Do not go short on Sensex post China rout, buy largecaps

By *Kshitij Anand*, ECONOMICTIMES.COM | 4 Jan, 2016, 04.13PM IST

Post a Comment

NEW DELHI: The S&P BSE Sensex plunged over 500 points on Monday in line with other Asian as well as European markets, which came under heavy selling pressure after official data showed a contraction in China's factory activity and the yuan weakened to a near five-year low.

The Nifty50 took a knock of nearly 200 points to register its worst percentage fall since November 9, 2015.

But analysts say it was more of a kneejerk reaction, and investors should not try and go short on the market after Monday's crash.

The S&P BSE Sensex broke below its crucial psychological support level of 26,000, led by losses in bank, realty, IT, capital goods and telecom stocks. It finally closed 537 points, or 2.05 per cent, lower at 25,623.35.

The Nifty50 finally closed 171.90 points or 2.16 per cent down at 7,791.30. It hit a low of 7,924.55 and a high of 7,937.55 during the day.

Slowdown fears in the world's second largest economy and a further devaluation of its currency are keeping markets across the globe on the edge.

The Chinese stock market plunged about 7 per cent on Monday, triggering the lower circuit, after data released in the morning showed Chinese manufacturing PMI for December declined to 48.2 compared with 48.6 in November.

"For India, it is a kneejerk reaction, But, whether it extends further or not will depend on the Chinese reaction. It is a given that they have been devaluing their currency, which is already causing panic around the world," market expert Ajay Bagga said in an interview with ET Now.

"They should come out with some stimulus later this week, that is my expectation. They have already cut interest rates multiple times. I am now expecting more active intervention," he added.

Bagga said there might be a couple of days of more weakness, but it is still better to stand on the sidelines. It's not the time to short the market, because the cuts are already there.

If traders go short from current level, they could get caught on the wrong side of the trade in case there is a whipsaw and the market moves back, experts cautioned.

Going by options data, fresh Call writing was seen in out-of-the-money contracts of strike prices 8,100 and 8,400, which suggest traders do not expect the market to scale this level anytime soon.

The index will face resistance around the 8,000 mark, which has a total OI of 33.71 lakh contracts, followed by strike price 8,100, which has a total Call OI of 37.51 lakh contracts, and then at 8,200, which has maximum Call OI of 47.06 lakh contracts as of Friday.

There was good support for the market at strike price 7,800, where there was good buildup of Put OI. Now the index has breached the 7,900 mark and it is more likely to bounce back from its strong support level at 7,800, which had maximum Put OI of 31.30 lakh contracts as of Friday.

"Nobody expected the Chinese market to fall 7 per cent and shut down there. I am sure that is having a huge impact on global markets; Europe is down, US futures are showing significant downtrend, which could cause the US markets to open lower," independent market expert Sudip Bandyopadhyay said in an interview with ET Now.

"Already the fall in the Indian market looks a bit overdone. I would not be surprised if some amount of recovery starts coming in at some stage," he said.

The China issue is big, but another factor that took the domestic market down was a sharp drop in India's own manufacturing output, which hit a 28-month low in December. The Nikkei India Manufacturing PMI, a composite monthly indicator of manufacturing performance, dipped from 50.3 in November to 49.1 in December.

This is the lowest level for the index since March 2013.

How to play the market now:

The dragon seems to be slowing down, and the impact of this on other global markets is going to be pretty evident. The Indian market lost about 5 per cent in calendar 2015, and the right investment strategy from here on would be to remain stock specific in the largecap space, experts said.

The Indian market is not cheap, but a further dip can actually make it more attractive. But a number of largecap stocks corrected about 10-20 per cent during calendar 2015.

"We think a bigger opportunity lies in the largecap space. As far as our models are concerned, midcap is a place where you will get a lot of undervalued stocks. But you have to be very careful since they are not as undervalued as the largecaps," said Vikas V Gupta, Executive VP, Arthveda Fund Management.

One of the standout themes of calendar 2015 was the $11 billion investment that domestic mutual funds made in equities in 2015, up from about $4 billion in 2014.

The benchmark indices might not do a whole lot, but for adventurous investors, stock-specific opportunities do exist as the real estate market is slowing down and gold has failed to glitter.

Analysts expect equities to continue attracting a growing share of Indian household savings. Equity-oriented mutual funds would remain their preferred vehicle for equity exposure. "Calendar 2016 would be as good a year for anyone, who wants to begin investing in equities. For the more adventurous investors, who wish to invest in stocks directly, there is a wide array of ideas to choose from. In my experience, success in equity investing is more about picking the right stocks than about getting the timing right," said Motilal Oswal, Chairman & MD, MOFSL.

"Bajaj Finance, Sun Pharma, SBI, ONGC and InterGlobe Aviation are the five largecap stocks to watch out for. Among the smallcaps, I would bet on Alkem Labs, DFM Foods, Astra Micro, Eveready and Lincoln Pharma," he said.