How to make money on the stock market
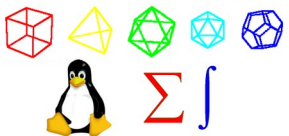
By : Khawar Nehal
Applied Technology Research Center

Methods

There are multiple methods to make money on the stock market.

I shall explain some of them and what I know about them.

If you know better or know more methods, please feel free to update me on khawar@atrc.net.pk
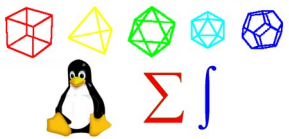
Value Investment

I shall start with the best method I know.

This is the best based on the probability of making money.

The probability over a period of over 1 year is over 99.99%.

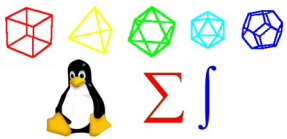That is a very good probability of making money.

ATRC

Value Investment

The amount of money made is from 20 to 40% per annum via dividends. This is the expected range based on PKR and the PSX market.

This does not include the 70% to 300% or more which are expected extra earnings based on the long term price appreciation expected.
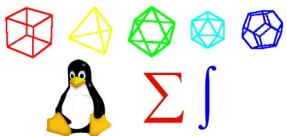
Value Investment

The Long term price appreciation can result in an extra 20 to 50% per annum extra income over an period of about 3 to 7 years.

The time to invest is above 10 years. And if the valuations supports it and the dividends keep rolling in, then the share is kept as long as they meet the criteria of high return shares.
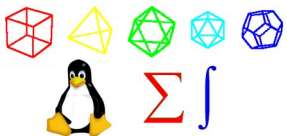
Value Investment

There are two calculations.

One is the calculation to buy the share.

The other is the calculation to keep the share.
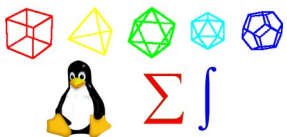
ATRC

Value Investment

Proof of method :

Long term proof is Mr. Warren Buffet's results.

My own results have proven the dividends portion. The value appreciation is partially done and expected within the next decade.

Based on my own experience you can expect a return of at least 30% to 40% per annum over a period of investment lasting over 10 years with a probability of over 99%.
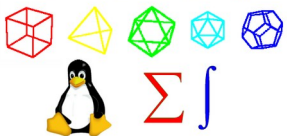
Value Investment

The >99.99% probability calculation and results are based on the actual results achieved by multiple value based investors.

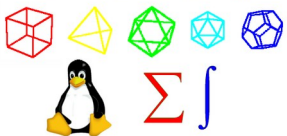This represents investments over a time period of more than 50 years.

Value Investment

By value investment, I mean a real investor with enough self control to be able to not make any mistakes related to the temptation of trying to make money on short terms or day trades.

Usually it means following the HODL approach for almost all shares.

Value Investment

Now I shall explain the formulas and actual values which I use in the PSX. The numbers shall change for PSX and other markets based on the state of the market. But those numbers can be tuned after some experience. If anyone wants to get help on how to come up with the actual numbers for other markets, then it is a long term exercise and we shall have to come up with some method of collaboration to do it.

ATRC
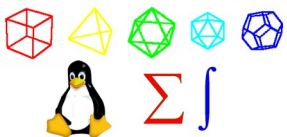
Value Investment

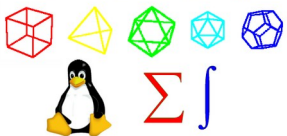Currently 2022 – 2023 I am using the following settings :

Market cap > 1 B PKR

Price to book value < 1

Dividends above 10% per year for at least 5 contiguous years.

PE ratio below 2

Value Investment

Select the top 5 based on the criteria and spend equally on all 5.

Buy when the market is red. If it is green then wait a few days to make an extra 1 to 2 percent.

But over a period of a few days until the whole amount to be invested is spent.

The top 5 usually remain there for a period of about two weeks before you can expect a change in the top 5 to be invested in list.
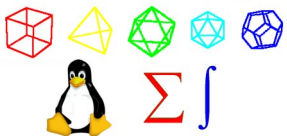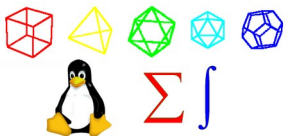
Value Investment

If you can follow this then you can expect to get from 30% to 40% in dividends per year.

Also extra from the price appreciation.

By the way, some of those in the top 5 have price to book ratios near 0.5. That means you are buying the company at half the price.

Some are even lower than 0.2. So you already are buying a company worth 5x the price.
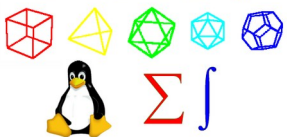
Value Investment

Just need to HODL and WAIT for the price to reach and exceed the BOOK VALUE.

The toughest thing in value investment to do is to stick to not being greedy and try to speculate on short term trades.

This is the easiest thing to learn and the hardest thing to DO.

It took me many years to get myself in control in the DOING part.

ATRC

Value Investment

For this presentation I had a look at the valuations today.
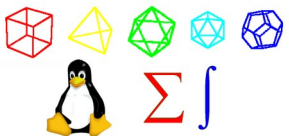
I was surprised to see a price to book value of 0.01.

BOP is the share. Book value Rs 418.72

Price Rs 3.8

That is a 99.093% discount on the BOOK value.
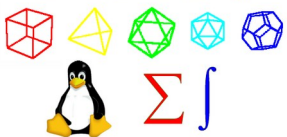
Value Investment

This is just an example. I am tempted to buy this but my formula prevents me from doing so because of the lack of dividends.

Also from experience, I know that speculators create high volumes on this share.

See. Now I have two choices.

Deviate from the path and take risks on a speculative type stock which people play with or just stick to the plan.
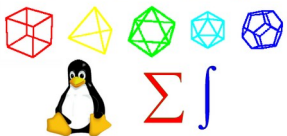
ATRC

Value Investment

I shall deliberately ignore this historically low valuation and TAKE the risk of losing the OPPORTUNITY of a life time.

The reason is that the strategy to maximize profits with the reasonable risk is already defined.

I am over 50 years old and can keep myself on the track which is defined.

This is the skill which needs to be developed.

Value Investment

Stay AWAY from temptations to go for short term gains.

They deviate from the low risk high return investment and move to high risk and very high returns expected. With a high risk of losing money.

Value Investment

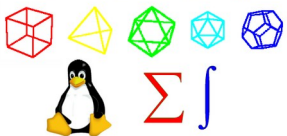This is where Mr. Warren Buffet's rules of making money are important.

Rule 1 : Never lose money.

Rule 2 : Do not forget rule number 1.

While making this presentation, I ran into the temptation to buy BOP against the plan.

So this is a very good example of sticking to the plan.

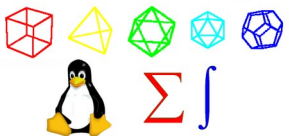# Value Investment

Mr. Warren Buffet's rules in more rules.

Rule 1 : Never lose money.

Rule 2 : Never forget rule 1.

Rule 3 : Focus on the long term.

Rule 4 : Know what you're investing in.
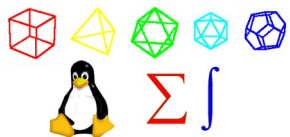
Value Investment

Rule 4 : Know what you're investing in.

It is important to have a deep understanding of the industries and companies you are investing in.

Takes the time to thoroughly research each investment opportunity, looking at factors such as the company's financials, competitive advantage, and management team.

By following this rule, you can make informed investment decisions and minimize your risk.
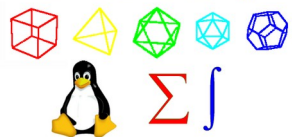
Value Investment

An example of Rule 4 was GASF and NCPL.

GASF was a company which was stellar in the 1990s and was touted as a winner globally.

I checked the value of the shares it owned and it came to about 2x the market cap.

So I bought it at Rs 6 and sold at Rs 11 in a matter of about 6 months. Thanks to AKD for noticing the difference also and buying it up and fixing the price.
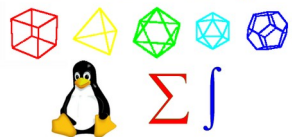
Value Investment

Another was ENGRO. It makes fertilizers.

My computers indicated a sudden drop in price to book value. Down to 1.3 which is low for such a large company. Also this was the time I was shifting to value investing practically.

So I bought it first then looked at why it got THROWN by other speculators.
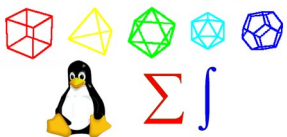
Value Investment

The reason was that it was at the last of the MSCI index and it got thrown out of the index because its market cap was beaten by other global companies.

That confirmed that there was no change in the company and the important thing it was doing. Making fertilizers and all and people need to eat.

So I was able to get a great dividend paying company at a low price.

Value Investment

Another was NCPL.

People were throwing it away because the government did not want to pay. It got its case won in the international court and that means the payouts shall be done over the long rin with a very high probability.

I was telling people for more than a year to buy this and it went on to set records in the long term highest dividends area in the PSX.
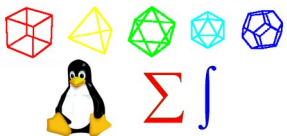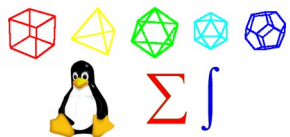
Value Investment

Most people who put money in the stock market do not care about PB and dividend yields because these are related to long term investments.

But the reason they make stable profits is because of probability and statistics.

It is possible to analyze and predict long term trends and expectations with a high probability.
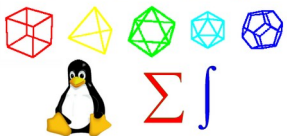
ATRC

Speculation

Now I shall explain about why most people fall flat in predictions over the short term.

For 30 years from the time I was a kid to about the age of 40 I learned about things like bollinger bands, SMA, and such.

I even made my own programs to analyze the biggest gainers and losers thinking there might be some way to make moolah in that.
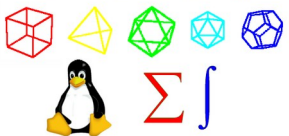
Speculation

After I made some analysis on the biggest losers, I learned that the charges per trade per share were about 12 paisa.

And the fluctuations are in the range of a few paisa.

So there is no way to cover the commissions with this idea of high frequency trading because that maybe assumes a trade commission of ZERO.
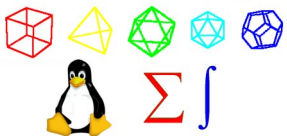
Speculation

My wife kept telling me that shares are a fraud and the house always wins commissions.

So I agreed to that idea when it comes to high frequency trading and normal commissions.

Then there is the extra taxes called capital gains taxes.

In dividends there are only income taxes because we almost never sell in value investing.

Speculation

I did market research and found that there was a need for python training. So I started that.

In that I learned how libraries are available for pattern matching and it makes running prediction functions easy.

A few days ago in Guru someone requested a way to predict trades based on MT4 data at an accuracy of 70%
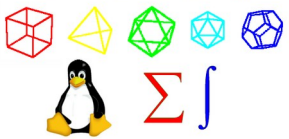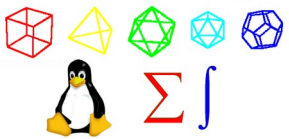
Speculation

So I thought why not 90% since the AI functions can be asked to keep learning until they reach a certain accuracy.

Then before I started, I knew from experience that in all these years of pattern matching no one has been able to pull it off. So I check the research and the indicators were having an importance value of up to 0.08. I need 0.9 and above.
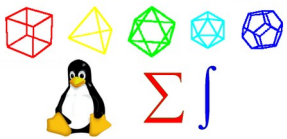
Speculation

The max importance of 0.08 confirmed my decades of research into pattern matching for stock prices.

There is no way someone is going to make money or beat the long term approach with the pattern matching stuff.
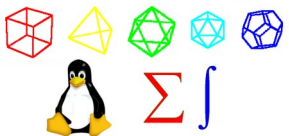
Speculation

I shall explain what can be expected to happen based on what I have learned so far.

A monkey selector shall follow the index.

The index might beat the monkey selector. (reason shall be explained later)

The pattern matching method shall lose money compared to the index due to commissions on sales. The index is assuming buying once and HODLing.
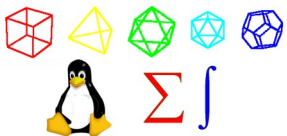
Speculation

The index shall beat the monkey because the monkey selector is random but the index specifically selects high market cap stocks from the top down.

Due to regulator oversight and other better management forces inherent with higher market caps over penny stocks. The chances of dividends are higher than a random monkey selector.
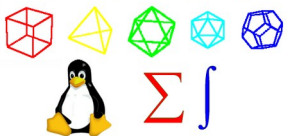
Speculation

The reason there is no importance feature in the shares price data is because there are thousands of VARIABLES.

These variables are the random number generators based on strange buy and sell decisions made by speculators who participate in setting the price. They are not a fair market or a market which shall reach the fair value. There shall never be a technical correction.
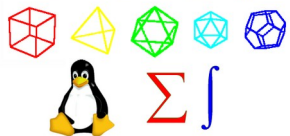
Speculation

In real estate there is a cost of building a building. Usually calculated in cost of building per square meter.

So if a building is priced below the cost to build, then you can expect it to be sold very quickly. The real estate is a better example of a fair market with "technical" corrections.

The stock market offering over 99% over the book value is NOT a fair market.
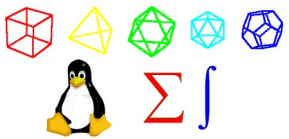
Speculation

For the shares that the majority decide to speculate in the market is totally the opposite of self regulating and self adjusting.

Mr. Benjamin Graham proposed the idea that - there is "Mr. Market" who is crazy but not crazy about everything and all the time. You need to identify pocket where Mr Market has gone crazy with greed or fear.
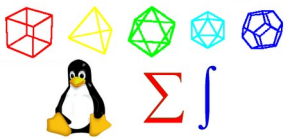
Speculation

Examples of fluctuation.

I have been able to get the top 10 gainers with less than Rs 100 spent.

This provides an indication of the butterfly effect.

In chaos theory, the butterfly effect is the sensitive dependence on initial conditions in which a small change in one state of a deterministic nonlinear system can result in large differences in a later state.
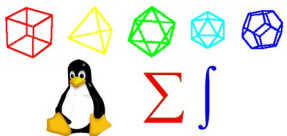
Speculation

The term is closely associated with the work of mathematician and meteorologist Edward Norton Lorenz.

He noted that the butterfly effect is derived from the metaphorical example of the details of a tornado (the exact time of formation, the exact path taken) being influenced by minor perturbations such as a distant butterfly flapping its wings several weeks earlier.
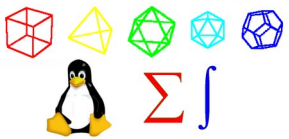
Speculation

Lorenz originally used a seagull causing a storm but was persuaded to make it more poetic with the use of a butterfly and tornado by 1972. He discovered the effect when he observed runs of his weather model with initial condition data that were rounded in a seemingly inconsequential manner.
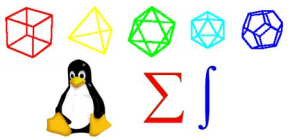
Speculation

He noted that the weather model would fail to reproduce the results of runs with the unrounded initial condition data.

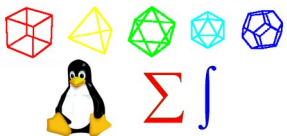A very small change in initial conditions had created a significantly different outcome.

Speculation

Do NOT ask me how it can be done. It was by accident and the info can only be used to mess up a market so the knowledge is useless for predictions.

I shall not be telling even if anyone asks.

All I want to tell is that a small amount of trades can change the prices a lot in the market.
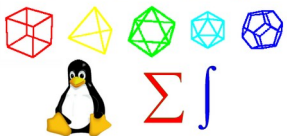
Speculation

The other issue is that there are thousands of traders who are making random trades.

I have seen employees making trades while in the office. Doctors in hospitals making trades between consultations.

Even I have made some trades during trainings in tea and lunch breaks. This was before I moved on to value investing.
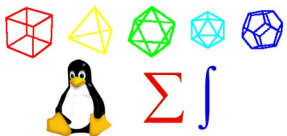
Speculation

With thousands of random number generators, it is not going to be possible for any AI/ML to come up with any feature of importance.

This is because a feature of importance depends on correlations being in effect.

Long term correlations over many years exist, but short term correlations do not exist.
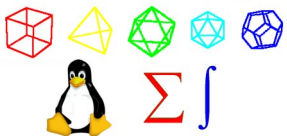
Speculation

There is one area which could be possible but I might not be spending my time or investing resources into this idea.

The idea is to look for partial patterns.

This means look for patterns over separate ranges of time. Look at all indicators and especially those which are visible to investors.

This includes the news and text channels.

Speculation

Also the behavior of different groups for different stocks is different.

A large reason patterns are not found is because the same pattern is being expected over different shares.

But different groups only deal with different types of shares at different times.

For example value investors only buy shares based on their criteria.
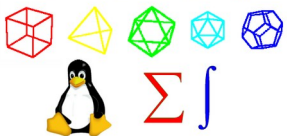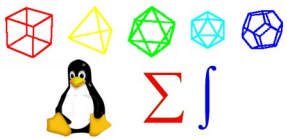
Speculation

Speculators usually go for low price penny stock with high volumes.

Each share needs to be analyzed separately.

Patterns shall change because the groups participating shall change over the long time ranges.

Speculation

If this method of partial ranges and separate neural nets for each share are used, then some patterns with higher importance values could be found.

When these patterns are found then the trades are to be done ONLY when the pattern is available. NOT in all cases.

Like Mr. Buffet says. Don't swing on every ball.
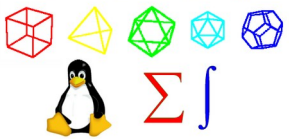
Speculation

If you understood what I mean by separate shares and partial ranges for patterns then you have an idea of what to do and look for.

But do not expect me to spend more time on this idea. I am too tired of failing because of the thousands of random variables participating in setting the price and the butterfly effect. I do not expect any method to beat the long term value investing based on experience of over 3 decades.
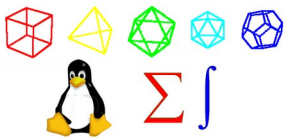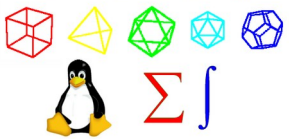
Speculation

It is like trisecting the angle.
I even tried that in school. So we have a habit of trying things which are hard or even considered impossible.
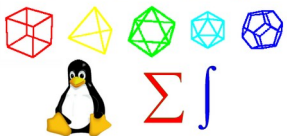
Best returns

So in summary the best returns are achieved by the value investing method and totally avoiding the speculation methods.

If you want better results than that, then invest the money in your own personal businesses which you own and control more than 50%.

Note : It takes 5 years of experience in business to make a profit and 20 years to stabilize the profits.
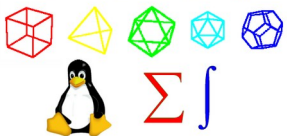
Pump and Dump

A common greedy method is called the pump and dump.

Either buy or sell with a very large capital so that you are able to get the sheep in the market to follow along. Then surprise them with the reversal because you decide the time you reverse the trend with your large capital.
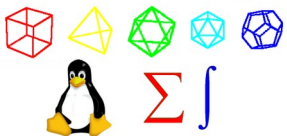
Pump and Dump

The issue is that when some people try the pump and dump, some other players are moving in the other direction at the same time. This lack of coordination causes both parties to lose millions in the same day. I have seen this happening in the data from the inside. They look like idiots.
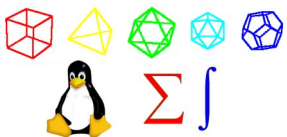
Pump and Dump

Legally it can be classified as market manipulation and there are some laws against this.

But the confusion shall arise when someone tries to implement the laws and clarify what level of price changes is going to be considered manipulation and what is not.

This because buying on share with a price difference of 1 paisa can be considered a change in the price just like any other trade.
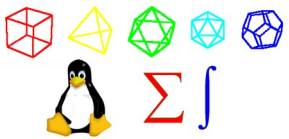
Pump and Dump

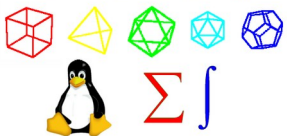The pump and dump is called the poop and scoop if the price is taken down instead of up.

When you place a trade online, it is executed according the the market.

If you make it through a broker, then the broker can profit from this.

For example, the customer wants to buy 100 shares of stock X.

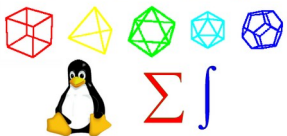**ATRC**

My trade before yours

The broker shall buy 10 shares at the current price.

Suppose the broker buys at Rs. 1.00

Then the broker shall set a sell at 1.01 for 10 shares.

Buy the shares at a set of 1.01 for the customer.
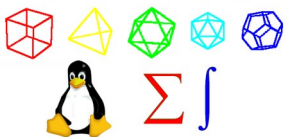
My trade before yours

If any shares of the broker get sold to the customer's account at 1.01 then the broker shall get a profit.

Repeat this trade 10 times until all the shares for the customer are bought.

Buy the shares to be bought at price y.

Set an offer to sell them at y+0.01 before placing the customer's buy order with a bid of y+0.01 for the same amount of shares.
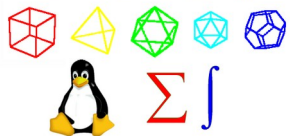
My trade before yours

I do not know the legal situation of these type of trades. But it is just to inform you that this could be done by some brokers.

Not sure if it is done in PSX.

I learned about this from articles about other exchanges.

ATRC

Commissions

This is a legal way to make money.

The house always wins.

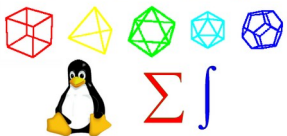Get a license for a brokerage and run it professionally.

Summary

This is basically what I wanted to explain.

Especially to the younger next generation.

If someone comes to you to do "trading" and make money and show you pictures of a person acting like they are wealthy because they are all suited and booted leaning against a Porche with a Gulfstream in the background.
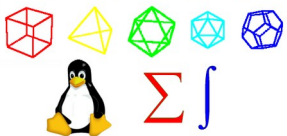
Summary

Use our experience.

Ask them to show results of their method over a period of a hour in real time.

If they say it needs time, then ask them to show it over a day, week or longer until it makes money with a probability of over 90%.

If they say you trade and pay them commissions, then you know they are playing the house always wins game with your lack of experience.
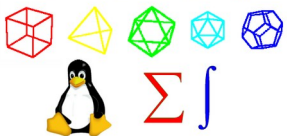
Summary

When it comes to digital currency. We told people to buy when it was about 1 to 3 dollars per bitcoin.

Then came ethereum. We predicted that well too. But we went against the value investing approach and invested in chia thinking that it has some of the best technology people in the world and lost money on that.

People might not tell you when they lose money, but we want you to know what NOT to go for.
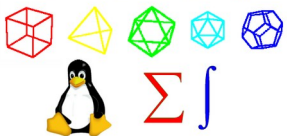
Summary

Don't know and don't want to know about what others are doing or going to do.

All I know is that I am going to stick to value investing and investing in my own companies.

Taking ownership directly or indirectly in any business is called having skin in the game and delivers the best results over the long run.

I hope you learned something.

Contact

Khawar Nehal

+92 343 270 2932

+92 331 2036 422

khawar@atrc.net.pk

http://atrc.net.pk