Market Dynamics

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Performance Management System

Don't Fight The Tape

Portfolios heavy with under-performing stocks almost never outperform the market.

Ignat's Law

"There are three kinds of lies: lies, damned lies and statistics."

Mark Twain

A collection of recent newsletters is available on the web site.

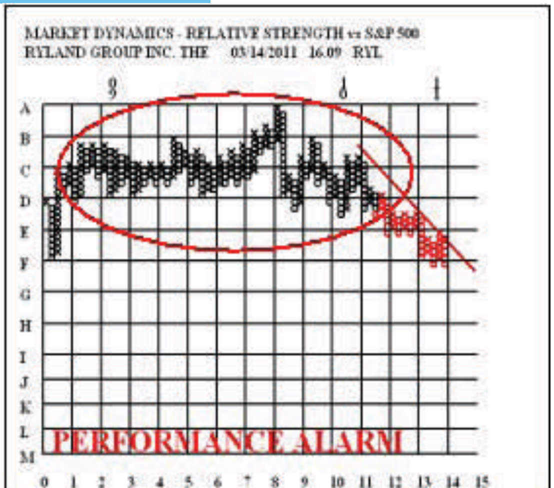
The TPARC report is a daily report that covers the long-term relative strength trends on stocks with a change in an analyst's investment rating. Almost daily, over the past six years, these reports have covered stocks that received an upgrade to "buy" in the face of a persistent downtrend in relative strength. These are examples of an analyst engaged in "fighting the tape."

The timeless advice to avoid fighting the tape has been repeated by investors for years. The simple conclusion is that a stock with a persistent long-term downtrend is best avoided. In other words, the ticker tape is usually right. But how can the tape be random and yet be right on the trend of the stock's performance?

There is little doubt that the movements of the stock market, day-to-day, are random. That implies that the stock market fluctuations are unpredictable. Randomness does not require the distribution of stock price changes to conform to a pattern of changes with a zero mean.

In the case of a stock with a persistent long-term downtrend, the distribution shows a large negative mean, although a histogram of the daily tock price changes will conform to a bell shaped curve that implies randomness. There seems to be considerable confusion regarding the randomness of stock price movements and the existence of long-term trends. The random walk tries to make the case that stock prices don't trend, and yet, relative strength stock charts show trends are very common and a pervasive feature of the stock market.

The advice to "not fight the tape" is based on the experience of



RYL - Rating change from "neutral" to "buy."

Breakout below a major congestion. Remains below the 45-degree bearish resistance line. Backing away from resistance. Massive overhead resistance. Resistance will probably turn it back down. Performing poorly. Limited upside potential.

many investors who have learned the hard way that the persistent long-term trend of the stock ticker tape is usually right. And yet, many Wall Street analysts are constantly recommending the purchase of stocks with confirmed, persistent long-term downtrends.

Are they unaware of the existence of the downtrend in the price of the stocks they rate as "buys?" Or are they in the camp that believes that trends don't matter because the stock market is random.. The randomness school is correct that stock price movements are unpredictable and yet persistent long-term trends seem to continue as if they were predictable. This is the fundamental difference between a process that produces a random output and the ability of that output to follow a trend. From a practical point of view, investors are better served by the advice "don't fight the tape" than to assume that trends of the ticker tape don't matter.

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