COVID-19: A Strategy to Help You Beat the Market in This Pandemic

Description

The coronavirus (which causes the deadly disease known as COVID-19) is still out there. But so too is the U.S. Fed, which has an arsenal of tools that it could put to work should things get any uglier.

With a second wave of cases a near inevitability, it still doesn't make sense to make a rash decision with your equity holdings, because, like it or not, the stock market is going to be less about the economy over the near term and more about the tug of war between the coronavirus and the central banks around the world (the U.S. Fed in particular). Moreover, with interest rates at new lows, stocks are becoming the only game in town, if they haven't already been for the past few years.

Stay the course amid the COVID-19 pandemic!

In this kind of unpredictable market environment, where the trajectory of the broader markets is being dictated primarily by exogenous news events rather than corporate earnings, it pays dividends to stay the course and resist the urge to try to time this market.

The bears believe that central banks can't print currency to get out of a public health crisis and that in due time, the stock market will eventually reflect the damage that's been done to the economy. On the other side of the spectrum, we have the bulls that see a near-instant return to normalcy once a vaccine lands and a semi-return to normalcy if future outbreaks can be effectively contained through social-distancing practices, contact tracing, or any other method to reduce the spread. Either scenario could happen, and going all-in on the wrong one could be very harmful to one's wealth.

With no real historical event to compare this crisis to, all we as investors can do is stay invested and observe the unprecedented crisis as it unfolds. To beat the broader markets in this pandemic, one doesn't even need to know what's going to happen next or when the vaccine will land with a strategy known as the "barbell" approach, which has been growing in popularity with self-guided investors of late.

Consider a "barbell" COVID-19 approach to portfolio

construction if you seek the beat the market

The “barbell” approach involves balancing your holdings in resilient names minimally impacted by the COVID-19 pandemic, such as a regulated utility like **Fortis** and the most at-risk all-or-nothing stocks that could make or break your portfolio depending on the COVID-19 timeline (think **Air Canada** (TSX:AC)).

By balancing your portfolio in “risk-on” and “risk-off” names, it’s possible to tilt the risk/reward in your favour, regardless of what ends up happening with the COVID-19 pandemic next. Depending on your personal risk tolerance, you can allocate a greater chunk of your portfolio to either the “risk-off” or “risk-on” side of the barbell as you look to find the optimal risk/reward.

Air Canada: An example of a high-upside stock for the risk-on portion of a “barbell” portfolio

In many prior pieces, I’ve called Air Canada a stock that’s too dangerous to hold on its own, unless paired alongside a risk-off bet. While Air Canada is looking like one of the survivors of the COVID-19 onslaught, because of its favourable liquidity position and now muted cash burn rate, the ultimate trajectory of the stock depends on news relating to the COVID-19 pandemic.

As one of the most at-risk stocks on the **TSX Index**, Air Canada will struggle to pull in enough revenues to keep the lights on, as it eats into its liquidity reserves through this pandemic. Although the airline may not seem like insolvency waiting to happen right now given the economy is reopening, it very well may be should worse come to worst, and government-mandated travel restrictions are back on for some unknown duration of time.

The uncertainties with a name like Air Canada are too high. It could either be a multi-bagger or a zero. So, for those who understand the risks, the name may have a place in a balanced portfolio leveraging the “barbell” strategy.

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