

To the Point – Early signs of capital market recovery

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The history of stock market crashes in the US

Between the start of the 20th Century and the end of World War 2, the US experienced five major stock market crashes, with the one that triggered the Great Depression in 1929 by far the worst. From the peak of the benchmark Dow Jones Industrial Average (an index of equity market capitalisation), the decline was 89% and it only started to recover three years later.

Prior to the Second World War, however, financial markets were not yet well developed or well regulated. Furthermore, currencies were still subject to the gold standard (until 1944), after which the Bretton Woods system was adopted. The latter appointed the US dollar as the international reserve currency, but exchange rates were still fixed. It was only in 1976 that IMF members adopted the Jamaica Agreement, whereby countries could choose between floating or fixed exchange rate systems. Most countries have since opted for floating rates, with the demand for and supply of foreign exchange determining the value of a country's currency.

Since a larger degree of sophistication was acquired by the global financial system, there have been ten major stock market crashes in the US, most of which have exerted a spill-over effect on other equity markets, including the JSE.

Worst US stock market crashes post World War 2 (Dow Jones Industrial Average)

Stock market crash	Peak-to-trough Decline %	Duration Months	% GDP decline
Global financial crisis (2007)	-54	17	-5
1973 oil crisis	-45	17	-3
Covid-19 pandemic (2020)	-37	1.5 ?	?
Dot-com bubble of 2002	-31	5	None
Recession of 1961	-27	6	-2
Black Monday of 1987	-23	1	None
Flash crash of 1970	-19	1	None
Russian debt default (1998)	-19	1	None
Iraq's invasion of Kuwait (1990)	-18	2	-1
Shanghai equity crash (2015)	-14	2	None

Sources: Statista; Forbes; Financial Times

Note: Ranked by % decline in equity market capitalisation

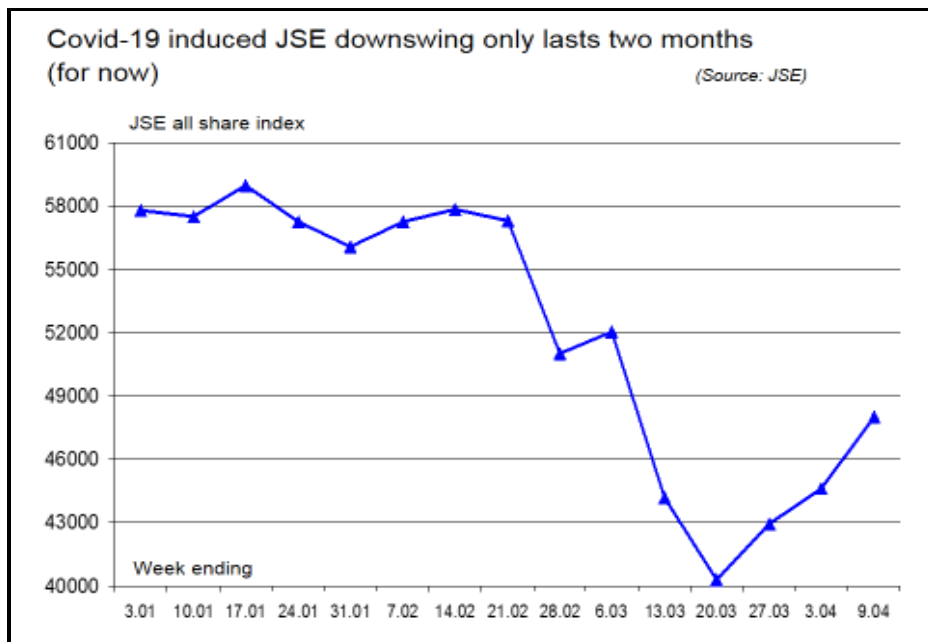
It is clear from the data in the table that most stock market crashes have been fast and furious, with the majority of them lasting two months or less. There is no need, therefore, to panic when equities start declining at double-digit rates – they always recover.

Another observation from an analysis of stock market crashes over the past 60 years is the fact that they do not always trigger a recession. Even during the global financial crisis of 2007 to 2009, several emerging markets and developing countries did not join the recession that was experienced in the US and Europe.

The latest of the fairly regular occurrence of sharp and sudden declines in equity prices was a direct result of the global Covid-19 pandemic. Although it is not certain whether the equity market downswing has run its full course, markets started to recover within the space of six to eight weeks.

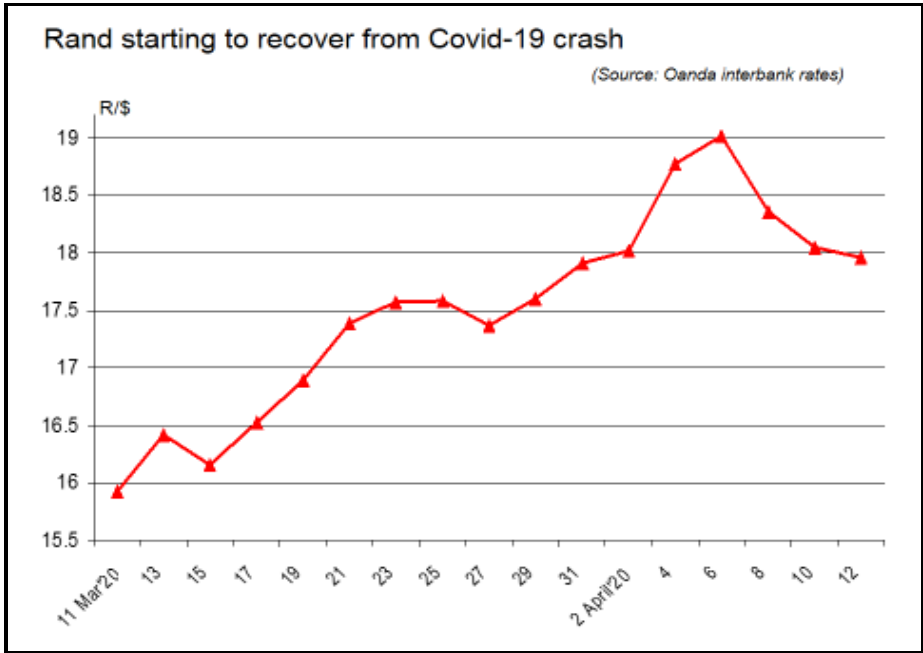
In South Africa's case, the JSE all share index (Alsi) lost 36% of its value between 17 January and 19 March, prompted by panic selling as investors switched mainly to cash (despite clear indications that short-term interest rates have started a declining trend). This decline was virtually identical to that of the benchmark Dow Jones index in the US.

Between 19 March and 9 April the JSA Alsi bounced back by more than 26%, resulting in significant short-term capital gains for investors that had grasped the opportunity to buy at or close to the date of the trough. A degree of volatility may still lie ahead, however, depending on the duration of economic lockdowns that have been implemented in virtually every country.



Rand turns the corner

The rand has also started to recover from its lowest level in history, more or less in tandem with the recovery of the JSE Alsi. Between 11 March and 6 April, the rand lost more than 16% of its value against the US dollar, but has regained 6% of its value since then (until 13 April). Two obvious reasons for the recovery of the rand are, firstly, a healthy trade balance, which has been in surplus territory for several years and, secondly, the highly attractive bond yields on offer in South Africa.



Conditions for an easing of the lockdown

The South African government has made it quite clear that the economic lockdown will not be lifted until such time as specific metrics are met regarding the occurrence of positive Covid-19 cases. The number of new positive cases needs to fall to below the average daily level of between 45 and 89 before an easing of the regulations will be considered.

Due to the quick and impressive response to the pandemic by South Africa, a gradual easing of the lockdown may start occurring before the end of April, but these will be implemented with the utmost caution and will be conditional on the maintenance of strict hygienic standards, including the screening and monitoring of all employees.

Compared to 44 countries with populations of more than 10 million people and positive Covid-19 cases of above 2,000, South Africa currently has one of the three lowest fatality rates (marginally above 1%).

It should be possible to allow certain sectors of the economy to start working again without compromising the health of employees. This could be done, *inter alia*, by limiting the number of people in work spaces; shift work; flexible time schedules; appropriate protective clothing and safe transport.

Sole proprietaries, certain business and IT services and capital intensive export industries, in particular, could be first in the queue for a return to some kind of normality.