

The Stock Market and the Media: Turn It on, But Tune It Out

By Dick Davis

Investors are faced with a daily barrage of business news. There's keen competition over who can break the story first. The clear inference is that the news matters—that keeping abreast of the news, especially as it relates to one's holdings, is one of the keys to investment success.

I disagree.

I believe one of the worst things that can happen to a long-term investor is to be instantly and totally informed about his stock. In most cases, spot news fades into irrelevance over time.

What's relevant is what the market decides to do. The news follows the market, not the other way around.

The Media's Mis-Focus

One big challenge faced by individual investors is dealing with misleading information. The financial media's inept handling of news is a constant irritant to me. Perhaps I'm overly sensitive because, unlike most business reporters, my background is in stocks, not news.

The media's lack of insight in reporting financial news is on display 24/7, but it is most glaring on big move days. On Thursday, July 26, 2007, the Dow Jones industrial average fell 450 points. It had been on a tear most of the prior year, climbing over 3,000 points from mid-July of 2006 to mid-July of 2007. During that steady rise, stocks climbed the typical "wall of worry"—growing weakness in the sub-prime lending and housing markets, worsening borrowing condi-



tions, slowing economic growth, and so on. The Dow reached a historic high of 14,000 on July 16, 2007, but in the following week reversed itself with a vengeance. It suffered one-day losses of 149, 226 and 208 points. But the big hit came on July 26, when the Dow plunged 450 points to its low, closing down 311 on huge volume.

On that evening's news, the media struggled with explanations. The News Hour with Jim Lehrer on PBS is among the most prestigious, reliable news sources on the air. I rarely miss it. Jim Lehrer, Gwen Ifill, Ray Suarez, Margaret Warner, Judy Woodruff, and Jeffrey Brown are all consummate professionals. On the night of July 26, award-winning 30-year veteran reporter Ray Suarez asked his two guest experts to explain why the stock market plummeted that day.

The choice of guests—two economists—negated from the get-go any insightful answers. It reflected the misguided thinking of all media everywhere: That a meltdown in the market must be tied to the news of the day. Interviewed were Thomas Lawler, a housing market consultant, and Diane Swonk, chief economist for a financial services firm.

Since the news that day revolved around housing and credit problems, these were logical choices—except for the fact that the market is illogical. For a full 10 minutes, both guests spoke eloquently about what they know, which is not the stock market.

However, nothing that they said could not have been said the day before, the week before, or the month before. They were never asked, "But why today?"

This same inadequate explanation was repeated by media outlets throughout the country. Reasons were given by everyone except those who have insight into investor behavior,

the complexities and randomness of the stock market, and the futility of trying to reduce explanations for the market's actions to one or two factors. Reporters who didn't know were asking analysts who didn't know. The result was a public that didn't know. But none of the parties knew that they didn't know.

But Why Today?

So, why was it that by 2:40 p.m. on Thursday, July 26, the Dow had lost 450 points—when the news background was exactly the same as it had been a week earlier when the Dow topped 14,000? In fact, the same bad news on the credit and housing markets had been dogging the market not for days or weeks, but for months.

What was there about this particular hot summer day in July that suddenly caused frenzied selling with news that had been ignored for so long?

The answer, of course, is that no one knows. But since the news that day was “old hat,” it's reasonable to assume something else was going on. Based on behavioral studies, if not just plain common sense, it's likely that investor emotions played a role—probably a dominant one. Fear and greed are highly contagious. Both are quickly activated by sudden, extreme price moves. The intensity of the selling and the steepness of the decline make investors believe that their worst fears are about to become a reality. As prices plunge and momentum accelerates, their instinct is to sell to protect profits and limit losses.

In other words, a major catalyst for the carnage is the unnerving action of the market itself.

Non-News News

Part of the problem is that, while some news does involve sharp and sudden stock reactions (only when it involves surprise), most of the never-ending flood of daily news is routine, insignificant and meaningless in terms of durable impact. It is important to PR firms, journalists, TV reporters and traders because it gives them a means

of making a living.

But to the long-term investor, it is little more than filler and noise.

I'm talking about news of quarterly earnings, most acquisitions, litigation, layoffs, product recalls, strikes, management changes, broker buy and sell recommendations and upgrades and downgrades, short interest, insider selling and so on. Then there's the non-stop stream of statistics on the economy.

These news topics are all important—they are what shape the underlying direction of a stock and the overall market. But there are few news stories that, standing alone, have long-term significance. What's important is repetition or the lack of it. The long term is made up of a lot of short terms. When one news story, let's say a report of higher earnings or a decline in the trade deficit, is confirmed or negated by the next news release and then the one after that, we begin to get a trend with some possible long-term consequence. Sometimes it takes years for such a trend to develop.

The Media Spin

What makes the impact of news even more nebulous is this: There is almost always both good news and bad news about a stock. In addition, the news story itself almost always has both a positive and negative aspect.

Let's say a company reports another in a string of quarterly losses. If the stock goes down, it's due to disappointment that the company still hasn't been able to climb into the black. If the stock goes up, it's because the loss was less than the previous quarter. The action of the stock comes first. Then the news on the stock is tailored to fit the move by accentuating either the positive or negative aspect of the story.

The truth is that, except in cases of obvious causality (when the news triggers an immediate and decisive reaction), we never know for sure why the market or a stock does what it does. Since a stock is bought and sold by thousands of individuals every day, it's reasonable to assume there is more than one reason

causing its behavior. In fact, there can be a myriad of reasons, some knowable, others not knowable. Buy and sell decisions are often motivated by a host of non-news-related, silent triggers that are rarely cited by the media.

However, over the years we have been conditioned by Wall Street and the financial media to believe that stocks move up and down for identifiable reasons. This is the way the stock market has been covered by the media forever: Tie the event to whatever news makes it plausible. Completely ignored is the independent force that controls everything: The market itself and the emotions of those who respond to it. This media treatment of the stock market is so routine, so accepted, and so entrenched, that its validity is never questioned. Millions ask “What happened in the market today?” and millions respond with what they hear/read in the media, as if it were fact.

Stock market news is reported by news organizations, not by behavioral scientists, psychologists, or students of the subtleties of the market. The business of news organizations is to report news. They are trained to answer the “why” of things with logical explanations that make for neatly packaged, complete stories. They are well-intentioned, with little awareness that their market stories are misguided. There is far less excuse for advisors and brokers in the securities business who often give the same vapid explanations. They should know better, but most don't.

The Media Wears No Clothes

I feel very alone in discussing this subject. The emperor has worn no clothes for such a long time, no one seems to care. But this is important. We're talking about people's money. If our net worth suddenly drops sharply, aren't we entitled to an honest, knowledgeable explanation of what is known and, more importantly, what isn't known? Why is truth in advertising more important than truth about our money?

It is a myth that what's reported on

market behavior by the media is fact.

It's a myth that such behavior can be explained by knowable, identifiable reasons (surprises like invasions, tsunamis, and assassinations are exceptions).

Correcting such long-entrenched, widely held misconceptions is difficult. It's unlikely to happen. I'm hoping those media sources with the most air-time and print space will try. Here are my suggestions.

In my view, every discussion on TV, radio, newspaper, magazine or the Internet that gives reasons for a big move in the market is unbalanced, incomplete, and misleading—unless it alludes to these six points:

- 1) The stock market itself is the all-powerful final arbiter. The day, hour, or minute it feels the rubber band has been stretched too far, it'll do something about it, not before.
- 2) Human emotions, responding to the markets' gyrations and triggered by fear and greed, likely play a key role.
- 3) Worries over a wide range of overlapping factors, both fundamental and technical, may or may not be additional influences. (Future

market historians may well cite long-standing housing and credit worries as major factors in shaping the market's trend. The significance of their role on the particular day of July 26, however, is unknowable.)

- 4) A market that acts randomly and irrationally cannot be explained logically.
- 5) Except in cases of surprise, most news is irrelevant in explaining the market's action on a particular day. The stock market leads; the news follows.
- 6) The answer to the question, "Why today?" is: "I don't know—nor does anyone else." The markets are complex and perverse. They defy definitive answers.

They Report, You Decide

In all likelihood, things will stay as they are. So it is up to you, the informed individual investor, to rise above the misinformed media.

If you are looking to the stock market to grow your net worth, you should be aware of the enigmatic nature of the phenomenon you're dealing with—even if your news provider is not. When

you're watching or reading the whys of what happened in the market that day, know that the reporter is innocent and well-intentioned but clueless. What he presents as facts are guesses that may or may not be pertinent.

I know this sounds terribly arrogant. I don't mean to be. On the contrary, if there ever were a situation that calls for humility, it's dealing with the stock market. I hope investors develop a respect for the perplexity and primacy of the market itself and remember it is autocratic, not democratic. When it acts as you predicted, it is mostly coincidence.

Fortunately, the media's daily ineptness is of less concern to someone who is truly a long-term investor—and maintains that long-term focus even when listening to the daily news. Big market moves may be inexplicable, but a long-term or dollar-cost-averaging approach precludes the need for explanations.

What can be said with confidence is that the one thing that is not random and irrational about the market's performance is its basic, underlying, 100-year entrenched uptrend.

Focus on the long term and you can ignore the media's distortions. ▲

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