WHAT INVESTORS SHOULD DO

Markets are down and portfolios are bleeding. Experts tell you how to make the most of this bearishness.

Though there will be short to medium term pain, a bear market is also an opportunity for long-term investors. A closer look at the previous eight-year cycles shows that there have been real bull markets and fake bull markets. While the bull market till 1992 generated compounded annual returns of 37%, the next eight years generated a paltry 4% per year. Similarly, the bull market till 2008 generated 17% CAGR, but the next bull market till 2015 that took the Sensex to 30,000 plus levels have generated only 5% CAGR. Most experts feel that the next bull market is going to be a really big one. "Somewhere during the stress, the next bull market will start and the next leg of the bull market is going to be very powerful," says Mehraboon Irani, Principal & Head (PCG), Nirmal Bang Securities.

However, this is not the time to buy because the bottom formation of the next bull market is going to take time. "Don't expect a V shaped recovery from current levels. The recovery will be U shaped, that too with an extended bottom," says Kunj Bansal, Executive Director & CIO, Centrum Capital. Historically, the broader market valuation also comes down significantly before the next bull phase starts. The Sensex PE has fallen to its 20-year average (see chart) so there is scope for a further decline.

BE SELECTIVE IN STOCK PICKS

Investors should not buy a stock just because it has fallen too much. Experts say that investors should maintain a portfolio of good quality stocks. "Start accumulating stocks where the results are looking strong or where the Government policy impetus is likely to drive growth," says Dipen Shah, Senior Vice President & Head of Private Client Group Research, Kotak Securities. On his radar are large-cap IT stocks and select road construction companies.

SWITCH TO LARGE-CAPS

Until recently, mid-cap stocks were zooming even as large-cap stocks languished. This was because foreign investors, who mostly invest in frontline stocks, were selling these as part of a broader emerging market strategy. Meanwhile domestic mutual funds, armed with continuing inflows from local investors to their mid-cap schemes, were pumping this money into a basket of mid-cap stocks. Traditionally, large-cap stocks trade at premium to mid-caps, but the mid-cap valuation went above the large cap in the recent past (see chart).

Though the recent carnage in mid caps has brought their valuation below the large caps, experts reckon that the large-cap universe still offers a good investing opportunity. Feroze Azeez, Deputy CEO, Private Wealth Management at Anand Rathi Financial Services, insists further buying into mid-caps is not advisable. "I strongly advocate investors stick to large-cap stocks as the risk-reward payoff is skewed toward this segment." Vikas Gupta, Executive VP, Traded Markets, Arthveda Fund Manage-

Dynamic allocation funds have done well

		RETURN (%)	
SCHEME NAME	AUM(CR.)	3 YEARS	5 YEARS
ICICI Pru Dynamic Plan-Reg	5,547	11.3	9.3
Franklin India Dynamic PE Ratio FOFs	753	8.9	8.8
Religare Invesco Dynamic Equity	87	13.0	9.5
HSBC Dynamic	56	4.9	3.5
DHFL Pramerica Dynamic Asset Allocation	28	4.2	3.9

Data as on 20 Jan 2016

Compiled by ETIG Database; Source: Ace MF ment, also feels large-caps are the place to be as these are significantly undervalued relative to mid-cap stocks. He suggests large-cap IT stocks as these are cash rich, priced attractively and likely to benefit from the rupee depreciation.

Similarly, mutual fund investors should also go with large cap funds. But those holding mid-cap oriented funds should remain invested rather than switching to a different category. "Mid-cap stocks do tend to be more volatile compared to large-caps. But if you invested in this category on the premise that India's recovery is likely to play out over a 3-5 year period, there is no reason to change your mind now," argues Arun Gopalan, VP-Research, Systematix Shares & Stocks.

BE READY FOR SECTOR ROTATION

The top performing sectors change in every bull market. It was banks and commodities that led the 1992 and 2008 rallies. Similarly, the FMCG, pharma and IT sectors were running the show in the 2000 and 2015 rallies. Investors should look at beaten down sectors now and enter when stock prices reach reasonable levels. There is more pain in store for commodities, so leave them alone for the time being. However, PSU banks are a good buying option now. "The price to book ratio of some PSU banks has fallen to 0.3-0.4 times. Investors with a 1-2 year investing horizon can consider buying them," says Ajay Bagga, Executive Chairman, OPC Asset Solutions.

INSURE YOUR PORTFOLIO

Since the market is expected to be volatile in 2016, investors also need to insure their portfolios. Investors with large and well diversified portfolio should consider hedging their portfolio with Nifty out-of-the-money put options to protect their existing holdings from further erosion. A similar strategy is possible for investors who are planning to get in at current level also. Even if you identify a very good stock, experts advise you not to jump in now without any protection. "If you want to buy a stock, you should buy a call option which will give you the upside while the downside is protected," says Mathews.

DYNAMIC ALLOCATION APPROACH

Investors also need to manage their portfolio more dynamically. Small investors may not have the time or the ability to do this. Their best option are the schemes that follow a dynamic asset allocation. They have a higher allocation to debt when markets are at highs and get into equities when markets are undervalued. Due to its lower volatility, this category is best suited for risk averse investors. "For retail investors, the easiest way to use the asset allocation

"Somewhere during the stress, the next bull run will start. The next leg will be very powerful."

MEHRABOON IRANI
PRINCIPAL & HEAD (PCG), NIRMAL BANG SECURITIES

"Stagger investments over the next 3-6 months through a mix of large and midcap funds."

KAUSTUBH BELAPURKAR
DIRECTOR – FUND RESEARCH, MORNINGSTAR INDIA.

mechanism is through dynamic asset allocation funds. These funds are structured to invest in equities when markets are cheap and book profits when markets are rising", says Nimesh Shah, MD and CEO, ICICI Prudential AMC.

BE A DISCIPLINED INVESTOR

All these strategies need active participation. Small investors who are not able to do so should continue with their SIPs to make the most out of the upcoming market volatility. This may seem like an oft-repeated dictum, but experts insist that the right approach at this time is to maintain one's asset allocation. It is a time-tested principle of investing which has proven its value over multiple market cycles. Simply put, it helps you average out purchase price over a period of time while capturing more units when prices are low and less when prices are high. When the market bounces back, the units bought at lower levels provide a huge boost to the overall return. "This is perhaps the best time to start a SIP if you have not already done so as your instalments will begin when pessimism is about to peak out," says Gopalan. Kaustubh Belapurkar, Director – Fund Research, Morningstar India, says, "Stagger your investments over the next 3-6 months through a mix of large and midcap funds, preferably in the ratio of 70-30% depending on your risk profile."