Investment in Equity (Part 8)

Before we proceed any further, we will do a pair of imaginary deals. We will do an imaginary purchase and then an imaginary sale. Just to get the feel of it all, just to see how the buying and selling are to be done. We shall handle Reliance Capital itself for the purpose.

Table 1

Date	Closing Price
21-Aug-12	371.55
22-Aug-12	364.60
23-Aug-12	352.30
24-Aug-12	344.30
27-Aug-12	332.60
28-Aug-12	328.20
29-Aug-12	321.25
30-Aug-12	320.10
31-Aug-12	319.80
03-Sep-12	320.25
04-Sep-12	331.55
05-Sep-12	330.25
06-Sep-12	329.00
07-Sep-12	335.65
08-Sep-12	337.15

After forming a high of Rs. 371.55 on August 21, 2012, Reliance Capital fell to form a bottom at 319.80, and after forming a bottom at Rs. 319.80 on August 31, 2012, it started rising. (Please see the Table 1.) As per my theory, a scrip is to be bought when price rises 5% from the last formed bottom. The last formed bottom was Rs. 319.80. 5% of Rs. 319.80 was Rs. 16.00. When we add Rs. 16 to Rs. 319.80, we get Rs. 335.80. Rs. 335.80 was the level at which we should have bought the scrip, if, only if, price rose and touched Rs. 335.80. The price did rise and touch Rs. 335.80 on September 8, 2012. So let us imagine that we bought the scrip as soon as it touched (and also surpassed) Rs. 335.80 on September 8, 2012. I am giving below the actual closing rates of the related brief period necessary for this illustration:

Table 2

Date	Closing Price	5%	Selling price
08-Sep-12	337.15	16.90	320.25
10-Sep-12	337.85	16.90	320.95
11-Sep-12	340.90	17.00	323.90
12-Sep-12	341.15	17.10	324.05
13-Sep-12	339.70		324.05
14-Sep-12	352.45	17.60	334.85
17-Sep-12	373.30	18.70	354.60
18-Sep-12	374.45	18.70	355.75

20-Sep-12	362.60		355.75
21-Sep-12	399.90	20.00	379.90
24-Sep-12	409.00	20.50	388.50
25-Sep-12	410.00	20.50	389.50
26-Sep-12	421.20	21.10	400.10
27-Sep-12	432.25	21.60	410.65
28-Sep-12	431.45		410.65
01-Oct-12	444.20	22.20	422.00
03-Oct-12	444.30	22.20	422.10
04-Oct-12	452.65	22.60	430.05
05-Oct-12	456.10	22.80	433.30
08-Oct-12	448.30		433.30
09-Oct-12	455.90	22.80	433.10
10-Oct-12	443.65		433.10
11-Oct-12	458.25	22.90	435.35

Having bought the scrip at Rs. 335.80 on September 8, 2012, our next action should have been to sell it away if, only if, the scrip fell 5% from the last formed high. As soon as we bought the scrip for Rs. 335.80, we took Rs. 335.80 as the last formed high. My theory tells us to sell the scrip away if it falls 5% from the last formed high. 5% of Rs. 335.80 is Rs. 16.80. If the price had straight away fallen 5% from Rs. 335.80, it would have touched Rs. 319.00, and it is at this level that we must have sold the scrip away, had the scrip fallen. In other words, Rs. 319.00 was our next selling price.

Meanwhile, I shall also state one important requirement of the system. According to my theory, when the price falls 5% from the last formed high, we must sell the scrip away, irrespective of (this is important) whether the sale would fetch us a profit or whether we suffer loss from it. In other words, what the sale will earn us – a profit or a loss – is absolutely immaterial. When the price falls 5% from the recently formed high, we must sell, come what may, that is, even if the sale would cause us loss, and whatever be the extent of loss. There should not be any hesitation in selling it away, when the scrip has fallen 5% from the last formed high.

The rationale behind the insistence is: When a scrip falls, it can crash 50% or 60% or even more, over a period of time. There have been umpteen number of instances of scrips losing as much as 90%, or even more. Therefore, we do not know how far the falling will continue, and we will also not try to guess how far the scrip will fall. We won’t do any guessing at all. When the price falls 5% from its recent high, it must be enough of a trigger for us to sell the scrip away. A 5% fall from the last formed high should trigger us into sale. So, in the instance on hand, having bought the scrip at Rs. 335.80, we should have been ready to sell it away if it fell 5% to Rs. 319.00.

In this particular instance, the scrip did not fall to Rs. 319.00. (Please see the Table 2.) Instead, after touching a high of Rs. 335.80, Reliance Capital rose a bit and closed at Rs. 337.15 on September 8, 2012. When we bought the scrip at Rs. 335.80, we were ready to sell it away if the price had crashed 5% to Rs. 319.00. Now that the price has risen further from Rs. 335.80 to Rs. 337.15, we should have been ready to sell it away if it fell by 5% of Rs. 337.15 to Rs. 320.25. When we bought the scrip at Rs. 335.80, we had reckoned Rs. 335.80 as the last formed top. When the price rose above Rs. 335.80 and rose further to Rs. 337.15, we must raise our selling price too to the same extent. We will find out the 5% of Rs. 337.15. It is Rs. 16.90. Deduct it from Rs. 337.15 and the level we get is Rs. 320.25. This must have been our revised or updated selling price.

The next day, Reliance Capital rose to Rs. 337.85. When it had closed at Rs. 337.15 on the preceding day, we were ready to sell it away at Rs. 320.25 if the price had crashed to Rs. 320.25. The price did not crash, and, instead, it went up from Rs. 337.15 to Rs. 337.85 on September 10.

Since the price had risen to Rs. 337.85, we must have taken Rs. 337.85 as the last formed high, and we must also have raised our selling price from Rs. 320.25 to Rs. 320.95 which is 5% below Rs. 337.85. On September 11, the price further rose from Rs. 337.85 to Rs. 340.90. Immediately, we must have raised our selling price from Rs. 320.95 to Rs. 323.90. On September 12, the scrip further rose to Rs. 341.15, and we must have raised our selling price to Rs. 324.05.

The next day, i.e., September 13, the price fell to Rs. 339.70. Though the scrip fell from its previous closing figure, the fall was less than 5% and was not enough to trigger us into sale. Had it fallen to Rs. 324.05, we would have sold the scrip away. Since the extent of fall did not come to 5% of Rs. 341.15, we did not do anything, we just waited. The next day, the scrip rose to Rs. 352.45. 5% of Rs. 352.45 is Rs. 17.60. Since the price had risen, we too raised our selling price from Rs. 324.05 to Rs. 334.85. If the scrip now crashes to Rs. 334.85, then only would we have sold it away.

The next day (September 17), the scrip rose further to Rs. 373.30, and we too raised our selling price from Rs. 334.85 to Rs. 354.60. The next day, price rose further, to Rs. 374.45, and, accordingly, we raised our selling price from Rs. 354.60 to Rs. 355.75. The next day, (September 20), the scrip fell to Rs. 362.60. We had decided to sell the scrip away if the price fell 5% from the recently formed high, and, accordingly, we would have sold the scrip away had it fallen to Rs. 355.75. But the scrip did not fall to Rs. 355.75. It fell to Rs. 362.60 only, and this was not enough for us to sell the scrip away. So, we just held on to the scrip and waited. The next day, the scrip rose to Rs. 399.90, and we raised our selling rate from Rs. 355.75 to 379.90.

These are all repetitive in nature, and there is no need to repeat them. From all this, one thing becomes clear. When we are holding a scrip, and when its price rises above the last formed top or high, we will also raise our next selling price to that extent. This will make sure that our next selling price is exactly 5% below the last formed high. We can describe it in this way: Whenever the top (or high) rises, we will raise our selling price too. This will help us to sell the scrip away when it falls 5% from its last formed high.

Thus we should take advantage of every rise in the last formed top. Whenever price falls, but the fall does not amount to 5% of the last formed high, we will not do anything, and we will just wait. In other words, our selling price should always be exactly 5% below the last formed high. The figures in the Table 2, given above, lucidly illustrates this point.

After October 11, the scrip entered a downward spiral. Please see the Table 3. It was on October 25, 2013, that the scrip completed the 5% fall; on that day, it fell to Rs. 435.35, which was our next selling price. When the scrip fell to Rs. 435.35, our imaginary sale should have happened immediately. We must have sold the scrip away then and there.

Table 3

11-Oct-12	458.25
12-Oct-12	452.05
15-Oct-12	454.50
16-Oct-12	438.85
17-Oct-12	444.05
18-Oct-12	455.45
19-Oct-12	440.90
22-Oct-12	444.55
23-Oct-12	440.10
25-Oct-12	430.45

As soon as we sold our scrip away at Rs. 435.35, we must treat Rs. 435.35 as the last formed bottom or low, and calculate our next buying price. We will buy the scrip again, if it rises 5% from the last formed bottom. We will deem Rs. 435.35 as the last formed bottom. In the instance on hand, the scrip fell further on the very same day, and closed at Rs. 430.45. The 5% of Rs. 430.45 is Rs. 21.50, and we must have bought the scrip if, only if, it rose to Rs. 451.95; please see the Table 4 given below.

Table 4

Date	Closing Price	5% of closing price	Next buying Price
25-Oct-12	430.45	21.50	451.95
26-Oct-12	417.40	20.90	438.30
29-Oct-12	413.35	20.70	434.05
30-Oct-12	398.35	19.90	418.25
31-Oct-12	381.95	19.10	401.05
01-Nov-12	387.20		401.05
02-Nov-12	392.20		401.05
05-Nov-12	394.55		401.05
06-Nov-12	394.60		401.05
07-Nov-12	406.55		401.05
08-Nov-12	401.05		401.05
09-Nov-12	390.05		401.05
12-Nov-12	394.20		401.05
13-Nov-12	392.45		401.05
15-Nov-12	386.70		401.05
16-Nov-12	379.60	19.00	398.60
19-Nov-12	376.05	18.80	394.85
20-Nov-12	376.15		394.85
21-Nov-12	381.00		394.85
22-Nov-12	384.50		394.85
23-Nov-12	382.90		394.85
26-Nov-12	393.85		394.85
27-Nov-12	402.15		394.85

You can see from the table that, on some days, the scrip fell below the last formed bottom, and thus pulled the last formed bottom further down. Whenever a lower bottom is formed (or, in other words, whenever the bottom falls) our next buying price should also be lowered correspondingly, keeping the distance between the newly formed bottom and our next buying price steadily at 5% of the newly formed bottom. The table 4 given above makes it obvious that the next buying price will always be 5% above the last formed bottom. Whenever the last formed bottom (or low) falls, we must take advantage of it by lowering our next buying price to the same extent. In between, the price rose on a few days, please see the table 4. So far as these rises do not reach 5% of the last formed bottom, we will not do anything; we will just wait. Only when the price rise reaches 5% above the last formed bottom, will we make our next purchase.

(To continue)