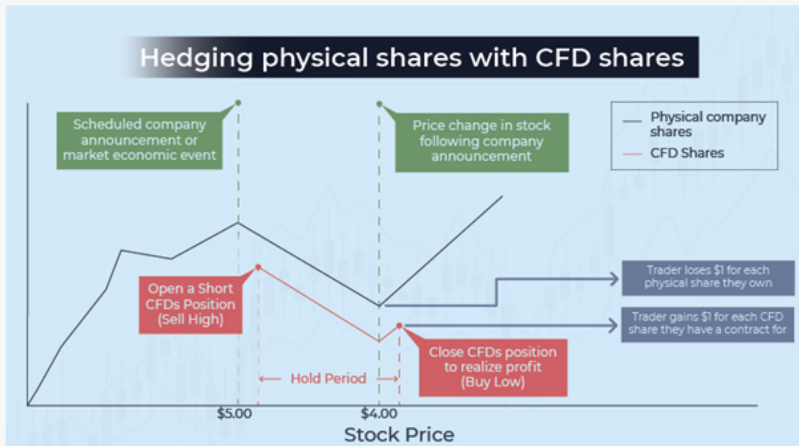
Investing Ideas – How to Protect your share portfolio by hedging with CFD Shares

Contributor article on Investorideas



Hedging Physical Shares With CFD Shares

POINT ROBERTS, WASHINGTON, UNITED STATES, July 8, 2021 /EINPresswire.com/ -- Contributor article on Investorideas: Investing in shares such as Apple (NASDAQ: AAPL), Netflix (NASDAQ: NFLX) and Microsoft (NASDAQ: MSFT) can be profitable, but it always entails a level of risk. Here is an unconventional investor idea you can use to minimise your risk of losses when trading - hedging using CFD shares.

What is Hedging With Stocks?
Hedging is a tactic to cancel out risks when stock trading by investing in shares that have negative correlation. A simple example is competing semi-conductor companies Nvidia (NVDA) and Advanced Micro Devices (AMD), if one company reports a positive result, then you will usually see the stock price of the other fall.

Airlines such as United Continental (UAL), American Airlines (AAL) and Delta (DEL) have a negative correlation with oil stocks such as BP (BP) and Royal Dutch Shell (RDSA.AS). This is because increases in crude oil hurt airlines bottom line and benefit energy producers. While using stocks with a negative correlation is a common strategy, you can never be certain price movements of your hedged stock will consistently move in opposite directions.

Short Sell Hedging
If you want a more consistent hedging strategy, you could consider short selling as a hedge. Short sell hedging works by borrowing shares of the same type you already own from a trading broker and then selling them immediately at the current market price. This allows you to buy the stock in future when the price is lower. In this way, your hedged stock moves in the opposite direction to your owned stock meaning any price losses are minimised.

Short Sell Hedging Physical Stocks With CFD Stocks
Justin Grossbard of CompareForexBrokers explains this practice can be difficult as it can be hard to find someone who will lend you the stock to use as your hedge and that there are fees to pay the person lending you stocks along with capital gain taxes making it costly. Instead, Justin suggests you hedge by using contracts for difference (CFDs) since you do not require an exchange of the underlying stock.

Let's assume you have 1000 Apple (APPL) stocks, and you are nervous Apple's upcoming company announcement could be bad. To protect yourself, you could hedge by short selling 1000 Apple CFD stocks before the upcoming announcement. This means you are opening your position with a "sell", if your prediction is correct and the company news results in a price fall, you will have negated any losses with the underlying Apple stock. This is because you can now 'buy' your CFD stocks back at the reduced price.

Using CFD stocks as your hedge to the underlying instrument is perfect because the price of the CFD stock and physical stock are matched to each other. This means you can hedge safe in the knowledge that your hedge will work regardless of market movement.

The other benefit is that you can save on costs since you will not need to pay stamp duty and your trading costs for stock CFDs are limited to the spread.

Justin says using CFDs as your hedge against your underlying instrument works best as a strategic tool to protect against upcoming events of concern. Examples of this include company announcements, interest rate changes and inflation.

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