Is the COVID-19 Stock Market Crash Already Over?

Description

The first half of April saw the TSX Index rise for two weeks in a row, gaining 5.87% by the close of trading last Friday. These gains came after a pronounced March selloff, bought on by COVID-19 and a collapse in oil prices. Investors started pulling out of equities in massive numbers after pandemic fears spiraled into business closures and mass unemployment. A Russia/Saudi oil price war happened at the same time, leading to a pronounced selloff in energy stocks. At the bottom, the TSX was down 37%.

Many investors were surprised to see stocks bounce back from the crash so quickly. COVID-19 is expected to last between a year and 18 months, while the duration of the lockdowns remains uncertain. For these reasons, some market commentators are adamant we're headed for a second massive dip. According to this thesis, stocks are only bouncing on stimulus and will resume their free-fall when earnings come out.

I wouldn't be so certain. If we look at history, it's actually quite possible that the worst of the crash is behind us. There have been events in the past similar to the ones we're going through. In many of these instances, stocks bounced back surprisingly quickly. In fact, in past crises, stocks recovered to previous high before the underlying problem even peaked. Let's take a look at one of those crises in more detail.

Signs from the Spanish Flu pandemic of 1918

The Spanish Flu pandemic of 1918 is the historical case study that most resembles what we're living through now. It was a massive flu outbreak that lasted approximately two years. Like COVID-19, the Spanish flu was far more lethal than seasonal flu. Also like COVID-19, it was accompanied by lockdowns, travel bans, and business closures.

As I wrote in a previous article, stocks crashed in the early months of the Spanish Flu outbreak. However, by October 1918 — the worst month of the outbreak — the market was back to its previous highs. This suggests that the markets priced in the effects of the pandemic early. If that's anyindication, the worst of the COVID-19 crash may indeed be behind us.

One stock that provides encouraging signs

One stock that provides encouraging signs for a recovery is **Air Canada** (TSX:AC)(TSX:AC.B). Over the past three weeks, the stock has soared 65%, despite the fact that the business is being hammered by COVID-19. There is absolutely no reason to think that Air Canada's business will turn around any time soon. If the pandemic lasts even *half* as long as projected, the company's revenue will be in the gutter until at least October.

Yet investors — including presumably well-informed institutional investors — are pushing the stock up anyway.

Why would that be the case?

Possibly, it's because the company's woes were priced in weeks ago. At the bottom, AC had fallen 77% from its pre-crash high. It wouldn't be surprising if Air Canada's earnings fell by 77% this year. However, stocks are typically valued based on their discounted earnings for the *entire* foreseeable future. Even if Air Canada is grounded for 18 full months, it's likely earnings for the next 10 or 20 years won't have fallen 77%. So, perhaps investors sensed that the stock's troubles had been more than priced in and jumped in on a "bargain" opportunity.

If we see more of that happening, then stocks might perform surprisingly well for the remainder of 2020.

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