Chapter – 1
How to Avoid Loss in the Stock Market?

1.1 Introduction

Ask your friends, neighbors or your relatives regarding stock market investing. Most of them will discourage you and mention that it is another form of "gambling". Many individuals still believe that there is no "logic" behind the stock price movement. Those who earn big from the stock market are just "lucky". On the contrary, the interesting fact is that almost all billionaires in the world have created their fortune through the stock market, either directly or indirectly**.** "Directly" refers to the direct stock investing and "Indirectly" refers to listing their companies on the stock market. One of the world's richest persons, Warren Buffet created his fortune from direct stock investing while other well-known billionaires like Bill Gates (founder of Microsoft), Mark

Zuckerberg (founder of Facebook), Larry Page (founder of Google) made their fortune by listing their companies on stock market. Even in India, you will find many billionaire investors (e.g. Rakesh Jhunjhunwala) who created their entire wealth from direct stock investing.

My question is if stock investing is another form of "gambling" then how have these billionaires created their fortune from the stock market? You may earn one thousand or one million from "gambling" but it is not possible at any cost to become a "billionaire" or to become the world's third-richest person by "gambling". Can you say they were just lucky enough? Luck can favor once, twice or even thrice, but they are consistently earning from the stock market over several decades. A gambler can't make billions consistently. Moreover, luck is not sufficient enough to create a billionaire. So, there must be some different story.

On the contrary to this, 80% retail investors lose their hard earned money on the stock market! In this book, the term "retail investor" is widely used. "Retail investors" refers to those who engage in some different full-time job (or source of income) and invests (or plans to invest) a portion of savings into the stock market. As per statistics, 80% retail investors suffer overall loss from equity investment. Now, the most important point that arises is why maximum retail investors (small investors) lose their hard earned money in this market while a group of people are creating their fortune?

This book will explain in detail why the majority lose money in stock market, how to avoid it and what are the methods to build a fortune from the stock market.

To avoid loss in the stock market, you need to know the reasons why people lose. I am going to share a real-life example that will explain the reasons for losing money. Existing equity investors can also co-relate with the following story.

1.2 An example worth sharing

Few months back, I was having a conversation with an investor (Rohit) and I was surprised to know that he had lost around ₹ 10 lakh (₹10,00,000) in the stock market. During the last five years in the stock market, he had applied various techniques, followed many analysts and ended up with a cumulative loss of around ₹ 10 lakh! However, at several instances, he made money, but the profit was too little as compared to the losses occurred.

I am dividing his stock market journey into 4 phases. Let's have a detailed look at each phase and let's analyze exactly where he went wrong.

1st Phase-

Around five years back, Rohit didn't have any idea about the stock market but was eager to invest. One of his friends was a stock broker who used to trade regularly. Rohit was interested but didn't have any idea how to start. In such a situation, Rohit approached to his broker-cum friend. Without delaying further, his friend opened a trading and a demat account. Rohit then handed over an initial amount of around rupees one lakh (₹1,00,000) to trade on his behalf. That was the best available option as he didn't have much knowledge about what and how to buy and sell.

Initially, everything was running smoothly. Almost, every day his broker used to share some news based tips and asks for his permission to trade on that stock. Then at the end of the day, Rohit used to receive a phone call regarding the earnings. After some initial gain, Rohit handed an additional fifty thousand to his friend-cum-broker for trading. It was a nice start, he had already earned 20% profit without any technical know-how.

All on a sudden, the situation changed. There was no trade confirmation over 15-20 days. His broker no longer used to call him. Rohit was worried. Suddenly, he got to know that 50% of his initial amount was wiped away! Rohit was shocked. For a first time investor, 50% loss on his invested amount is too hard to accept. He came to know that due to unfavourable macroeconomic situation the market crashed badly and it won't change soon. With deep frustration, Rohit instructed his broker-cum-friend to sell his entire holdings. While closing his trading account, he figured out that including brokerage and other charges 55% of his invested amount was wiped away!

Where he was wrong?

In stock market, blindly following your broker (or friend) may cost you badly. Have you noticed that whether you gain or lose, your broker always remains in profit? You have to pay brokerage for every transaction (buy and sell). Your broker can earn only if you trade. So, it's obvious that your broker will encourage you to buy and sell frequently. All of us are concerned to maximize our income. While you are concerned to earn from stock market, similarly your broker is also concerned about maximizing his income. Due to this simple fact, maximum broker encourage frequent trading. Exactly, here the problem arises. The more you trade; the chances of suffering loss will widen and at the same time your broker's income will keep increasing. In the later part of this chapter, I will mention in detail why frequent trading widen the chances of losing money. Big brokerage house often send stock tips via SMS and email to their clients to encourage trading. Sub-brokers are pressurized to meet minimum turnover target. Sub-brokers can also lose their license if they fail to meet the minimum trading volume. It is the retail investors who are affected the most in this entire process. You might have also noticed that brokers are always ready to reduce brokerage if you trade frequently in large volumes. This is an indirect encouragement to trade more so that at the end of the day they can gain big, irrespective of your position.

2nd Phase –

Rohit had closed his trading account after the first incident. I was eager to know what inspired him to come back in the market.

After 6 months from his first bitter experience in stocks, he started following few business newspapers regularly. For stock tips, watching television channels like CNBC, browsing internet and reading newspapers became his habit. This was the time when equity market was on bull-run. Almost every day, market touched new heights; most of the stocks were in upward trajectory. Various analysts in television and newspaper were also expressing their optimistic view. Many of them were commenting like- "***This time it is different, market will continue to rise for at least next 2-3 years***" Rohit was tempted and was eager to make the most out of this situation. Without wasting much time he applied for a new demat and trading account. This time he got associated with a reputed broker. He was eager to enter in the market rally to earn some quick bucks, so he opted for intraday trading; one of the most common ways to earn quick money. The best part is that intraday trading tips are available at free of cost on various newspapers and television channels. There are plenty of market analysts who offer free trading tips. Rohit started following them. His broker was ready to provide up to 10 times margin for intraday trading i.e. for every ₹100 in his trading account he can trade worth ₹1,000 in intraday. He dedicated ₹ 50,000, so with this amount he could trade up to ₹ 5 lakh in intraday. Everything was great. There were plenty of free trading tips and enough margin money to trade. There were several instances when Rohit gained from these tips, but the problem was that only one or two loss making trades wiped out the entire gain earned from 5-6 profit making trades.

This is a peculiar problem. Gains are always little compared to the losses. Rohit couldn't figure out exactly where he was wrong. He had applied "Stop Loss" as per analysts, but many a times the stock started its upward journey after touching "Stop Loss"! After 4 months of trading, he took a break to calculate his overall gain. The result was shocking. In spite of various successful trades, his initial capital didn't appreciate at all. Moreover it was 20% overall loss! The interesting point is that during these 4 months around 70% of his trades were successful. He made money on those occasions. Only 30% loss making trade wiped out the entire gain! That was really frustrating. In spite of keeping "Stop Loss" and "Target", he ended up with booking small profit on successful trade and big loss on unsuccessful ones. For example, once he purchased Reliance at ₹ 800, it achieved first target of ₹810 and he booked profit of ₹10. Another day, he purchased Reliance at ₹ 800, and put "Stop Loss" at 790. However the stock crashed so badly that it reached 780 without touching 790! So, he was forced to sell at ₹780 and book loss of ₹ 20 per share Rohit was in deep frustration while sharing this "Why does every time stock market behaves with me in such a way?!"

Where he was wrong?

He was wrong at the very beginning. Intraday trading is almost a sure-shot way to accumulate loses. Can't believe it? Well, show me a single person who is consistently making money from intraday trading for at least 1-2 years. Throughout the world show me a single billionaire who made his fortune only from day-trading. You won't find a single person. You can make money once, twice or thrice but you are bound to lose after that. Generally, loss is always larger than profit. Try it yourself. Take day-trading tips from anywhere, from any analysts. There are many paid stock tips provider who claim 99% success ratio. Follow their tips and trade in intraday and check the result. It may sound bitter but the reality is that not a single market analyst can help you in creating wealth from intraday trading. Now you may think; if this is the case then why so many people jump into day trading. There are various reasons which I will discuss in detail in the latter part of this chapter.

As of now just note the indirect encouragement from your broker. You have ₹50,000 in trading account, however your broker allows you to trade worth 5 lakh (₹5,00,00) in intraday i.e. up to 10 times your original amount.(which is called “Margin Trading”) What will you like to say? Do you want to make money for your broker?

3rd Phase –

Rohit had burnt his finger in day trading. Now he committed not to repeat the same mistake again. He was now more careful but also highly optimistic to earn from stock market. The only problem was that he had limited funds. He started accumulating few well known stocks and planned to hold on for next few months. His portfolio was showing around 20% gains over 10 months. In this process he had accumulated around 8 lakh. During this time, he came across an attractive offer; “loan against shares”, in which one can keep stocks as collateral for loan. Depending upon the stocks, one can receive loan up to 80% funding of the total net worth. Bank has rights to liquidate collateral stocks if you fail to maintain minimum collateral value.

Rohit didn’t think twice. He was getting around 20% annualized return from stocks. Considering 12% interest rate on bank loan, it was an attractive deal. So, he kept his entire investment as collateral and didn’t hesitate to take loan. Things were going fine as long as the market was moving in the upward direction. Rohit was happy to notice that his investment was growing at exponential rate. For every percentage increase in share value, bank was ready to provide additional loans. Rohit was planning for more leveraged position. While everything was going smooth, stock market suddenly took a U-turn. Within 10 days his portfolio value dropped by around 20%. Rohit was supposed to maintain the collateral amount but with further market downfall he was in big crisis.

He was forced to sell a part of his investment to maintain collateral. Things were worsening. Market continued its downward journey. There was a wide spread pessimism. Equity analysts, who were predicting big targets just few months back, were also expressing their bearish view. Rohit was not able to swallow the decline in this investment. Meanwhile, bank continued to pressurize for maintaining collateral. Things were moving out of control. Finally Rohit sold his entire investment, mainly due to fear and pressure from bank. Over the past 2 years he had accumulated around 10 lakh, just few months ago he was in good gain but he ended up with 25% loss. The entire loss was just because of "forced selling". Had he avoided "loan against shares" scheme, he wouldn't have to force sell his stocks during market downturn.

Where was he wrong?

Investing in stocks from borrowed money is a dangerous practice unless you have enough expertise on the subject. This practice can exponentially increase your gain as well as multiply your loss. Almost all sophisticated investors leverage their position. They know risk management, they know when and how much to leverage and above all they have in-depth understanding on the subject. Figure out whether you have enough expertise or not. For retail investors, it is better to stay away from loan against share. During bull-run any investor can do well, but what separates the intelligent investors from the rest is the ability to minimize loss during market meltdown. Retail investors tend to go for "loan against shares" during bull-run. After 1-2 years of good return, you start believing that you have mastered the game and then market will teach you a lesson. Leveraged position can even create bankrupt situation during market fall. So it is always better for retail investors to avoid the same.

4th Phase –

Enough is enough. After 3 unsuccessful attempts Rohit decided to go with any professional stock tips provider. He did a Google search and found so many names. All most all of them claimed 90%+ success ratio and showcased fabulous past performance. He was confused and so he subscribed for 3 days trial from various stock tips provider. After 3 days trial, he started receiving many phone calls from them. One such service provider mentioned that he can make money not only when the market goes up but also when market goes down through "Futures and Options." Rohit was surprised. Earlier, he had suffered loss mainly during market crash. So, "making money while market will go down" was attractive enough to catch his attention. He was eager to avail the services provided by that stock tips provider. The only problem was that they were asking for a huge subscription amount. He delayed his decision. On the other hand, they kept on calling him and insisted on joining the package. Finally, they agreed to provide “2 trial calls”. Surprisingly, both the calls hit the target. Moreover, they assured 100%+ monthly return from their “Futures and Options” trading call. Rohit was highly convinced. He paid ₹ 30,000 as subscription amount for highly profitable “Futures and Options” call.

He was ready to dedicate five lakh (5,00,000) to start with. He started with ₹ 3 lakh (3,00,000) on the first call. Surprisingly it was showing 50% gain within 15 days. He realized the magic of “future trading” and decided to put extra fund. He had made handsome gain from the first call and was eagerly waiting for the next call. As expected, he invested the larger amount in the next “trading tips”. What he didn’t realize was the uncertainty that Futures & Options (F&O) carries. No doubt, F&O can provide extraordinary return but at the same time it can also lead to “unlimited loss”.

For every correct bet, you can earn 50%- 100% whereas a wrong bet can lead to 100% loss. The same happened with Rohit. He had earned 50% return within 15 days from the first “trading call” and lost 90% from the second call in the next 20 days.

Where was he wrong?

Trading in “Futures and Options” is the worst ever decision for any retail investor. You can lose your entire life’s savings. Many analysts or stock tips provider will claim that one can earn up to 100% return within a month from “Future” trading. My question is why they themselves don’t trade? What’s the necessity of selling “tips” when you can earn 100% monthly return from your own analysis? If you can take a bank loan of 10 lakh and earn 100% monthly return then after repaying bank loan you can become a billionaire within a 2-3 years. Now show me a single person, who turned billionaire through “Futures and Options” trading. You won’t find a single person throughout the world.

Next time onwards, if any stock tips provider tempts you for “Futures and Options” (F&O) trading, simply mention them the above statement. Just conduct a Google search, you will find many stock tips providers claiming such extraordinary return from their trading calls while reality says something different. Don’t be get trapped. Stay away from stock tips provider who claim extraordinary return.

Basically, F&O is meant for institutional investors and hedge fund. They are the one to get benefited from this option. Big companies or high net worth individuals hedge their position using F&O. Future trading is a great option for hedging. Retail investors, who jump in F&O for extraordinary returns will surely end up with lots of disappointment.

> "Intraday, short term trading and F&O — all those are nothing but another form of gambling."

1.3 Sure shot way to lose money in stock market

From the earlier stated example, you are now aware of the certain methods to lose money. Summarizing the above topic stands as "Retail investors will lose money (most likely) from trading in stock market". Here "trading" refers to intraday, Futures and Options and all other activities where you purchase stocks to sell and generate a profit within 1-15 days. "Retail investors" refers to the individuals engaged in some other full-time profession and investing a portion of their savings into the stock market.

Why trading is a sure-shot way to lose money for retail investors?

Trading is meant for institutional investors and hedge funds. They can only make money. Being a retail investor, you can make money from one, two or three successful trade but a single unsuccessful trade will erase your entire gain. Following are the reasons why trading is a sure-shot way to lose money for retail investors –

You don't have enough expertise and time – It requires huge knowledge, experience, time and discipline to earn consistently from trading. Admit it; you don't have that amount of knowledge, experience, and discipline. Most importantly, retail investors can't dedicate a huge amount of time as they are already engaged in some other full-time profession. Being a retail investor, if you believe that you are wise enough for trading, then you should immediately leave your job and apply for the job of a professional trader. There is a real shortage of quality professional traders in the industry!

Simply putting, if you engage in some other full-time job and still want to trade with your own brain then you are one-step closer to losing money.

Consider brokerage and taxes while calculating profit and loss:-

Suppose you purchase a stock at ₹100 and after few days you sell it at ₹110. Apparently, it seems you earned ₹10. However the story is different.

For every transaction (buying/selling) you need to pay brokerage, Security Transaction Tax (STT), Service Tax and exchange charge. The list does not end here. You also need to pay Short Term Capital Gain Tax (15% of profit in India) to the government. Normally we don’t consider these fees while calculating profit or loss. Let’s calculate net profit and loss in two different cases. In the first transaction, consider buy rate as ₹100 and sell rate as ₹110; i.e. gross gain of ₹10. In the second one, purchase rate as ₹100 and sell rate as ₹90; i.e. gross loss of ₹10. To simplify the calculation, I am considering 1% on total turnover as brokerage+ STT+ service tax+ exchange charge. So, you need to pay ₹ 1 on every ₹ 100 both for your buying and selling transactions.

Net Profit and loss calculation from trading		
	1st Transaction	2nd Transaction
Buy Rate	100	100
Sell Rate	110	90
Gross Profit/Loss	10	-10
Brokerage + STT+ Service tax+ Exchange charge (Both on Buy and Sell side)	1+1=2	1+1=2
Short Term Capital Gain Tax (15% on profit)	1.5	Nil
Net Profit/Loss	Net Gain (10-2-1.5)=6.5	Net Loss (10+2)=12

The above table depicts a surprising result. Gross profit of ₹10 turns into net profit of only ₹6.5 where as gross loss of ₹10 turns into net loss of ₹12. So, 10% gross profit is originally 6.5% net gain where as 10% loss is originally 12% loss.

Do you calculate net profit and loss in such a way?

This is one of the most important reasons of losing money in trading. The odds are against you. The system is designed in such a manner that it is next to impossible to make money consistently. Brokers, stock exchange and government – only they can earn consistently from trading. Every time you trade you need to pay all of them. They don't bother whether you are gaining or losing. I hope now the reason is clear why your broker, media and several websites always encourage you to trade frequently. They all want to earn money for themselves, not for you. Do you still want to make them richer?

> "Your broker, stock exchange and government can only become rich from short term trading."

Why free trading tips are dangerous?

Why someone will provide money making ideas (stock tips) at free of cost? In your real life, do you get any quality products/service at free of cost? Nowadays, you need to pay even for pure drinking water! From watching movies to reading newspaper everything comes at a price. Occasionally, retail chains like Big Bazaar, Pantaloons offer free gift voucher. Why? Their motive is to bring back their existing customer.

Tune into any business channels, you will get dozens of free trading tips each day. Your broker is also eager to provide trading tips at free of cost. Moreover, dozens of websites offer bunch of new trading ideas everyday totally free of cost. Including Facebook and Whatsapp groups, the list of free trading tips provider would be very long. None of them are doing charity. None of them have the motive of making you rich. Let's have a detailed look on their motive –

Motive #1 – Many operators provide free trading tips after offering the same to their paid clients. Thus, stock price gets manipulated which in turn helps only their paid clients. Suppose I have two websites; freetips.com and paidtips.com. One is for providing tips to paid clients and another for free clients. However clients don't know that both the websites are operated by the same person (or same group of people). So, what I am doing is, I am offering tips to my paid clients first. After their purchase, I am distributing the same to free subscribers.

While, free subscribers start buying the same stock, the price starts moving in upward direction. Exactly at the same time, I am recommending “Profit Booking/Exit” call to paid clients. Thus, free subscribers get stuck at the top. So, my paid subscribers are getting good return at the cost of free clients. My motive is to collect more subscription fees from paid clients! This way one can easily manipulate the price of lesser known stocks (specially, midcap and small cap stocks).

Motive #2 – Operators often offer free tips just to have a smooth exit at hefty profit. I am providing a real-life example. During 23rd and 24th July, 2014, I received a SMS as follows, “Sure-shot buy call – Buy Naisargik (BSE code -531365) at ₹ 175. Target 350 within few weeks” The company is in microcap category and I didn’t hear the name before than that. Trading volume was much higher on both the days and stock price appreciated a lot. The pattern suggested that the operator had sent the same SMS to thousands of retail investors and many of them purchased the stock. The most surprising fact is that on those days three operators sold around 1,20,000 quantities worth of ₹ 1,97,69,661 (around 2 crores). So, operators were selling a particular stock and simultaneously sending SMS to thousands of retail investors to buy for “sure-shot” target of doubling the money!

In the next 10 days the stock was hitting lower circuit continuously and stock price reached to below ₹ 100. There were no buyers for the same and as a result it got stuck in lower circuit. Just before publishing this book, the stock is traded around ₹4.Thousands of retail investors got stuck lost around 90% or more and expressed their anger in the moneycontrol.com forum.

Check out the historical data from BSE website; check out moneycontrol.com message board discussion. You will find the proof of the entire episode and how thousands of innocent investors got trapped and lost their hard-earned money! Nobody is there to save them. With the advent of mobile phone and internet such practice is quiet common. Be careful from the next time if you receive such SMS!

Why paid trading tips are sometimes more dangerous?

You can lose your investment amount from free trading tips but what about paid tips. Surprisingly paid tips can make you suffer more because in this you not only lose your invested amount but also your subscription amount. Just conduct a basic Google search. You will find several trading tips provider showcase fabulous past performance, promise 50%-100% monthly return and offer 2-3 days free trial. Now I will show you how any stock tips provider can trap you from offering 4 days free trial tips.

How paid stock tips scam works?-

Suppose I develop a website for stock tips scam and offer as follows - "Our latest stock trading strategy can predict the stock price movement with 99.99% accuracy. Join our 4 days free trial for intraday tips and check out yourself how you can earn big from our highly accurate trading calls."

From the statement "4 days Free Trial" many investors will immediately join. I can also purchase database (email-id and mobile numbers) of demat account holders to run this scam. In such manner, I collect mobile number of 5,000 traders. Consider Rohit as one among 5,000 subscribers. Each day I will send a single trading call via SMS. So, here goes my "4 days Free Trial".

Tip 1 (First Day) – Reliance Industries will move up today. Buy Reliance for immediate intraday gain.

Reaction – Reliance really went up. Rohit feels good; however he is confused and not sure. It may be just because of luck. Anyways 3 more free trial calls are left. Let's see what happens.

Tip 2 (Second Day) – Reliance will go down today. Short-sell and gain from intraday. Short sell refers to selling first and then buying at lower rate to gain on the same day.

Reaction – Reliance really moved down. Great, Rohit is amazed with the performance. In spite the market moved up, this particular stock is down! There *m*ust be something with the trading call. His confidence has started building up. If the next tip works, then Rohit can surely invest some money. Now he is excited to receive the next call and verify the performance.

Tip 3 (Third Day) – Reliance will go down today. Short-sell and gain from intraday.

Reaction- Reliance really moved down! Rohit is now surprised. He can't believe 100% accurate call on 3 consecutive days. The strategy is really amazing. He is now ready to trade as per the last (4th tip) free trial tips. He already started calculating on how soon he can make big gain from following such amazing calls. He can't wait for the last free trial tips.

Tip 4 (Fourth and Final day) – Reliance will move up today. Buy for intraday gain.

Reaction – Rohit had put 1,00,000 to make some quick bucks. He was nervous at the beginning as there was no such upward movement in morning trade. However the stock really moved up during afternoon trade and he was in good profit! He booked the entire profit as per the call and was super excited. He made his mind to follow the tips at any costs and thus can easily earn big bucks in short period of time. He is ready to sell his other investments to dedicate the entire sum in trading calls. Rohit can now visualize how he can become a millionaire by subscribing to the tips over next 1-2 years.

4 days Free Trial Tips are over-

Rohit and many such already experienced the magic. 4 consecutive calls and all are perfect. 100% success rate on 4 days trial is really amazing. Now, here my message goes, “You already experienced our 4 days trial and noted how accurately we predict stock price movement. Years of hard work and research helped us in developing such highly accurate strategy. If you want to continue with our daily trading calls, it would cost ₹20,000 for 6 months. You can also subscribe to our 1 year package at discounted rate of ₹30,000 only. You can expect the same accuracy like our “4 free trial calls.”

The subscription amount is bit high but Rohit had already experienced the amazing result. Subscription amount will be easily covered within 1 month of trading and visualizing himself as a millionaire over next 1-2 years, he wants those calls at any cost. With little hesitation, Rohit subscribed to 1 year package of intraday trading calls for ₹30,000.

The tips are coming from the very next day but there is an issue. Somehow, this time not all tips are working. Out of 10 intraday calls 4-5 are working and rest are not. Rohit is fully frustrated. He already had invested a big amount and staring at big loss! Every time he thinks it will work and recover the entire losses, opposite happens. The loss keeps getting wider!

Actually, Rohit got trapped in stock tips scam.

Now, let’s see how this scam actually works. Initially I had 5,000 subscribers. I divide them into two groups (2,500 each) – Group A and Group B. I send “Buy” call to Group A and “Sell” call to Group B. Now, either the stock price will move up or down. So, one of them will be surely correct. I already noted which