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Stay invested, be hedged, prefer largecaps: Devina Mehra decodes stock market trading strategy amid high volatility

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Mehra believes there may be volatility in the Indian share market for the short term. To mitigate this, she suggests remaining fully invested but buy insurance via hedges to manage potential downsides. This strategy may incur costs, but is a prudent measure to avoid significant losses.

While Devina Mehra remains positive on the large caps and some parts of the midcap universe, she has severely cut back exposure to stocks with market capitalisation below ₹5,000 crore.

With the Indian stock market hitting all-time high amid heightened volatility, investors are often left wondering how to navigate these uncertain waters. Devina Mehra, Founder and Chairperson of First Global, has offered a nuanced approach and discussed her strategy of positioning the portfolios in her PMS.

In a post on social media platform X, Mehra said she remains positive on the market in the medium term.

Giving a historical context, Mehra highlighted the lackluster performance of the Indian stock market from 2010 to 2020, where a ₹100 investment grew to just ₹230, barely outpacing fixed deposit returns. This contrasts sharply with the 1980s, when a ₹100 investment soared to ₹700.

Given this historical underperformance, Mehra believes there's still room for growth and despite the recent market surge post-COVID, she believes there is a potential for more upward movement.

“This is the reason why I remain positive on the markets as even after the run up post Covid lows, we are not even close to the trend line, let alone above it.

Risk management amid volatility

However, Mehra believes there may be volatility in the Indian share market for the short term. To mitigate this, she suggests remaining fully invested but buy insurance via hedges to manage potential downsides. This strategy may incur costs, but is a prudent measure to avoid significant losses.

She emphasized the importance of staying invested to capture market gains, noting that missing just one of the best days each year can drastically reduce overall returns.

"And while some volatility is possible, a sustained down move is not what we are looking at and hence we have not moved into cash because the other thing to remember is that while there is a risk to being invested in the market, there is also not being invested and missing out on an up move. If you miss out, on the average, even ONE day a year (the best day for that year) you miss out on 90% of the market move. That is what data shows us," she wrote in the post.

In short, when you are positive in the medium term but there can be some ups and downs in the short term, the best strategy is to remain invested, but to be hedged, she added.

Market cap dimension

While this was the time dimension to look at your portfolio, the second way is to look at the market cap stratification, according to Mehra. Here, Mehra advises caution with small-cap stocks.

While she remains positive on the large caps and some parts of the midcap universe, she has severely cut back exposure to stocks with market capitalisation below ₹5,000 crore.

According to her, this is a segment that has done extremely well for the last 18 months or so but also where the risk is building up. She also does not look at stocks below ₹1,000 crore market cap for her PMS or Smallcase but has cut back severely in the ₹1,000 - 5,000 crore market-cap as well.

"Again it comes down to risk management. While this strategy may have cost us some performance points vis a vis our more aggressive competitors, our first focus always is to preserve the capital, the hard-earned money, of our investors," she said.

Risk management comes first and in small caps risk management via stop loss levels does not work as well because when those stocks fall often there is no exit, she added

Historical data supports this caution. In 2008 - 2009 the small cap index fell 78%. It reached those levels after 8 years.

However, this was also only theoretical as components of the index had completely changed by then, Mehra noted. Further, there was another 65% fall in 2018-19.

"Also remember if something falls 80% and then compounds 50% each year for 3 years, you would still be down one third from your original investment. Outlier returns in any segment of the market do not last forever. Therefore time to be very careful on the frothy areas of the market," Mehra said.