Value Research

Mutual Fund Insight

January 2026 ₹200

Complete Personal Finance Guide

Crash coming?

How to survive the 3 biggest risks

NIRMAY CHOKSI

Why low volatility is not a substitute for quality?

How low volatility and quality work better together than alone

In markets that swing harder and faster than most investors like, two ideas have risen to the top of the "defensive" playbook: low volatility for a smoother ride, and quality for sturdier businesses. Their popularity makes sense. What complicates matters is that the two have historically moved together, showing a correlation of about 0.83.

This has led many investors to treat them as near substitutes. They aren't, and the difference is more meaningful than it first appears.

Low-volatility investing

The strategy is built on the behaviour of prices. It uses standard deviation, semi-deviation, beta, or other parameters to identify stocks that move less than the broader market. This stability offers clear benefits: gentler drawdowns, smoother return paths and often better risk-adjusted outcomes over time.

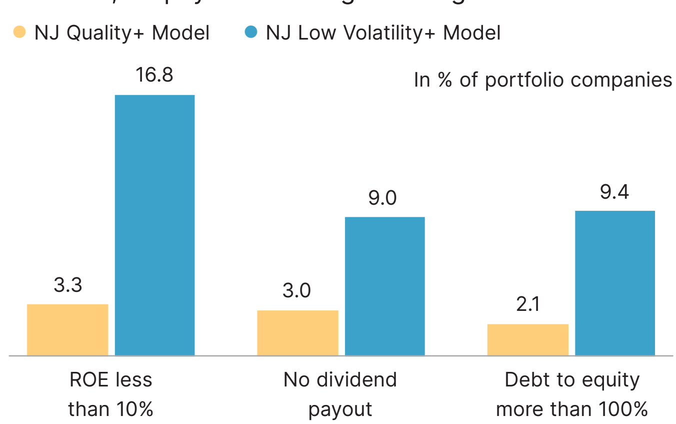
But the factor has limits. Because it operates purely through market behaviour, it can pick stocks that look calm for reasons unrelated to business strength. Illiquid companies, stagnant businesses or simply overlooked names may all qualify. And in strong bull phases, when markets reward aggression, low-vol portfolios generally lag. So, while low volatility can be a sign of quality, it should never be a substitute for assessing fundamental strength.

Quality: The other side of safety

Quality investing looks at the engine, not the dashboard. It emphasises companies with consistent ROE, stable earnings, low leverage, reasonable payouts and disciplined capital

When stability masks weakness

Low-volatility portfolios can include businesses with low ROE, no payouts and high leverage



Source: CMIE, NJ Asset Management Private Limited Internal Research, and NJ's Smart Beta Platform (an in-house proprietary model of NJ AMC). Calculations are for the period September 30, 2020 to November 30, 2025. Debt to Equity is calculated on non-lending companies. NJ Quality+ Model and NJ Low Volatility+ Model are in-house proprietary methodologies developed by NJ AMC. These methodologies are dynamic in nature and will continue to evolve with ongoing research and insights, and may be updated from time to time. Past data may or may not be sustained in the future and is not an indication of future return.

Where strength meets stability

Blending quality and low volatility improves both resilience and outcomes

Portfolio	Annualised return (%)	Sharpe ratio	Annualised volatility (%)	Maximum drawdown (%)	3 year loss probability (%)	Median rolling return (% pa)			
						1 yr	3 yrs	5 yrs	10 yrs
High Quality Low Vol. Stocks	20.2	0.8	13.3	-41.9	0.3	16.8	23.3	23.6	20.7
High Quality High Vol. Stocks	18.0	0.5	22.1	-68.9	6.9	14.8	18.9	16.4	17.7
NJ Quality+ Model	19.1	0.6	16.8	-59.1	1.1	15.8	21.9	19.6	19.9
NJ Low Vol. Model	17.6	0.6	14.4	-52.6	0.5	15.0	19.3	18.0	18.0
Nifty 500 TRI	12.7	0.3	19.9	-63.7	4.0	10.9	13.5	13.2	13.5

Source: CMIE, NJ Asset Management Private Limited Internal Research, and NJ's Smart Beta Platform (an in-house proprietary model of NJ AMC). Calculations are for the period September 30, 2006, to November 30, 2025. High Quality Low Vol. Stocks and High Quality High Vol. Stocks represent the top and bottom tercile (33 per cent) stocks based on volatility ranking. NJ Quality+ Model and NJ Low Volatility Model are in-house proprietary methodologies developed by NJ AMC. These methodologies are dynamic in nature and will continue to evolve with ongoing research and insights, and may be updated from time to time. Past data may or may not be sustained in the future and is not an indication of future return.

allocation—traits that support durability through cycles.

Historically, quality companies tend to be less volatile and protect investors during market downturns; they may become more volatile in the short run, as markets debate valuations or earnings prospects. Quality, therefore, addresses fundamental risk rather than price behaviour, a different kind of protection.

Breaking the myth: Low-volatility ≠ Quality

Much of the confusion comes from treating these two factors of risk as identical. Low volatility manages how a stock trades, while quality manages how the business performs. One reflects market temperament and the other reflects business strength, and using them interchangeably blurs a crucial line.

The graph titled "When stability masks weakness" makes this contrast clear. It compares the NJ Quality+ Model and the NJ Low Volatility+ Model across three guages of quality: low ROE, no dividend payout and high leverage. Pure low-vol portfolios include far more companies with weaker fundamentals, showing that calm prices do not necessarily mean strong businesses.

This is the core distinction. Low-volatility stocks can appear stable for reasons unrelated to quality, and quality stocks can be volatile for reasons unrelated to risk.

Strong fundamentals and steady prices together build resilience across various market cycles

When strong meets steady

Since both factors solve a different problem, combining them creates a more well-rounded approach. Low volatility helps investors stay invested without emotional strain, while quality ensures the underlying businesses continue to compound. Together, they create a more balanced and resilient core.

The table titled "Where strength meets stability" illustrates this synergy. Across returns, volatility, drawdowns, and rolling outcomes, high-quality, low-volatility portfolios stand apart from pure-quality, pure-low-vol, and the broader market. They offer greater consistency and stability, helping investors ride through market noise and providing resilience across cycles.

Conclusion

Low volatility and quality are complementary, not interchangeable. One cushions the journey, while the other strengthens the destination. Together, they offer an effective defence against the forces investors struggle with most: erratic prices and uneven fundamentals.

Markets will continue to surprise, and no single factor can be a reliable strategy. A portfolio built on both strength and stability offers the confidence to stay invested long enough for compounding to work. ☑

Nirmay Choksi is the Director and Head of Investment at NJ Asset Management Private Limited. The views expressed above are his own.