wall Street.

The good news for investors is that it's shifted from the sell side to the buy side of the ledger.

Michael Painchaud, who has built a business on tracking insider trading, says the market turned in a most unlikely sector at an unusual time.

"We first saw the change in the technology sector back in early July," Painchaud says.

That, of course, was just as the market was tanking in one of its worst months in recent history.

The Seattle-based investor says the system that he has developed over the past 13 years keys on insider trading to point to both buying and selling opportunities, and it flagged the tech sector as strong as it could be.

Painchaud examines every insider transaction filed with the SEC, ranking insider activity for each stock on a 1 to 10 scale.

Instead of looking at the shares bought and sold, he also considers such factors as the buyer or seller's past prescience, his or her title, and the transaction size.

"We use a scale of 1 to 10, with 10 being bullish. Tech jumped up to a 10 after being flat-lined at a 1 or 2 for months," he says.

Painchaud says that when his research firm, Market Profile Theorems, made its call advising investors to begin moving back into tech stocks, "we were derided by those who were still saying that the end of the world had come in the

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sector."

At that time, the overall market was taking a horrific beating, falling below 8,0000 for the first time in four years.

Interestingly enough, he says that the downtrodden telecommunications sector, which includes Nortel, Nextel and AT&T, has seen the most aggressive insider action.

Painchaud takes insider trading analysis further than most. It's not merely a case of buying and selling shares, he says.

"It also can be the more discreet ways an insider acts. For instance, if their normal bias is to be a net seller of company shares upon receiving their options, not selling can be very telling. It's a change in their bias."

Painchaud uses insider trading to chart the future course of stocks over the ensuing two to six months and says that when it's as bullish as this signal, the gain can be 15 percent to 20 percent.

He says that the overall stock market did not turn bullish until Aug. 3, when he warned investors to reduce their cash to zero and to use the market's weakness to do some selective buying.

The investment adviser says that he's seen seven similar buying signals since 1994 and although the market already has had a decent run, investors can anticipate further gains.

Among the stocks that Painchaud has found a positive move in insider buying are IBM, which he says saw its first insider buying in more than a year.

He also says that stable names such as Sealed Air, Andrew Corp., American Express, Bank One, Baxter International, Beckman Instruments, Bell South and Occidental Petroleum have had positive insider trading.

This shift to bullishness is the first since a shift recorded in the first week of October 2001, which presaged a rise in the Dow from 9,119 on Oct. 5 to 10,635 by March 19, 2002.

Sacramento money manager Dan Seidman says that while insider trading can be a useful tool for investors, "they need to look at each buy and sell.

"For instance, when you see that Bill Gates has sold 1 million shares of Microsoft, you have to understand that this is part of his regular program to sell shares to diversify his holdings. It doesn't mean that he's bearish on his own company."

But, he says, if a CEO or another top officer has suddenly made a number of purchases, it can be a buy signal.

The good news is that more and more investment data bases are providing insider trading information based on SEC filings. That gives individual investors an edge that they didn't have just a few years ago.

Personal finance chat -- Sacramento financial planner Pamela Christensen and I will be hosting a Webcast on financial planning at noon Wednesday.

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Christensen, former president of the Northern California Financial Planners Association, has been a financial adviser since 1993 and specializes in cash flow and budgeting and beginning investors.

We'll be answering questions about financial planning, investment strategies, money management and getting the most out of your 401(k).

Bee readers are invited to post their questions before the event and then check back that day to view answers to selected questions. Questions may be posted at forums.sacbee.com/sirard.

About the Writer

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