Be wary of scary financial headlines

One week ago, the top article on a popular financial website was titled, "Three Black Crows Could Spell Doom for the Market."

That sounded scary, so I read on. The "Black Crow" is a candlestick chart pattern where the market closes exactly on its daily low. Closing on its exact low is what the S&P 500 did on Monday, Tuesday, and Wednesday last week.

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The article said that was unusual, but it failed to say how unusual and it didn't test the pattern's reliability. So I did.

I tested the Three Black Crow pattern on the S&P 500 dating back to 1950. It turns out last week was the only time where the Black Crow pattern occurred on three consecutive sessions.

I'm pretty sure one positive sample isn't statistically significant and I'll let you know in a month how the pattern tested!

What if we soften the criteria and only look for two consecutive Black Crows on the S&P 500? That pattern occurred on four occasions (12/8/99, 10/27/05, 11/25/11, and 3/25/15).

For the first three, the S&P 500 gained 3.85% one week later and 6.12% a month later. Again, not a good sample size but it turns out the pattern has led to very bullish results!

Another scary pattern that sometimes appears in the headlines is the "Death Cross." This is a pattern where an index's 50-day moving average crosses below the 200-day moving average.

Once again, test results aren't nearly as scary as the pattern's name. Since 1950, the S&P 500 index is about unchanged in the month following a Death Cross pattern.

The most read financial articles are ones with scary headlines. We are told patterns such as Three Black Crows or Death Cross spell doom for the market.

Unfortunately, those articles rarely site statistics as proof. Their goal is to get you to read any maybe post the article for others to see.

This is good business for the financial press, but it's not helpful for your portfolio.

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