



Warning: Should You Sell This Stock Based on Insider Activity?

Description

I recently had a discussion on social media about the false representation of insider activity. A poster was warning against an investment in a particular company because it had significant insider selling. However, not all insider selling is created equal. Let me explain using the case of **Absolute Software** (TSX:ABT).

If you take a look at the insider activity chart of Absolute, you'll see dozens of trades on the open market over the past six months. At first glance, you might have the impression that insiders are dumping the stock. However, if you look deeper into the numbers, you'll notice that these trades are made in conjunction with the exercising of options. Many insiders use options as a means of supplementing their income.

Investors should not put these trades in the same category as a sell on the open market without any options attached. The problem with many of the financial websites or tools available is that they provide investors with an incomplete picture. As such, you are not making informed decisions without taking a deeper look.

Circling back to Absolute, despite gaining 17.6% year to date and trading near 52-week highs, there hasn't been a single sell on the open market that wasn't attached to options. This paints a much different sentiment picture. It is also worth noting that Absolute has not seen any insider buying on the open market either. In this case, there is very little evidence to support bearish or bullish sentiment.

Fast-growing company

What do we know about Absolute? It is [posting record](#) quarterly results. Earlier this month, the company posted second-quarter results that beat expectations. Earnings of \$0.04 beat by a penny and revenue of \$24.4 million beat by \$0.16 million.

Revenue grew 6% year-over-year, while adjusted earnings before interest, taxes, depreciation and amortization (EBITDA) grew by 88% over the second quarter of 2018. It saw growth across all of its segments with double-digit growth in the Enterprise (+12%) and Government (17%) sectors.

In 2019, the company expects revenue growth of between 3% and 6% and has increased adjusted EBITDA margins by 200 basis points to 17.5% of revenue. Analysts expect the company to average 50% earnings growth through 2020. This gives it a price-to-earnings to growth (PEG) of 1.12. Given this, the company appears to be fairly valued at today's prices. In fact, considering the recent run-up in share price, it is approaching overbought territory and may be due for a short-term pull-back.

Foolish takeaway

It's important for investors to always do their own due diligence. Using Absolute as an example, current valuations and insider sentiment point to a reasonable priced stock. This doesn't make it a bad stock, and insider activity at the company is certainly not a reason to sell. Although I would not recommend starting a position in the company today as there could be short-term weakness, it is a [good little software company](#) to own.

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