Beware: This Warren Buffett Indicator Suggests Winter Is Coming!

Description

For *Game of Thrones* enthusiasts, the phrase “Winter is coming” holds special meaning. As winters were severe in the fantasy land of Winterfell and extended several years, it was understandably a dreaded time for people and can be likened to the current global economic situation.

The ongoing COVID-19 pandemic (aka, the White Walker) has decimated several sectors spanning retail, airline, hospitality, restaurants, travel, and tourism. While Canada has managed to successfully flatten the curve, there is a chance for a second COVID-19 wave to wreak havoc this fall.

Further, the country’s unemployment rate has spiked and consumer spending has taken a hit. Several entertainment avenues, including malls, remain closed, and people are still wary of traveling. Amid the chaos, the broader markets have recovered to trade at pre-pandemic levels.

In fact, the S&P 500 Index touched a record high last week, despite a sluggish economy. The Warren Buffett Indicator in the U.S., which is one of the easiest ways to check if the stock market is overvalued or not, is at a multi-year high of 179%.

The Warren Buffett Indicator, also known as the market cap-to-GDP ratio, suggests that the equity markets south of the border are significantly overvalued. A ratio of about 100% will mean the markets are reasonably valued, while a ratio below 90% will mean the markets are underpriced.

The S&P 500 fell 36% in less than a month in early 2020. While the decline was unprecedented, its V-shaped recovery has equally surprised investors. The economic uncertainties loom large, and the recent upward spiral is largely driven by investor optimism.

So, does this mean that markets will come crashing down in the next few months? While it is impossible to time a market crash, the recent rally is not sustainable.

Does Warren Buffett expect another market crash?

Warren Buffett-owned **Berkshire Hathaway** ended Q2 with $146.6 billion in cash, up from $128 billion at the end of 2019. Warren Buffett has, in fact, been a net seller of equities this year and surprised followers when he did not go bargain hunting amid the pandemic-led market crash. It is quite possible that the Oracle of Omaha expects another correction in the near future given the frothy valuations.

However, Berkshire Hathaway added one Canadian stock to its portfolio in Q2. According to its 13F SEC filings, Berkshire bought 20.9 million shares of **Barrick Gold** (TSX:ABX)(NYSE:GOLD) worth US$613 million. This indicates a 1.2% stake in the gold mining company.

This was an investment that raised eyebrows given Buffett's aversion to gold as the asset does not pay dividends, and its value is derived on the assumption that someone will pay a higher price for it in the future. However, Warren Buffett is not solely responsible for Berkshire's investments. Barrick Gold is a gold mining company with a healthy business.

Barrick Gold stock is up 60% year to date and has returned 309% in the last five years. The stock gained over 10% after Berkshire's 13F filings. Gold prices are hovering around the US$2,000 per ounce mark and might breach $2,500 by end of 2020, driven by low interest rates and a weakening dollar.

If you are bullish on gold prices, miners such as Barrick Gold will be able to expand profit margins at a healthy rate in the upcoming quarters. Barrick also aims to be net debt zero by the end of the year and is a top stock to hold looking at macro-economic challenges.

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