Swine Flu Panic: Trading the Hype

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I wanted to discuss this whole swine flu hype that’s been blown out of proportion to illustrate how the media creates illusions from what would seem to be valid information. This also relates to the investment world because today, virtually everything that hits newswires is spun further by the financial media. This of course is done intentionally.

In the end, most who jump aboard the hype - whether it’s the stem cell hype, the ethanol hype or the swine flu hype – end up losing while the ones who understand what’s going on take your money.

As you might know, I do not watch CNBC or FBN. I don’t even have cable because I don’t have time for trash (although I realize there are a few good channels). But I’m willing to bet the bubble networks have been all over the swine flu panic as a way to create trading blurbs.

Understand this. You should always stay away from this trash unless you are a dedicated day trader. Then again, I don’t recommend anyone try to become a day trader because they eventually all get blown out.

Despite any real evidence of the swine flu posing a threat to become a pandemic, the mainstream media continues to blow it out of proportion. But if you have a decent memory you will recall they did the same thing with the bird flu a while back.

Much of the blame is due to the warnings from public health organizations, such as the Centers for Disease Control (CDC) based in Atlanta. As well, the Geneva-based World Health Organization (WHO) has declared the flu a "public health emergency of international concern.” The organization has raised the threat level for a pandemic; the term used to designate a global epidemic.

The current variation of this virus is of the H1N1 type, which (as far as I can tell) is not of the pandemic type. However, public health officials are concerned that mutations could create a large-scale pandemic. But recall that the reemergence of the avian flu in 2003 ended up killing only 257 out of 421 infected in 15 countries. Most of the deaths were in the elderly, very young, those with chronic respiratory disease, and/or in countries with poor hygiene. These are the typical conditions that really make the flu virus deadly. That doesn’t mean it won’t become a pandemic. It only means that those who use this speculation for event-driven trading need to know what they are dealing with.

For traders, all that matters is perception because that affects market psychology. And apparently the traders have seized the opportunity to pump up several stocks thought to
be associated with the swine flu hype. But unless we see real evidence of a major problem, this is all hype as far as investments are concerned. So if you plan (or have already) gotten involved with the stocks I am about to mention, you had better plan to trade them short-term. And regardless whether you make money or not, you need to avoid getting stuck in them.

Understand that the swine flu is of the same virus (influenza A) that kills tens of thousands of Americans annually and up to 500,000 worldwide, yet you don’t get a panic from the media. There are a few slight differences in this virus, but nothing that has warranted the media hype.

Thus far, there has been only one (suspected) death in America due to the swine flu. If I didn’t know better, I’d have thought thousands had died in just a few days based upon the media exposure. The fact is that the current identified strains are not of the pandemic type. And they are responsive to medications currently available.

So the first lesson is this. If you’re going to try and profit from short-term events, you must first recognize they are short-term events. This is critical because what it means is that any investments related to these events are likely to fall not only back to prior to the event, but even lower. I know this to be generally true based on several years of observation.

The bottomline is this. If you aren’t in on these stocks early on, you are really asking for one of two things. You will either get stuck holding the bag or you will suffers losses.

This brings me to the next point. If you plan to take advantage of event-driven trading, such as the current swine flu hype, you better be very skilled in short-term trading. This implies you will use stop-losses. Otherwise you are sure to get stuck holding the bag as the stock price deflates.

So now, let’s have a look at some of the stocks that have been linked to the recent swine flu panic.

First we have a microcap thought to be a potential beneficiary if the swine flu becomes a big problem and is unresponsive to Tamiflu. This is most likely to happen if the virus begins to mutate.

Understand that some of the biggest names in venture capital (Kleiner Perkins and Prospect Venture Partners) invested $20 million into the company a couple of years ago. But if you think they’re smiling now, I wouldn’t bet on it. Their buy-in price was $4.35 per share. But if the hype continues, they might start smiling.

As you can see, NVAX began its speculative run-up towards the later part of the day last Friday, just as the news broke of the deaths in Mexico. This was when it hit the mainstream wires. You probably remember. I certainly do. I was already thinking these stocks would begin to move.
But if you hadn’t gotten in by the close on Friday, you probably got steamrolled after watching the stock soar by over 130% in early hours trading, opening at over $3.60 per share on Monday. This was when the sheep rolled in. I’m willing to bet it’s also when CNBC hyped things further.

Always remember who gets first pick at event-driven stocks; those who have access to pre-market trading (institutions). I can guarantee you most of the sheep bought the stock and watched it drop. Some of the others know how pre-market surges play out with event-driven stocks, especially when they have no real fundamentals, not to mention no revenues to speak of.

By Tuesday, NVAX showed some recovery, closing above $3. The key thing to focus on here is the trading volume. As you can see, while still holding up, it appears as if it might soon show signs of dropping off. When that happens, look out below. If you’re in this stock, you’d better have stop-losses in place.

But we aren’t finished analyzing the stock. We should also have a look at the historical chart in order to get an idea about what current levels mean. I don’t know about you, but from the technicals alone, it’s easy to see where this stock is headed. So why would I even care to look at longer-term trends if I plan to trade it short-term? Because it further reemphasizes the need for proper risk management. We don’t want our capital stuck in this stock when the air runs out.
Next we have a similar smallcap biopharma, BioCryst Pharmaceuticals (BCRX). Kleiner Perkins has an even bigger stake in the company. Along with Texas Pacific Group (the LBO/private equity firm that pissed away over $7 billion on Washington Mutual in one of the worst investments in at least a decade) they’ve invested nearly $100 million in stock and warrants at around an average cost basis of $9. Continued media hype might give them the ammunition needed to license its experimental flu drug peramivir. But it doesn’t matter unless the flu gets really bad.

Upon examination of the stock price charts for BioCryst, we see a similar situation. But there are two notable differences. First, as you can see, the recovery since Monday looks stronger than for NVAX. Also notice the new high made just after the open on Tuesday. And it managed to close higher than the previous day’s close. But you should note that the volume looks to be drying up, although it’s still too soon to tell.

Looking at the historical chart of BCRX, although the long-term trend mirrors that of NVAX, there are insufficient points to confirm this. In other words, the chances of the trend being broken are somewhat higher than with NVAX.

Now, if you think the partners of these venture firm don’t know some big hedge fund managers and media executives, you aren’t thinking clearly. I do not know whether they have helped swell the hype. What I do know is that the swine flu as it currently stands is complete hype. And the media continues to blow the issue out of proportion each day.
As well, I can assure you this...those connected with the financial media are making big money pumping these stocks up. But in the end, the bottom is going to drop out. The higher they rise the harder they’ll fall. This is one of the main laws of investing.

Meanwhile, Roche, the owner of Tamiflu, has also seen sizable gains over the past few days. Currently, Tamiflu is thought to be the most effective treatment for the flu. But this could change if the flu mutates. Millions of orders have already been placed for Tamiflu by several nations. Is this starting to sound familiar? Do you remember the bird flu scare?

If we examine the 5-day chart, you can see the Monday pre-market reaction of the swine flu mania. However, it’s held up a bit better than the smallcaps, as you’d expect. You’d also expect the gains to be much smaller, as has been the case. But keep in mind that this is a real company that will continue to do well without or without a pandemic.

GlaxoSmith Kline is also in play due to its antiviral drug, Relenza. By now, you’re probably already looking for the Monday pre-market surge, and a large one it was. But notice that after only one day, it’s already given up the gains made on Monday.

Have a look at the historical chart of GSK. Although it’s difficult to say, it appears as if the longer trend would imply that the stock will fall from current levels down to the mid-20s. Much of this will depend on the forward market direction. Assuming the market remains in a narrow trading range (not likely), I would expect GSK to fall to the mid-20s over the next several months. Market weakness would make this decline worse, depending on when and how severe it was.
Gilead is also involved with Tamiflu. As you can see, the charts are similar to the others.

Notably, the historical chart looks like a gem. Hopefully, you know a bit about GILD. They’re a great story. As far as shareholders go, what’s been Amgen’s loss has primarily been GILD, DNA and CELG’s gain over the past few years. However, I would caution you against buying into strength during this market. Rather, generally speaking (unless you are trading short-term) you should be looking to buy strong companies that have already been beaten down because it’s unlikely that many companies will make it through this mess without getting hit. It’s only a matter of time.

Finally, we turn to the drugstores, thought to be the real beneficiaries of the swine flu hype. With millions of Americans fooled by the media panic, they’ve flocked to buy surgical masks and gloves. In many locations, supplies have run out. But you can bet it won’t be long before they restock because they know this hype isn’t likely to last long. Besides, there really is no need for masks and gloves unless you work in a hospital or live
in crowded regions with poor hygienic conditions (like some nations in Southeast Asia and Latin America).

After just a couple of days, it already looks as if the juice is fading with CVS.

I’d say the long-term chart looks good, but I wouldn’t be a buyer here.

Next we have Walgreen’s (WAG). I actually like the short-term chart better than CVS.

And the long-term chart looks better as well. Finally, Walgreen’s much lower debt is a sign of good management. And I cannot leave out their excellent merchandising.
So what’s the lesson here? Keep your head on straight and know what you’re getting yourself into. In other words, LOOK BEFORE YOU LEAP. Know what you’re up against and have a game plan.

While the small-cap biopharmas certainly offer a much higher chance of big gains, they are unlikely to hold them. And when they correct, unless you have stop-losses or day trade them, you’re likely to end up stuck holding them.

Remember, it’s only the flu. And until I see massive deaths (God forbid) I won’t bother wasting my time listening to the media drama about it. And you shouldn’t get sucked into the trading trap.