

# IS THIS 1929 OR 1998?



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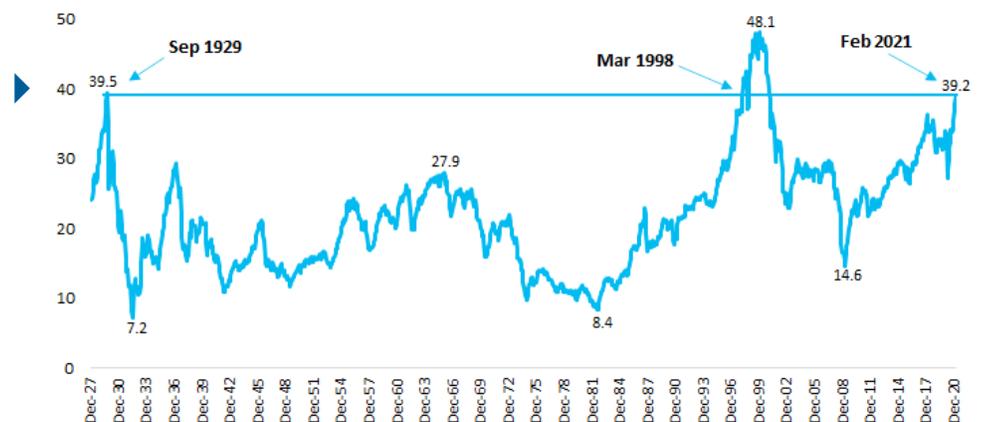
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The CAPE Ratio just crossed above 39.<sup>1</sup> In layman's terms, what exactly does that mean? Equity valuations in the U.S. are quite high. How high?

Going back to 1871, the only periods in history with a CAPE above 39 are as follows...

- ▶ September 1929
- ▶ March 1998 to January 2001
- ▶ Today

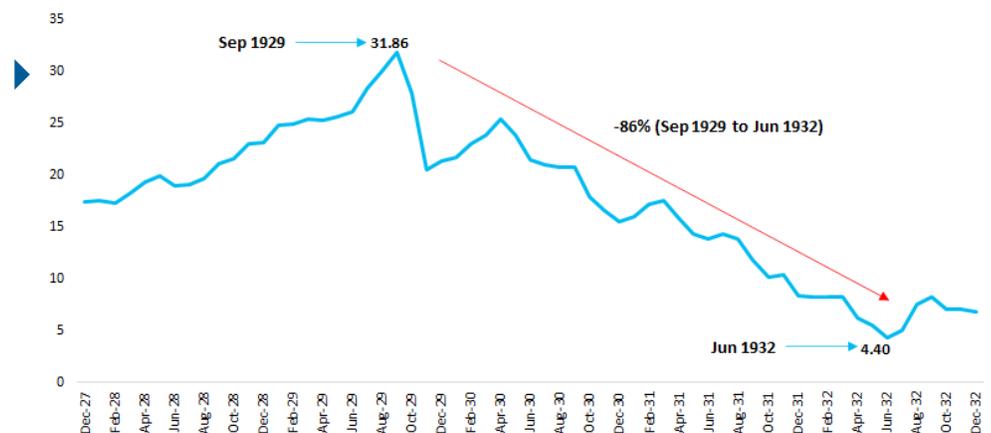
**S&P 500® INDEX TOTAL RETURN CAPE RATIO: 1928–2021**



Past performance is not indicative of future results. Data Source: Robert Shiller.

In September 1929, the CAPE ratio moved above 39 for the first time in history. That same month, the S&P 500® Index would hit a generational high. From there, it would fall over 86% before bottoming in June 1932.

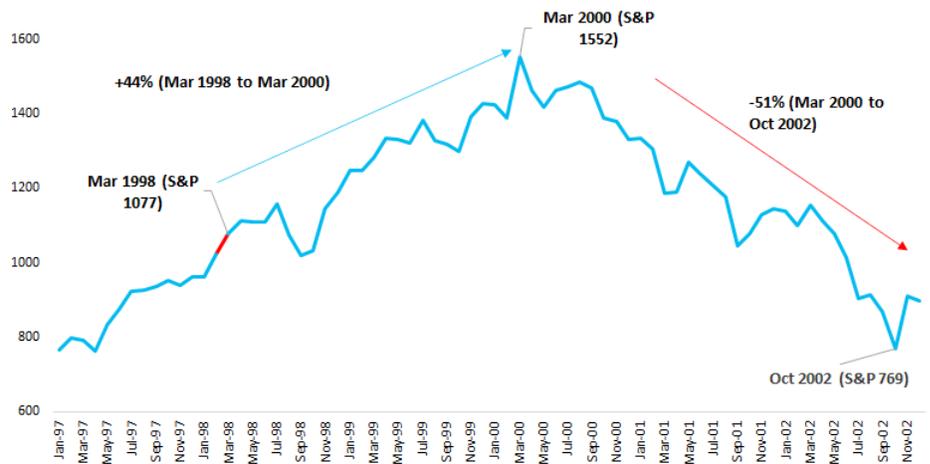
**S&P 500® INDEX TOTAL RETURN CAPE RATIO: 1927-1932**



Past performance is not indicative of future results. Data Source: Robert Shiller.

In March 1998, the CAPE ratio moved above 39 for the second time in history. From there, the S&P 500 would gain another 44% before peaking in March 2000. From the peak in March 2000 to the low in October 2002, the S&P 500 would give back all of those gains and more, declining more than 50%.

S&P 500® INDEX TOTAL RETURN CAPE RATIO: 1997–2002



Past performance is not indicative of future results. Data Source: Robert Shiller.

**So is this 1929 or 1998? Neither. This is 2021.**

No one knows what will happen from here because every time is different. Valuations may be the same as these years, but the path ahead most certainly won't be. Stocks could fall starting tomorrow (1929 example) or they could run for a few more years (1998 example), going from overvalued to more overvalued. Or they could trade in a sideways range for years to come, frustrating bulls and bears alike.

Literally anything can happen in the **short run** that is determined by sentiment (fear and greed) more than anything else. We shouldn't be surprised by any of it.

That said, with the CAPE ratio above 39 (98th percentile), what should investors be prepared for in the **longer run**?

1) Below average forward returns...

		S&P 500 Average Forward Total Return (1928 - 2021)									
Valuation Percentile	CAPE TR Ratio	1-Yr	2-Yr	3-Yr	4-Year	5-Year	6-Year	7-Year	8-Year	9-Year	10-Year
90-100%	Above 31.5	4.4%	0.9%	-2.2%	-3.8%	-2.2%	-0.5%	1.1%	1.1%	0.6%	0.8%
0-90%	Below 31.5	12.1%	11.1%	11.0%	11.0%	11.0%	11.0%	11.0%	11.1%	11.1%	11.1%
Differential		-7.8%	-10.3%	-13.2%	-14.8%	-13.2%	-11.5%	-9.9%	-9.9%	-10.5%	-10.3%

2) Above average forward volatility...

		S&P 500 Average Forward Annualized Volatility (1928 - 2021)									
Valuation Percentile	CAPE TR Ratio	1-Yr	2-Yr	3-Yr	4-Year	5-Year	6-Year	7-Year	8-Year	9-Year	10-Year
90-100%	Above 31.5	16.8%	16.5%	17.2%	18.6%	18.0%	17.1%	16.5%	16.3%	16.5%	16.6%
0-90%	Below 31.5	12.6%	13.3%	13.5%	13.5%	13.6%	13.5%	13.5%	13.4%	13.3%	13.3%
Differential		4.2%	3.2%	3.7%	5.0%	4.4%	3.5%	3.0%	2.9%	3.1%	3.4%

3) Above average forward maximum loss<sup>2</sup>...

		S&P 500 Average Forward Maximum Loss (1928 - 2021)									
Valuation Percentile	CAPE TR Ratio	1-Yr	2-Yr	3-Yr	4-Year	5-Year	6-Year	7-Year	8-Year	9-Year	10-Year
90-100%	Above 31.5	-9.8%	-17.0%	-25.5%	-33.4%	-34.9%	-35.0%	-35.0%	-35.0%	-35.0%	-35.0%
0-90%	Below 31.5	-5.9%	-8.6%	-10.2%	-11.4%	-12.0%	-12.2%	-12.4%	-12.5%	-12.7%	-12.8%
Differential		-3.8%	-8.4%	-15.4%	-22.0%	-22.9%	-22.8%	-22.7%	-22.5%	-22.3%	-22.3%

Past performance is not indicative of future results. Source: Compound.

These are just averages and probabilities based on what has happened in the past at similar valuation junctures. There are always exceptions to the rule, and, as we saw from 1998, trying to time the market based on valuation is a fool's game. There is nothing stopping investors today from bidding up stocks to even higher multiples.

But, an objective observer will note that the risk/reward in U.S. equities is less favorable today than it has been in quite some time. That says nothing about what will happen tomorrow, but if the price one pays for something still matters, it will be a factor weighing on returns for years to come.

After the CAPE ratio hit 39 in 1929, the S&P 500 would trade at the same level 25 years later—in 1954.

After the CAPE ratio hit 39 in 1998, the S&P 500 would trade at the same level 12 years later—in 2010.

This is not 1929 or 1998, but investors are faced with a similar question: with the CAPE ratio above 39 once more, how many years into the future will the S&P 500's current level of 3900 be revisited?



To learn more, please contact us at 800-243-4361 or visit [virtus.com](https://www.virtus.com).

<sup>1</sup>In this post, the CAPE Ratio is the Cyclically Adjusted Total Return Price to Earnings Ratio (TR P/E10 or TR CAPE). It is also known as the "Shiller P/E", as it was developed by economist Robert Shiller. Data source: Robert Shiller.

<sup>2</sup>Maximum loss is calculated by taking the lowest monthly future closing value over x number years (1-10) and comparing that to the starting value.

The **S&P 500® Index** is a free-float market capitalization-weighted index of 500 of the largest U.S. companies. The index is calculated on a total return basis with dividends reinvested. The index is unmanaged, its returns do not reflect any fees, expenses, or sales charges, and it is not available for direct investment.

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