mint
June 18, 2024

Devina Mehra feels THIS is the reason why you should book profit in micro, smallcap stocks

Nishant Kumar

Devina Mehra of First Global believes several micro and smallcap stocks are at unreasonable valuations and cautions investors against them, especially those with a market cap below ₹5,000 crore.

Devina Mehra, the founder, chairperson, and managing director of First Global, said microcap and smallcap stocks can be very volatile and difficult to manage due to the lack of effective risk management tools. **(Agencies)**

Devina Mehra, the founder, chairperson, and managing director of First Global, believes several micro and smallcap stocks are at unreasonable valuations and cautions investors against them, especially those with a market cap below ₹5,000 crore.

Mehra highlighted the risks associated with investing in microcap and smallcap stocks in an exclusive interview with Mint. She said microcap and smallcap stocks can be very volatile and difficult to manage due to the lack of effective risk management tools like Nifty options and stop losses.

"I certainly think that if you look at microcaps and stocks below ₹5,000 crore market cap, there is more than a little froth there, and investors should limit their exposure there. It is also because risk management measures do not work well for this segment as neither can you hedge those via Nifty options (as those stocks do not necessarily move with the Nifty), nor do stop losses work well here as the stocks can fall very rapidly without allowing you to sell," said Mehra.

Equity benchmark Sensex has gained over 21 per cent in the last one year. On the other hand, the BSE Midcap index has surged 63 per cent, while the BSE Smallcap index has jumped 59 per cent in the same period.

Mehra observed in the case of a bust in the smallcap space, several stocks from the segment never came back.

"In every small cap bust, hundreds of stocks disappear, never to come back again. The Smallcap index fell 78 per cent in 2008-2009 and did not recover those levels for eight years. Even though the index crossed those levels in 2016, the composition was completely different. Many stocks that fell never came back. After a one-and-a-half-year boom, there was another two-thirds fall in the Smallcap index," said Mehra.

Short periods of boom in the small-cap space may lure many investors, but Mehra points out that investors should look at the broader picture and avoid getting carried away by short-term trends.

"When something falls 80 per cent, it can compound 50 per cent for three years, and at the end, you will still be down 33 per cent. Remember this when smallcap managers and advisors tell you they have compounded 50 or 60 per cent for two or three years. If you go back five or seven years, the picture may be completely different," said Mehra.

"This is a risky area of the market, and if you are lucky enough to have made money here, book most of your profits and reinvest in steadier stocks," Mehra said.