Little Risk of a Big Crash, But Tread Safely on D-St

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In my 30 years of being in the markets, I have never made an equity index projection for New Year or Diwali! This is in the category of what Daniel Kahnemann calls 'Objective Ignorance' — something that you not only do not know but also cannot know. My current view is that the risk of a big crash in the stock market remains low, but you should limit exposure to the risky ends of the market like small caps.

Indian equities have been far below the 15-16% average compounding for years. In 2010-20, the compounding was only 8.8% — barely above fixed deposit returns. A ₹100 investment would have become ₹230 over this decade. Contrast this with ₹100 invested in 1980 that would have become ₹700 over a decade.

In short, the equity market was far below the trend line at the beginning of this decade, and even since then, the mainstream indices have not given returns that would even bring them to the trend line, let alone above it. In such a situation, the risk of a crash is minimal.

The corollary to that is that you should remain invested for whatever is your equity allocation. As an aside, I do not recommend a 100% equity allocation for even a young person in a good job. However, caution is advised on the small-cap side where indices are up 45-55% this year. What many newcomers to the market do not understand is the kind of sharp falls this segment of the market can see. For example, the smallcap index had a near-80% fall in 2008-09, reached that level again only in 2016, and then fell 65% again in 2018. Not only that, in smallcaps, a good number of companies simply fall off the radar, never to return. Therefore, limit your exposure to the risky ends of the market like smallcaps, microcaps, IPOs, etc.