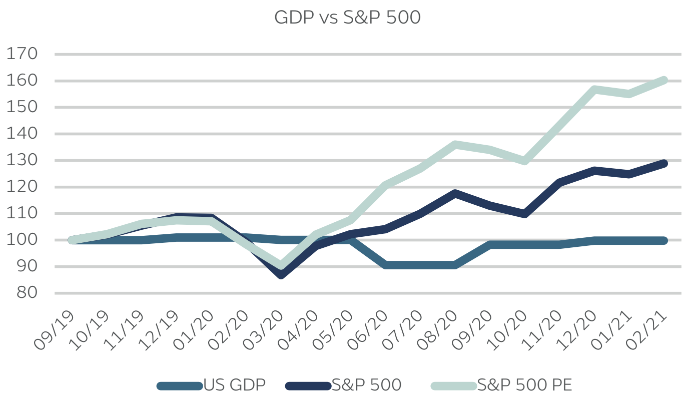
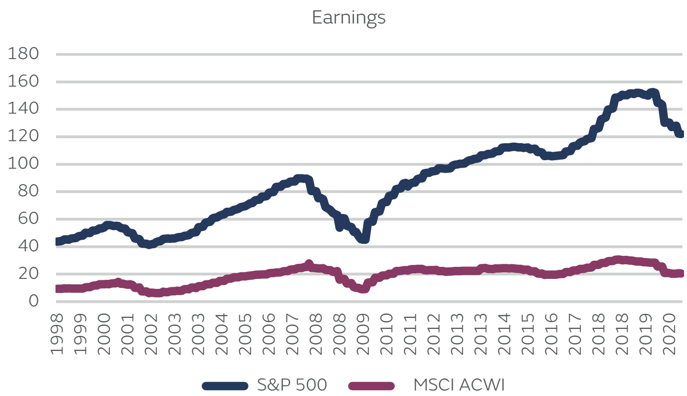
Blowing bubbles

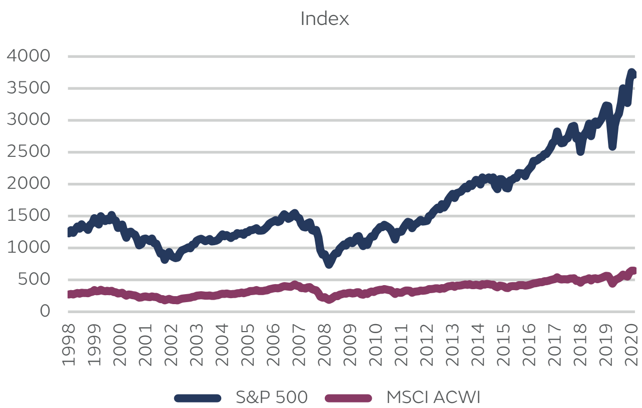
During 2020 financial markets once again disconnected from underlying economic activity, leading increasingly to the question of asset price bubbles and when they might pop.

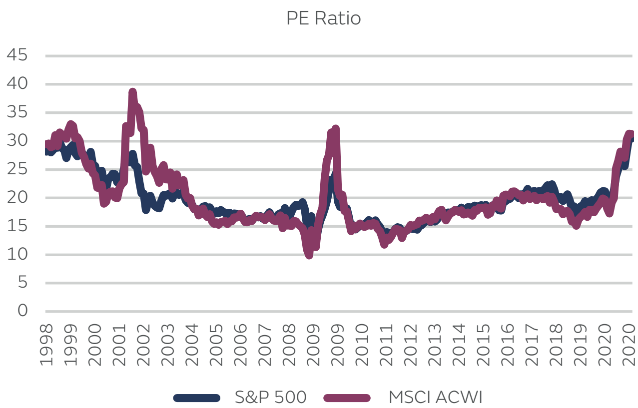
> "Giant bubbles are once again inflating all over the financial world..." Politico, March 1, 2021

Certainly, forward-looking index measures marched ahead of trailing GDP performance and simple arithmetic shows that as US and world earnings fell, PE ratios rose.







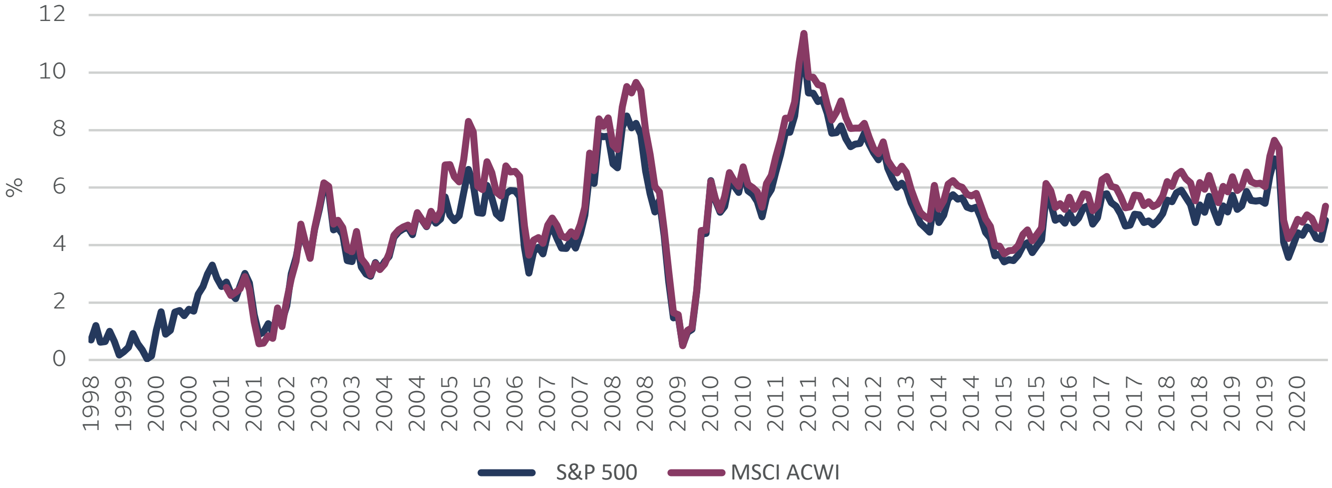


Sure, the 2 prior P/E ratio spikes were followed by steep market corrections (the dot.com bubble and the global financial crisis). But not all spikes and not all bubbles are created equal. While a Shaq SPAC[1] and a Dogecoin[2] meme garner headlines, broader market performance isn't in the same bubble as in previous market corrections.

[1]https://finance.yahoo.com/news/shaq-spac-2-0-coming-133637566.html
[2]https://www.cnet.com/news/dogecoin-how-a-meme-somehow-became-a-real-cryptocurrency/

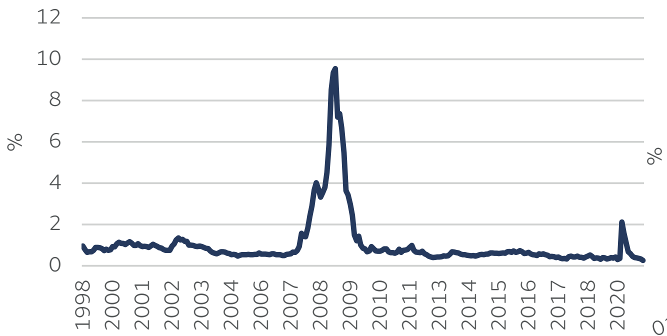
Chart sources: Bloomberg & GIB Analysis, March 2021

S&P 500/MSCI ACWI Earnings Yield spread over real 10Y Treasury

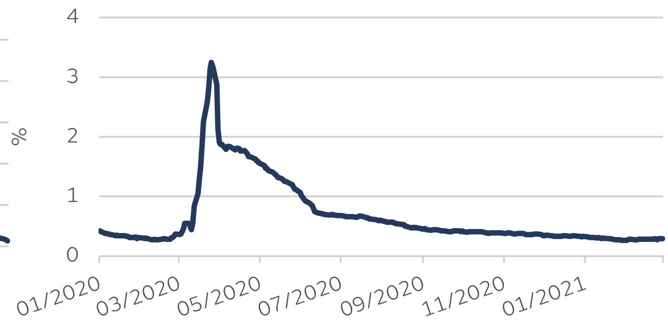


The earnings yield over real risk-free rates is simply nowhere near previous bubble pops, suggesting that risk premia are alive and well. The same is true of the credit markets with ABS prices, while tight, back in line with historic ranges.

Aggregate ABS spread

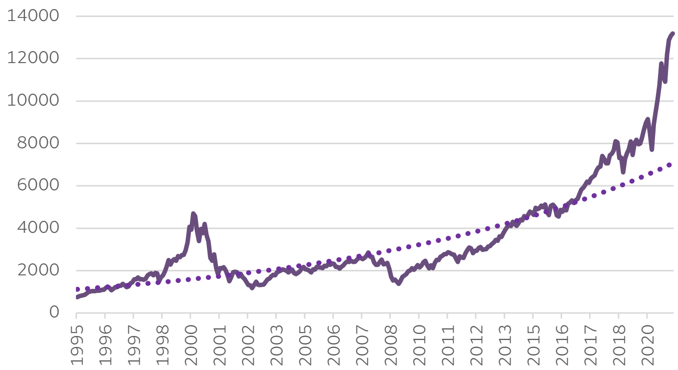


Aggregate ABS spread

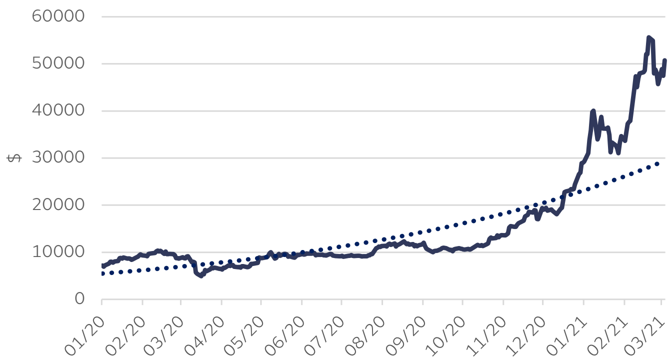


From the GI Joe with the king-fu grip[3] to synthetic CDOs expensive bubbles are always around. But higher prices aren't always bubbles. While NASDAQ and Bitcoin trend lines might look similar, one is clearly moving into uncharted territory relative to the other.

NASDAQ Composite Index



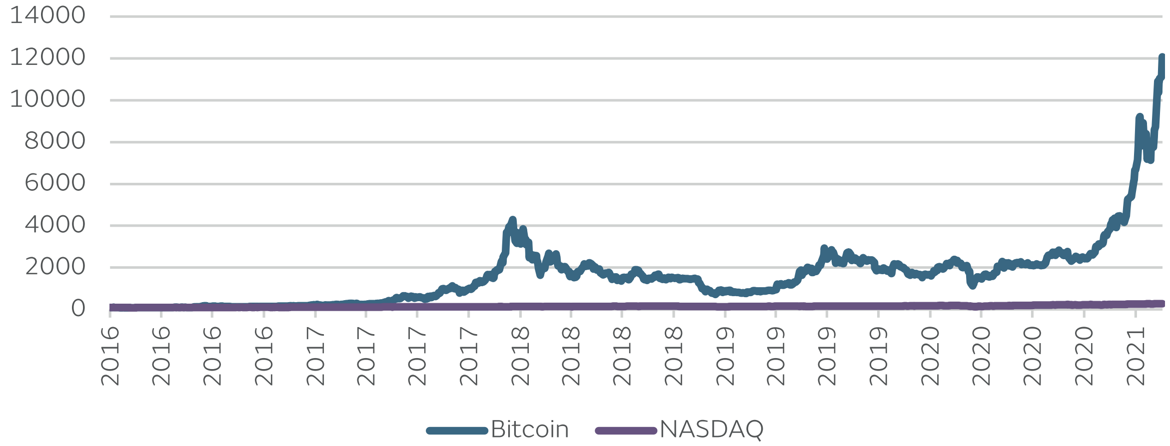
Bitcoin price



[3]See Trading Places, the ultimate bubble movie

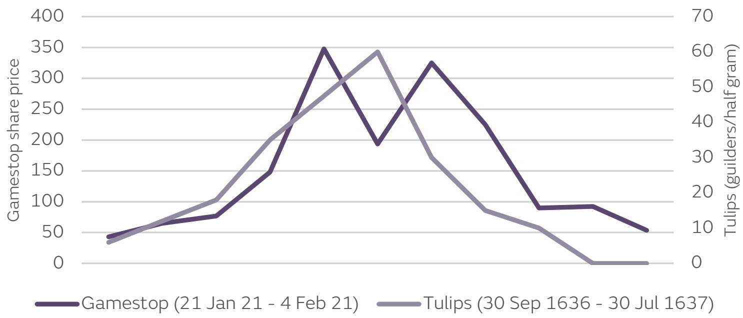
Chart sources: Bloomberg & GIB Analysis, March 2021

Bitcoin vs NASDAQ
Index 100 = Jan 2016



Bitcoin as a bubble has been compared to the tulip bubble of 1636-7. But that's unfair to tulips. The tulip bubble of 1636 -7 wasn't a bubble, it was a technical correction as physical spot deliveries couldn't keep pace with futures prices. Tulip mania is much more analogous with a short squeeze, such as Gamestop.[4]

Gamestop and Tulips



Across asset classes our view is to focus on long term investment objectives and strategies to get you there. Buying dips and selling peaks is easy with hindsight and bubble headlines are a distraction, not a market factor driving medium term market returns. Market outperformance is hard, requiring investment views underpinned by fundamental change factors, not a fad that's here today and (pop!) gone tomorrow.

[4]Different timeframes consistent with faster information technology in 2021 than in 1637.
Chart sources: Bloomberg & GIB Analysis, March 2021