

## An Insect's Guide to an Upbeat Market

By Mariko Gordon

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If you don't actually live in Manhattan, you may dismiss it as a barren, concrete jungle. As a longtime resident, however, I can assure you that would be a mistake.

Beyond the less than delightful sightings of pigeons as big as chickens and rats as big as sumo wrestlers, New York offers many magical "Animal Planet" moments: sparrows nesting in the crossbar supports of traffic lights; ginkgo trees turning bright yellow and dropping their leaves all at once; and the cricket that hung out in the locust tree outside my window, all summer long.

I grew quite fond of that cricket.

I'd check-in with him every time I walked in or out the door and listened for him through the open window in the evening. So besotted was I that I even changed the alarm-clock sound on my phone to cricket chirps.

Big mistake. Here's why...

Last week, while on a business trip through the rural Midwest, I checked into a hotel that at first appeared totally normal. And it would have been, except for one thing. Deep in its ventilation system there lurked a ninja cricket.

Every time I'd fall asleep, the ninja cricket would start chirping and wake me up.

It wasn't a loud noise, but it didn't matter. Thanks to my cricket alarm clock, I had thoroughly conditioned myself over the summer to wake up at the sound of a raspy, insectoid chirp.

At that point, the only difference between me and Pavlov's dog was a tail. No matter how much I ordered my brain to file the ventilation cricket noise under "Ignore, Will Robinson" it insisted on filing it under "Wake up, you jackass!"

For sure, sleeping in 20-minute snatches made for a VERY long night. But just to prove that nothing is ever wasted (even a bad night's sleep), it did get me thinking: if it's this hard



to sort out the signal from the noise with *insects*, we hardly stand a chance when it comes to figuring it out from the market news flow.

The confirmation bias is a well-known behavioral trope, one that has shipwrecked many a sell discipline. It states that we are wired to ignore information suggesting we are wrong and only pay attention to information that tells us we're right.

Good investors know this and compensate by obsessing over the risks associated with a holding.

And there are many - bad stuff happens all the time and blows stocks up. Anything from plagues (the last avian flu scare infected chicken stocks) to people (more than one rogue trader has brought down the bank) to governments (whole industries are legislated out of existence with a pen stroke) can cause a stock price to plummet in an Acapulco swan dive.

But when there's *nothing* but bad news, you need to change the ring tone on your alarm clock, making up for the fact that sometimes we investors can get *over-fixated* on the risks and show an anti-confirmation confirmation bias, so to speak (not unlike a Watergate-ian "non-denial denial").

In other words, we can be so concerned with our tendency to *ignore* bad news and hold on too long that we overreact in the other direction, flinching at every chirp of the "bad news cricket," as it were.

The same can be said for company-specific news; it's never the *last* earnings downgrade that makes a bottom in a stock. The first downgrade rattles, the second spooks, the third flushes out the last of the weak holders. Every downgrade thereafter is already in the stock. The chirp has gone out of that cricket and the absence of incremental, new bad news is good news in and of itself.

This is also true of the market itself these days. One of my favorite market prognosticators is Michael Painchaud of [Market Profile Theorems](#). We've been getting his research for eons now, and he's not only thoughtful, but seemingly always right.

Painchaud is seeing glimmers of good news ahead:

1. The market has already taken it on the chin - sentiment is very negative;
2. Insiders are buying hand over fist;
3. The rate of change in reported earnings has stopped declining.

Take a look at the graph below showing the rate of change in reported earnings growth versus the market. If the market continues to swoon while earnings growth flattens and

starts to rise as in the spring of 2009, Painchaud would chirp like crazy to get up and get going long.



[Click to enlarge](#)

There, that's my gift to you, whether you're a New Yorker or not - a market cricket whose more upbeat chirp may be the one worth heeding.

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*Mariko O. Gordon is founder, CEO and CIO of Daruma Asset Management, a NY-based small cap investment management firm. Subscribe to her free monthly e-newsletter On Daruma's Watch [here](#).*

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