

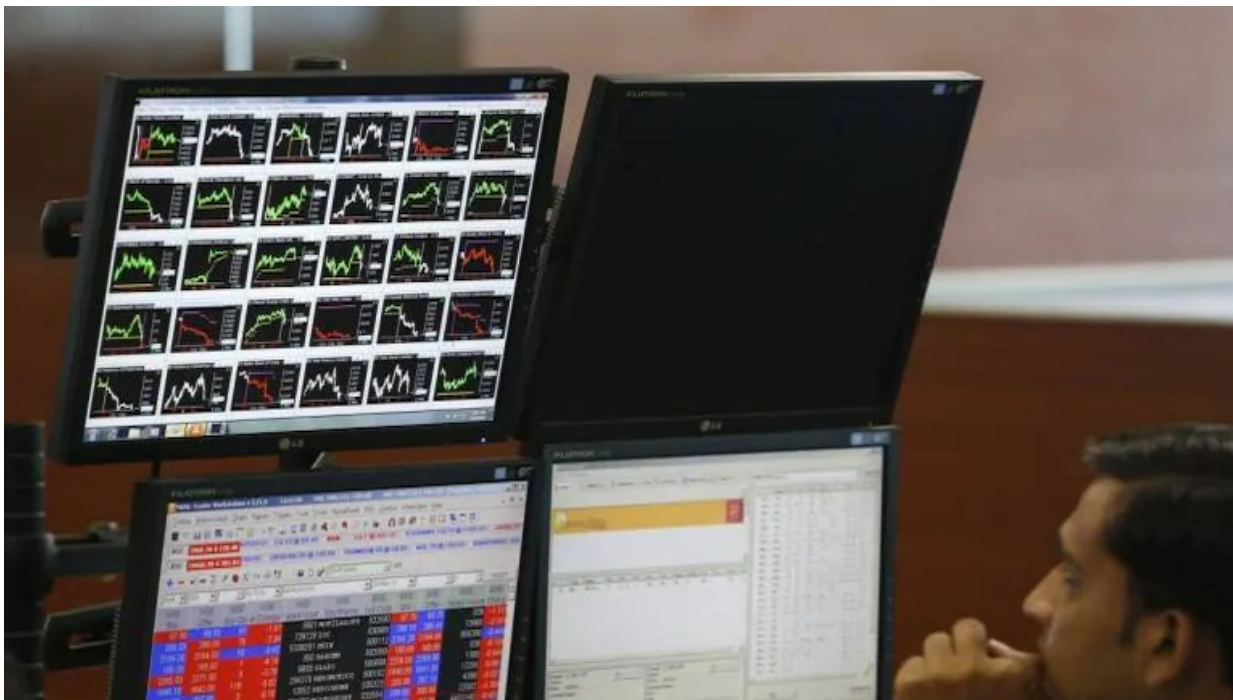
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Here's how retail traders can join the algo bandwagon

While one can learn algo trading, those who do not have the inclination or time to learn can look for SEBI approved algo system providers

SHISHIR ASTHANA | DECEMBER 30, 2020 / 10:36 AM IST



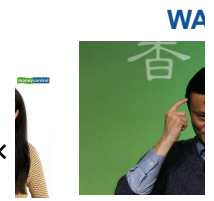
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There are two types of market participant, one who knows what he is doing and another who needs advice or expert help as he does not have the time or the interest to pursue the subject of investing or trading.

For the second type of market participant, the general advice that has been given to them over the years is to let professionals handle their money. Mutual Funds were traditionally the best investment vehicle for them. But these days portfolio management services are being pushed.

While mutual funds have a net asset value (NAV) reporting system every day, PMS services do not have a similar transparent system in place. Nonetheless, as advisors are getting much higher fees from PMS players, they are promoting their products. The option of PMS however, is not open for the retail investor as the minimum requirement set by SEBI is high.

There is, however, one more option that is opening up for retail traders and investor--algo trading or investing.



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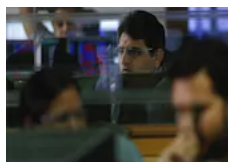
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What is algo trading

In this form trades are taken based on a given set of rules which are converted into instructions to generate trading signals. The output of these algos is taken as an entry or an exit signal.

Say, a very simple algo can give a buy signal when a stock hits a new 52-week high among the Nifty 50 stocks and an exiting signal when a stock hits a two-month low price. When the programmer runs the scanner he will get a few stocks where he can enter and in some other cases, he would get exit signals.

There are many more complex programs that are written and used in the market.

How to participate in algo trading

While one can learn algo trading, those who do not have the inclination or time to learn can look for SEBI approved algo system providers. But just like PMS, there is no transparent mechanism of knowing their true return.

One has to take the data that is put up on the websites of these algo providers at face value, test it for a small period, and then commit a bigger amount to it if one is comfortable with the returns, strategy, and operations. Another way is to reference check the service provider before putting in money.

Algo trading versus algo based recommendations

A point worth mentioning here is some algo or machine learning companies give recommendations to their clients based on their screeners, while others have systems that have programs that trade on behalf of the client after asking for a confirmation to initiate the trade. Depending on the availability of time and operational capability, one can select the type of algo trades they can manage.

Pitfalls

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signing up with a service provider.

Since it is a nascent industry the ground rules are not yet defined and one needs to try and test with small amounts before really jumping into it.

Advantages

Algo trading has one big advantage over manually operated funds – they remove the psychological element of participating. Most trading algos use price as the key input or some derivative of it which takes its value from price. Investing algos also use price as a deciding factor apart from other valuation parameters. Also, trading is said to be more of a psychological game than an intelligent one and algo trading can offer the edge.

Service providers

Let's now look at some system driven investors/traders based on publicly available information. These are randomly selected players in the industry since there is no data source where we can compare various players as yet.

Weekend Investing

Alok Jain's Weekend Investing follows momentum investing and has various products to offer depending on the risk profile of the client. His top-selling product – named Mi ST ATH is a 10 stock portfolio that chases all-time high stocks in momentum. The stocks are chosen from all NSE listed liquid stocks with a market capitalisation of Rs 1,000 crore and above.



Source: Weekend Investing

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receive the adjustments that are needed to be made and have to do it manually.

The reason for outperformance, says Alok Jain, is because all their momentum strategies start reducing exposure as the market falls and go to full cash if the market drop continues. By mid-March, most of their strategies were in cash. As for re-entries when markets pick up there is a lag since momentum strategies wait for upward momentum to be established. Nonetheless, the strategy tends to outperform in a rising market and drawdowns are lower in a falling market.

The chart below shows how Weekend Investing's momentum strategy performs much better in a rising market thanks to a portfolio of top-performing stocks, and more importantly, the drawdown or fall from its peak, is less in a down market.



Source: Weekend Investing

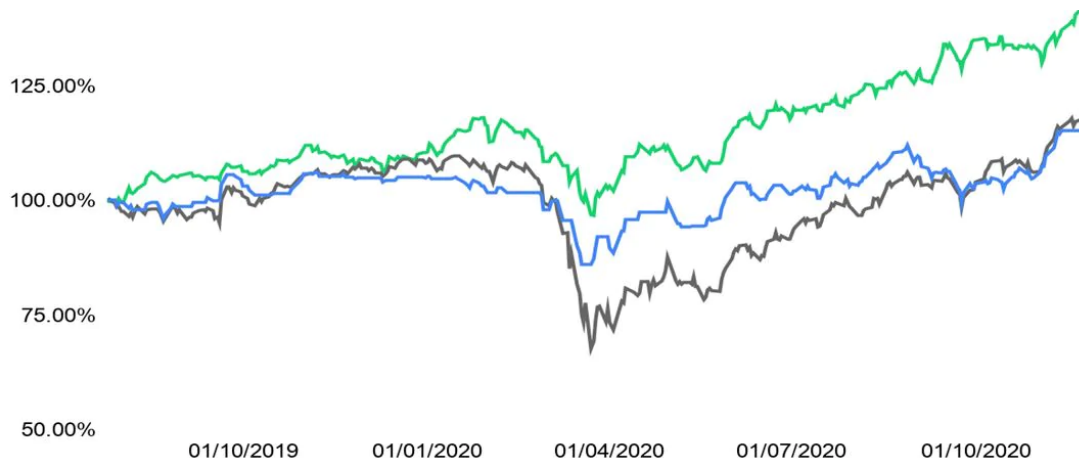
Wright Research

Sonam Srivastava's Wright Research is a quantitative investment management firm. They use statistics and systematic rules to make investment decisions in an automated fashion for running two systematic strategies – Multi Factor Tactical and Statistical Arbitrage.

Multi Factor Tactical

This is a moderate risk long-only strategy that aims to outperform in all stages of the market cycle. This is achieved by dynamic allocation to various equity factor baskets like momentum, growth, volatility, etc along with bonds & gold ETF based on the changing market regime. The strategy has been live for over 16 months and has delivered a consistent outperformance of over 20 percent in this period, not only in the bullish phases but also during the drawdowns in March, with a much lower risk than the market. In the current calendar year, the strategy has delivered a 79.66 percent return.

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Source: Wright Research

Statistical Arbitrage

This is a Long-Short strategy, which is a quantitative market-neutral strategy on stock derivatives based on various factors in the market combined using machine learning techniques. This is a leveraged strategy recommended only for investors with a high-risk appetite. This portfolio is expected to generate consistent returns over time that are uncorrelated to the market. The strategy has been live for 6 months and has delivered an annualised return of 75.3 percent with a 4.69 percent drawdown as compared to 21.7 percent growth in Nifty with a 6.7 percent drawdown.

Squareoff.in

Kirubakaran Rajendran's Squareoff.in offers trading bots to its clients to trade intra-day strategies without any manual intervention on part of the client. These fully automated intra-day trading strategies too have performed reasonably well over the last one year.

According to Rajendran, the cumulative return of their clients on this strategy is 30 percent on an unleveraged basis for the year. But if one considers the 10 times leverage that clients use with the brokers that are empanelled for such bots, the returns are much higher.

Trade Tron

Umesh Ranglani's website is an algo strategy marketplace that helps traders create their own algos for a small fee apart from showcasing algos of other traders which can be purchased for a fee. The good part of the site is one need not know any coding to create an algo. The company engineers help create the algo.

Conclusion

With nearly 90 percent of all orders seen on the terminal and over 50 percent orders executed being done by algo trading, retail traders need to equip themselves to compete with the machines. There are boutique offerings available in India which can offer a good testing ground apart from being a new avenue for participating in the market.

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TAGS: #algo trading #algorithm trading #algorithms #Squareoff #Trade Tron #Weekend Investing #Wright Research

FIRST PUBLISHED: DEC 30, 2020 10:36 AM

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