Is the Stock Market Really About to Crash?

Description

Every time the stock market closes in the red, so-called pundits start touting with their market crash rhetoric. Indeed, the second wave of the pandemic and a new round of lockdowns hint at fresh weakness. But there are a whole lot of other factors to consider as well.

Concerning VIX

The **TSX Index** and the **S&P 500 Composite Index** have fallen more than 5% in the last couple of weeks. The volatility indexes (or the VIX) of almost all major global equity indices peaked recently, indicating immense anxiety among investors. Despite the recent market weakness, fair quarterly corporate earnings growth and not-so-concerning stock valuations suggest that there won't be a crash in the short term.

Certainly, the VIX might bother some market participants. But U.S. presidential elections are just a few days away. Global equities generally turn this rough during the U.S. elections. Investors should note that the same will likely drive large swings in equities until early 2021.

So, is it time for investors to be cautious and stay out of the market? Is it too risky to throw in fresh money in stocks right now?

Canada corporate earnings growth

More than any other economic indicator, stocks are largely driven by earnings. We have already seen a terrible crash in March on the weaker corporate earnings growth driven by the virus outbreak.

However, third-quarter earnings indicate a slow-but-stable recovery, despite the prolonged pandemic. The south of the border heavyweights **Apple** and **Amazon** have reported record numbers for the quarter ended September 30, 2020. Stocks are turning lower amid the market chaos, and they should soon recover as the volatility subsides.

Here in Canada, **Shopify** (TSX:SHOP)(NYSE:SHOP), the TSX Composite's biggest constituent, has yet-again reported better-than-expected results for the third quarter. Its revenues once-again almost doubled and it posted record profits.

Being some of the pandemic's biggest beneficiaries, Shopify stock is already up 150% so far this year. Notably, its recent quarterly earnings highlight that the stock has yet to peak. Despite the valuation concerns, Shopify stock might continue to soar higher as the tech giant has well-exceeded market expectations on several operating fronts in Q3.

Why stock market crash seems unlikely

Financials account for more than 25% of weighting on the S&P/TSX Composite. There is a high possibility that Canadian bank stocks will continue to feel the heat amid the prolonged pandemic. However, almost all Big Six banks are well-capitalized and practice prudent provisioning.

Royal Bank of Canada (TSX:RY)(NYSE:RY), the country's biggest bank by customers and market capitalization, has set aside $3.5 billion for bad loans in the last six months. With reasonable provisioning, Royal Bank will have a relatively lower impact on its earnings for the next few quarters.

Additionally, Canadian banks like RY offer stable and reliable dividends. Amid broad market uncertainty and a low-interest-rate environment, income-seeking investors might turn to banks from bonds, ultimately boosting stocks. Notably, the dividend yield spread on Canadian stocks and bonds is currently the highest in decades. Royal Bank of Canada yields 5% at the moment, higher than TSX stocks on average.

TSX stocks at large are currently trading 23 times of their forward earnings, which is not exorbitantly high. Similar is the case with the U.S. indices. Thus, markets will likely continue to trade rough with underlying uncertainties. However, the crash seems unlikely due to reasonable valuations and decent corporate earnings growth.

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Date
2025/08/24
Date Created
2020/10/30
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