

Warren Buffett's Market Indicator Remains Near All-Time High

The 'Oracle of Omaha's' top holding sets new intraday high close to \$209

August 06, 2018 | About: [AAPL +0%](#) [BRK.A +0%](#) [BRK.B +0%](#) [MKL +0%](#)

On Monday, [Warren Buffett \(Trades, Portfolio\)](#)'s favorite market indicator reached 144.4%, approximately 4.1% from its all-time high. Apple Inc. ([NASDAQ:AAPL](#)), Buffett's top holding, set a new intraday high in morning trading.



Buffett's market indicator remains above 140%

The Berkshire Hathaway Inc. ([NYSE:BRK.A](#))([NYSE:BRK.B](#)) CEO mentioned that the ratio of the [Wilshire 5000 full-cap index](#) to the U.S. [gross domestic product](#) is “probably the best single measure of where market valuations stand at any given moment.” As of 11 a.m., the total market index is approximately 1.444 times greater than the U.S. GDP. Based on this market valuation level, the U.S. market is expected to return -2.2% per year over the next eight years.

Figure 1 shows the historical trends of the index and GDP, while Figure 2 shows the historical trend of the Buffett indicator.

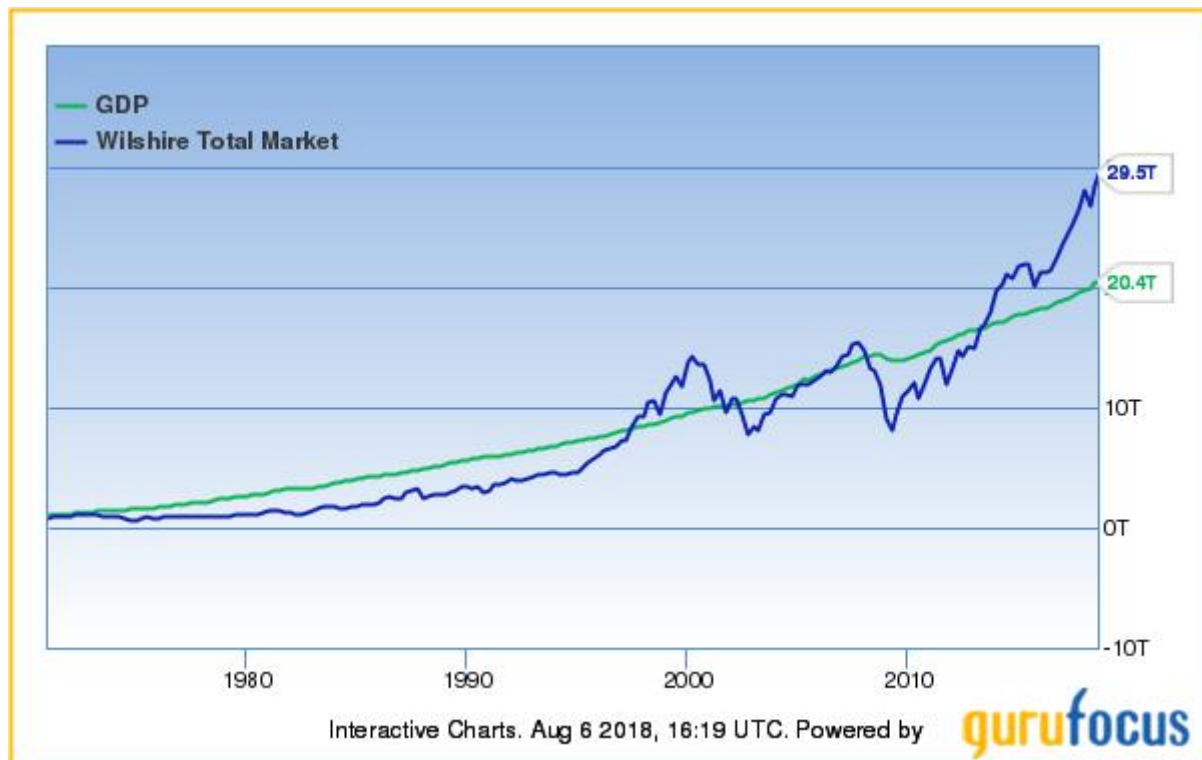


Figure 1

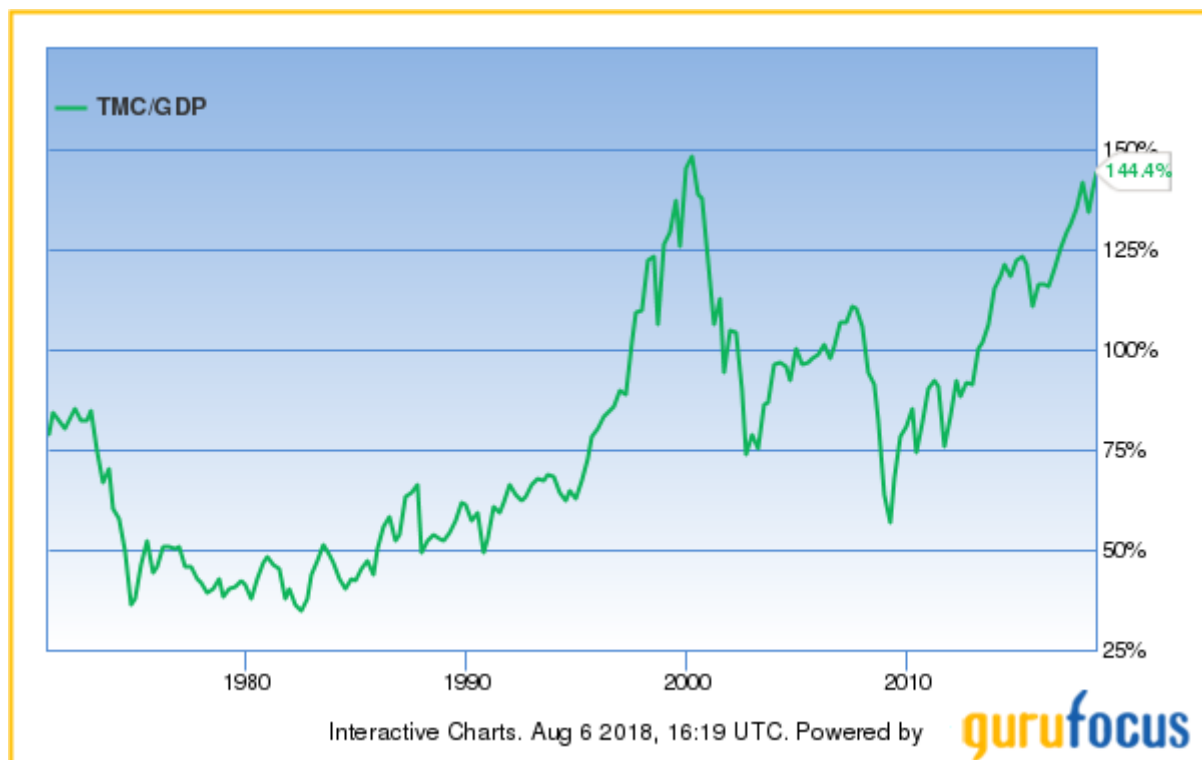


Figure 2

The predicted market return includes three components: the dividend yield, the business growth rate and the change in the market return. We compute the change in the market return as the ratio of the ending market ratio to the current market ratio raised to the one-eighth power less one: $(R_e/R_b)^{1/8}-1$. We set the period to eight years, approximately the length of a full economic cycle.

Figure 3 illustrates three cases for the ending market ratio: an optimistic case of 120%, an expected case of 80% and a pessimistic case of 40%. According to Figure 3, the expected market return ranges from -9.9% to 2.6%.

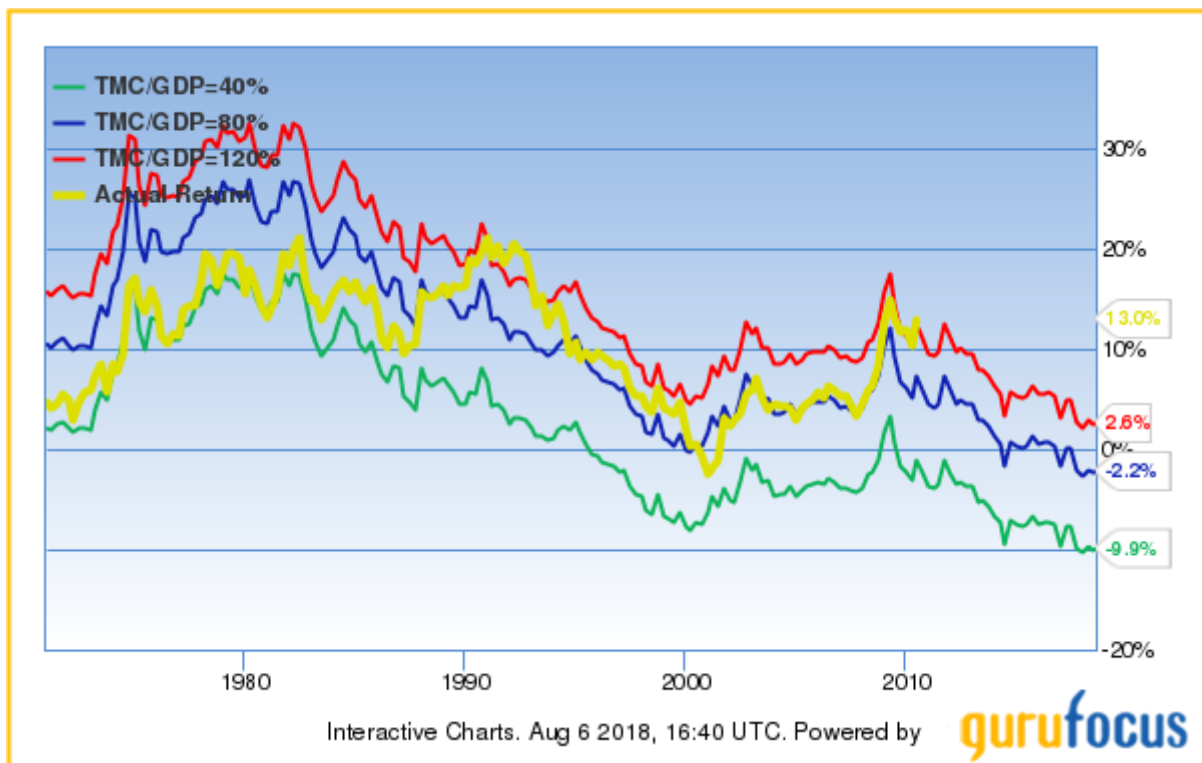


Figure 3

Other market valuation metrics, including the [Shiller price-earnings ratio](#) and the [Tobin Q ratio](#) suggest that the U.S. market is significantly overvalued. As of noon, Robert Shiller's cyclically adjusted price-earnings ratio stands at 32.6, approximately 93% higher than the historical mean of 16.9 as Figure 5 illustrates.

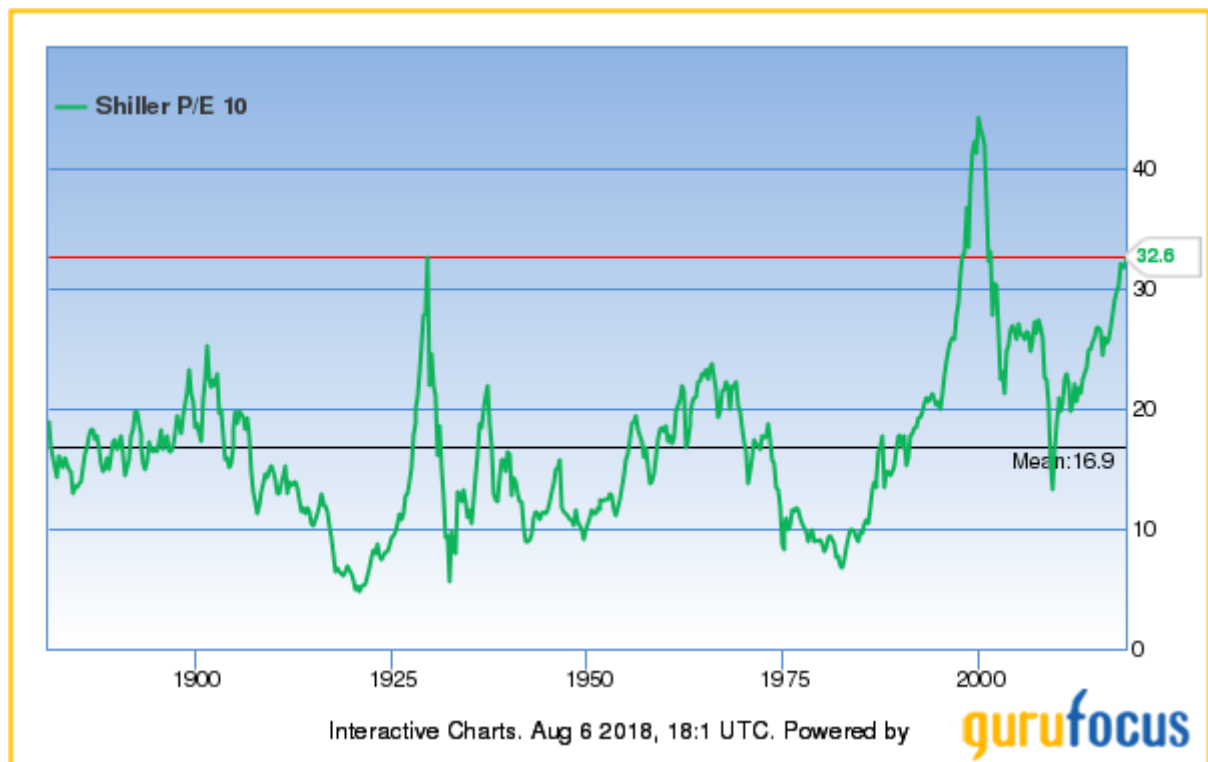


Figure 5

According to the economic indicator pages, Tobin's Q-ratio measures the ratio of the market value of a company to the company's assets. According to Figure 6, the Q-ratio for the U.S. market as of first-quarter 2018 is 1.1, implying moderate overvaluation.