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Stocks Still Steep for Insiders

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Although some analysts think stocks are cheap after a monthlong slide, corporate insiders seem to disagree.

After the recent big drop in the major averages, several analysts have declared that stocks are now attractively priced. Indeed, the price-to-earnings ratio on the **S&P 500** is currently sitting at an eight-year low, and many technology stocks have seen their multiples contract sharply.

"According to our valuation model, equities are precisely as undervalued as they were overvalued in December 2000," wrote TrendMacrolytics analyst Donald Luskin in a recent note.

The S&P is now trading at 17.6 times trailing 12-month earnings, the lowest level since 1996, according to Merrill Lynch. And Luskin said the technology sector is "as undervalued as it's been at any time since the October 2002 bottom, and is undervalued even relative to the standards of the conservative pre-1996 era."

Some companies seem to think their stocks are a bargain, too. However, plans to buy back stock don't always come to fruition, and the recent actions of corporate insiders suggest this might not be such a good time to get into the market.

Jonathan Moreland, publisher of the newsletter *Insider Insights*, said his weekly insider buy/sell ratio ended last week at negative 80%, indicating that there were 80% more companies seeing insider sales than insider purchases.

"There were only 178 companies with buyers, and 320 with sellers," he said. "This hardly represented insiders jumping out of the woodwork to take advantage of obvious bargains."

The **Nasdaq** fell 1.8% last week and is down almost 11% since the end of June. The S&P 500 also fell more than 1% last week and just closed at a new low for the year, as investors worry about decelerating profit growth, high oil prices and the possibility of rising interest rates.

"If insiders fail to step up more convincingly in the midst of further market weakness, it would be yet another ominous sign for the market," said Moreland.

Michael Painchaud, director of research and principal at Market Profile Theorems, said the ratio of insider sales to insider purchases has come down since the start of the year, but he noted that a further decline is necessary before a buy signal can be triggered.

"We have not received any confirmation that insiders believe, in the aggregate at least, that they should be buying their own companies' shares," he said.

And insider selling remains heavy right now, according to David Coleman, editor of *Vickers Weekly Insider Report*. Looking at the total number of transactions, he recently found 3.57 sales for each purchase, which is well above the neutral zone of 2.50 sales for every purchase. "I think [the market] is still overvalued," he said. "I'm still bearish."

Painchaud did note, however, that some sectors are seeing more bullish action than others. "We're seeing improvement in technology and we're seeing degradation in finance," he said.

Since corporate insiders, like directors and officers, tend to have more knowledge about their companies and their companies' prospects than anyone else, it can pay to follow their lead, said Coleman.

Insider buying and selling has "been a consistent, long-term reliable indicator," he said, noting his model portfolios have soundly beaten the Dow Industrials over the past 20 years.

As for companies that are beginning to see their shares as a bargain, Internet service provider **EarthLink** (ELNK:Nasdaq) said Monday that it would buy back another \$100 million in stock. Last week, **Clear Channel Communications** (CCU:NYSE) said it intended to repurchase \$1 billion worth of its common shares over the next year while **Microsoft** (MSFT:Nasdaq) said it would buy back \$30 billion of its stock over four years.

"As we looked at our cash-management choices, our priorities were to ... increase our stock-buyback efforts, given our confidence in the company's growth prospects," said Microsoft CEO Steve Ballmer.

Walgreen (WAG:NYSE) , **KeyCorp** (KEY:NYSE) , **Federated Department Stores** (FD:NYSE) and a number of other firms have also said they will step up purchases of their own shares.

So far in July, there have been 24 announced buybacks, amounting to \$36.5 billion, according to Thomson Financial. Buyback announcements are down so far this year compared with the same period in 2003, although the dollar amount of the transactions has increased.
