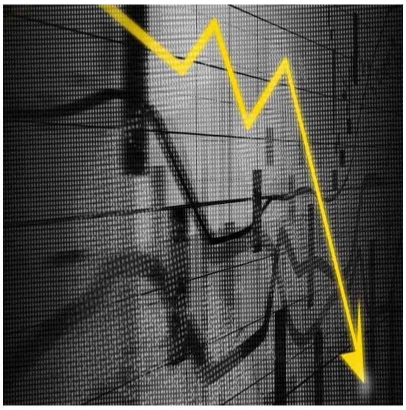

WARNING: Warren Buffett’s Favourite Stock Market Indicator Signals More Pain to Come!

Description

Recently, Warren Buffett’s business partner Charlie Munger made headlines by saying that Buffett hadn’t been buying the dip in the March stock market crash.

These comments were surprising, because usually Buffett is one of the first to buy on bad news. The worse the news gets, the lower stocks typically go, creating the kinds of bargains that value investors go for. Historically, these types of situations have inspired Buffett to buy.

Not this time, according to Munger. He and Buffett are focused on liquidity: “We’re not playing, ‘oh goody, goody, everything’s going to hell, let’s plunge 100% of the reserves into businesses.'” Instead, he said, they were focusing on weathering the storm with “a whole lot of liquidity.”

It might seem like a drastic change of pace for Buffett and Munger. Yet when we look at one of Buffett’s favourite economic indicators, it shines light on their recent moves. According to this indicator, stocks are *still* overvalued in April. And they could get even more expensive after GDP contracts.

Stock market valuation to GDP

Stock market valuation to GDP — sometimes called the Buffett Indicator — describes how expensive publicly traded stocks are compared to GDP. When the percentage is too high, stocks may be overvalued. At the start of the global financial crisis, the indicator sat at 110%. By the trough, it was at 56%.

As of April 17, the Buffett indicator sat at 137% for the United States. In Canada, it was closer to 100%, which is significantly lower but still fairly high for a country with a more sluggish stock market. Over the years, U.S. stocks have far outpaced Canadian stocks, so it would make sense that the U.S. would have a higher ratio.

In any case, the high ratio could explain why Buffett hasn’t bought American stocks. An interesting question, then, is whether he may be more interested in Canadian stocks as they're comparatively cheaper.

Could Buffett buy Canadian stocks?

It is possible that comparatively cheap Canadian stocks could get Buffett interested. With that said, there are no signs that he's been buying.

One Canadian stock that Buffett owns is **Suncor Energy**. As an energy stock, it's been badly beaten down in the COVID-19 stock market crash. As such, it has gotten cheap. At current prices, Suncor trades at 11.7 times trailing earnings. The trailing P/E ratio here is a little misleading, because this year's earnings won't be as high as last year's. Nevertheless, it's a stock that's looking cheap by a traditional valuation metric.

That aside, I don't see Buffett buying more SU any time soon. The stock has been a loser for Buffett since he bought it last year, and there's no sight of an oil recovery any time soon. If oil prices stay low, I could easily see Buffett exiting the stock at a loss. Just recently, Buffett ditched $300 million worth of **Delta Airlines** shares, after buying $45 million worth on the dip. These moves are consistent with Buffett making liquidity a priority, just like Munger said he was.

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