



# Prosperity Dispatch

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## COMPANY INSIDERS ARE TELLING YOU TO DO THIS NOW

October 8, 2009

Insiders are dumping shares at record pace.

So is it time to sell?

After all, no one knows a company better than insiders. They see the day-to-day operations, the sales figures, expenses, and everything else. They know their business better than anyone else. Their business is what they do every day.

So it makes sense to track when insiders are buying and selling their own shares. Buying is bullish and selling is bearish, right?

Well, it may be. But if we take a look at history, it's not as clear cut as many analysts make it out to be. More importantly, the insiders are teaching us one very important lesson that will go a long way to making you a more successful investor.

### Insiders Rush for Exit

The recent rally has presented many investors the opportunity to take some money out of the markets. Insiders have jumped at the opportunity.

TrimTabs research has found that insiders unloaded \$6.1 billion worth of stock in August. That's the highest rate of insider selling in 16 months.

More importantly, insiders haven't been buying much either. Trimbabs also found the ratio of insider selling relative to insider buying has surged to 30-to-1. That's the highest the ratio has hit in five years.

Charles Biderman, the CEO of Trimtabs, pointed out in the *New York Times* that, "You have a classic case of greed stampeding investors into believing that nirvana is at hand. We just don't see how the market's going to last."

But what does massive insider selling really tell us?

### The Truth About Insider Buying and Selling

We know there are plenty of [stock market myths](#) which are perpetuated over time to match whatever the market sentiment is. Insider selling might be the myth *du jour*.

Thankfully, insider selling has had a long track record to which we can see whether it's something to be concerned about now.

For instance, I recently came across this *Associated Press* report:

*Rampant Insider Selling Raises Red Flags*

*Major Corporate Execs, Including Some from the Homebuilding Industry Are Dumping Stocks - Serious Predictor of a Coming Crash*

You'd think it was a recent headline. There's been a recent wave of insider selling, homebuilders have been big winners, and fears of another crash are still high.

It is, however, from December 2004. That was over a year before the peak in housing. And it came at a time when the S&P 500 was at 1200 and almost three years before its recent peak at well over 1500.

In more current times, insiders haven't been very trigger shy about pushing the selling button either. Back in June *Bloomberg* reported: Insiders exit at the fastest pace in two years.

Here we are two months later and the market has held up exceptionally well.

On the other side, insider buying isn't always bullish either. For instance, corporate insiders in the retail sector recently saw a big "opportunity" to load up on company shares.

Bloomberg reported: [Insider Buying of Retailers, Led by Dillard's, Climbs](#):

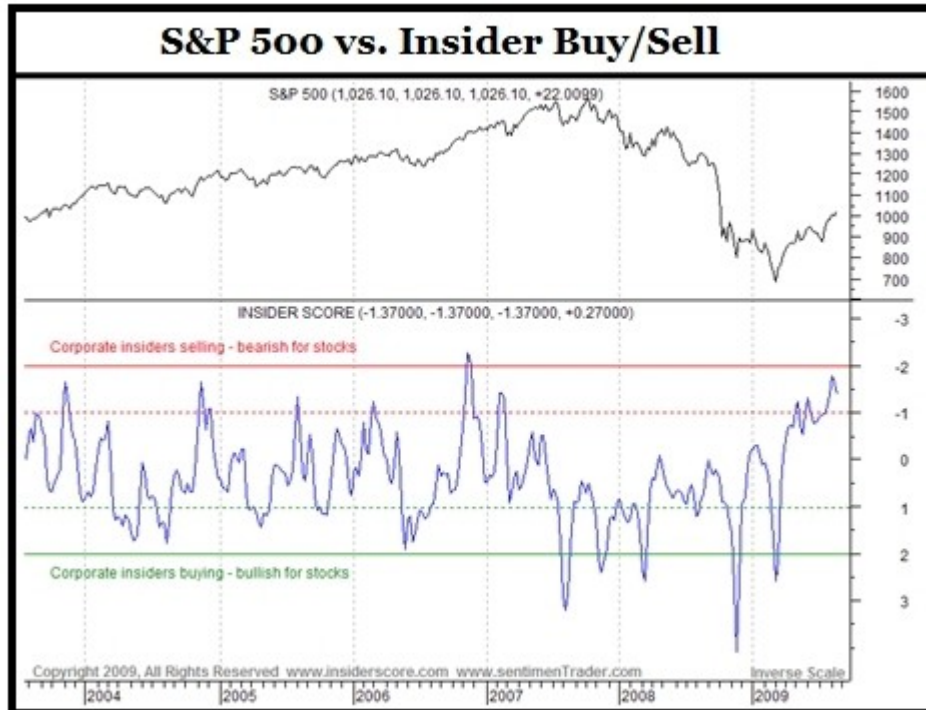
*Consumer confidence is falling, the odds of a recession have risen, analysts predict the worst holiday shopping since 2002 -- and retail-industry executives are buying their companies' shares like never before.*

*Limited Brands Inc. Chief Executive Officer Leslie Wexner and eight other executives bought a record amount of stock last month after prices fell to a four-year low. Dillard's Inc. director Warren Stephens made the biggest insider purchase ever as shares of the Little Rock, Arkansas-based department store chain headed for the steepest decline since at least 1980.*

A lot of retail executives saw opportunity, but this article is from December 2007. That was two months into the official recession. And the moves haven't proven to be very wise since. **Dillard's (NYSE:DDS)** went on to fall 75% and is still down 40 from then. The retail sector as a whole has been lagging well behind too.

Of course, these examples are just that – examples. They're hardly enough to define a true trend.

The chart below from [Sentimentrader.com](#) shows a much better picture of the trend and the relative importance (using that terminology very loosely here) of insider buying and selling as an indicator for the overall market direction:



### Investing 101: Let History Be the Judge

As you can see, insider buying and selling trends have been very volatile over the past decade. There have been plenty of times when insider buying and selling is at the right time *and* at the worst possible time.

This time should be no different. The wave of insider selling and lack of insider buying may be a warning sign. It may simply be what it always has been: something to be aware of. Or it may be even more proof that the majority of company insiders are just like the majority of investors, really bad.

There is one thing we can learn from company insiders though...

### Did Enron Teach Us Nothing

That's to stay diversified.

When company insiders buy their own stock, have the majority of their 401K's tied up in company stock, and have their jobs, insurance, and salaries tied to one company, they are not well-diversified.

This is what those tens of thousands of Enron employees went through. Most of them had bet big on their own company. No one was complaining when Enron's shares nearly tripled in two years, the company was printing stock options and shares for employee 401Ks, and salaries were rising.

Most everyone in the company was highly leveraged...and loving it. Eventually, as all investors do eventually learn, the ups and downs are only more severe when you're not diversified. Most folks with families and bills just aren't prepared for the risks.

So I think the same way when I hear about how corporate insiders are selling out in droves. It's more likely most just relearned the value of diversification the hard way. Now they are trying to salvage what they can.

You know my take on the markets since April: don't bet against it until it starts going down. So right now is not likely a good time to sell out, but if you're sitting on a few big winners, it could a good time to get more diversified.

Good investing,

Andrew Mickey  
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