Reading a stock chart against its index and its sector

RELATIVE STRENGTH

A name's performance measured against its index or sector rather than in isolation: the stock divided by the benchmark, charted. It is the reading tool that implements module 1's decomposition - stripping the market and sector layers so the chart shows only the part that is about the company.

Module 1 said a stock's day is mostly not about the stock. This lesson is the chart-reading version: never read a single name naked.

The three-chart habit

The name's own chart: what happened - the raw series everyone watches.The name against its index: the ratio line - rising when the stock beats its market, whatever direction both moved. A stock down 1% on a day the index fell 3% is outperforming, and only the ratio shows it.The name against its sector: the sharper ratio - peers share the industry tide, so beating the sector is the closest chartable proxy for 'something is genuinely different here'.

What relative reading catches that absolute reading cannot

Persistent relative strength through a falling market is the classic tell that lesson 6 of module 1 predicted: the name layer pulling against the tide - visible for weeks in the ratio while the raw chart just looks like everything else, only shallower.The reverse reads too: a name that cannot rise on its sector's good days is being sold into strength by someone, and the raw chart hides that entirely. Neither reading is a signal; both are exactly the kind of observation module 5 will demand a mechanism for.

The practical setup

Every serious equity chart carries its benchmark: either the ratio line below the price, or the index overlaid.Which benchmark is a real choice - the index for the market layer, the sector for the industry layer - and reading both ratios locates the move in module 1's decomposition within seconds.The discipline costs one extra pane and removes the single commonest equity reading error: crediting a company for its market's day.

Check your understanding

1. A stock falls 1% while its index falls 3%. What does the ratio chart show, and why does it matter?

a. A falling line - the stock lost money

b. A rising line - the name outperformed by two points, which the raw chart cannot show and module 1's decomposition says is the informative part

c. A flat line - both fell

Answer: b. Relative strength strips the market layer. Outperformance through weakness is the name layer speaking - visible only in the ratio, and the kind of observation worth a mechanism hunt.

2. Why is the sector ratio a sharper read than the index ratio?

a. Sectors are calculated more accurately

b. Peers share the industry tide, so beating the sector isolates the name layer more tightly than beating the broad market does

c. Sector data updates faster

Answer: b. The index ratio removes one layer; the sector ratio removes two. What remains after both is the closest chartable proxy for company-specific difference.