Stock Market Crash: Could a 2000-Style Drop Be in the Cards?

Description

Stop me if you've heard this one before: the stock market is expensive going into 2021. Potentially so expensive such that prospective returns moving forward are low and the risk of a 2000-style tech-lead stock market crash is high. While the **TSX Index** and **S&P 500** may be "expensive" based on traditional valuation metrics, with tech leading the way in the latter index, I'd say it's quite the stretch to say that we're due for a repeat of the events that unfolded after the tech frenzy of the late 1990s.

Tech stocks haven't been this hot in quite a while

Are stocks really partying like it's the late 1990s? With the exception of Bitcoin, a handful of overbought recent Initial Public Offerings (IPOs), EV makers that I shall not name, and a few other isolated pockets of severe overvaluation, I'd say no, it's not partying like the late 1990s — not even close.

Back when the dot-com bubble inflated, tech may have led the upward charge, but valuations across the board were so stretched beyond belief. The NASDAQ went parabolic for a while, surging more than 100% from trough-to-peak in around a year.

While the NASDAQ is up almost double from those ominous March depths, it's up just a modest 30% from pre-pandemic highs, and it's up mainly because of a few dominant tech behemoths, which are profoundly profitable, have been beneficiaries of this horrific pandemic.

A 2000-style market crash is unlikely, but what about those bubbles?

Unlike in 1999, when many euphoric investors were betting on stories (like with those white-hot shares of **Shopify**), today's dominant tech leaders are generating so much cash that it's ridiculous. Their valuations are backed by earnings, and heck, the FAANG stocks may actually still be undervalued here, given their dominance increased substantially in 2020.

I can't say the same about white-hot software-as-a-service (SaaS) stocks (think Shopify), many of which have been bid-up by investors exhibiting the fear of missing out mentality. Sure, stocks may not be as expensive as they seem, given the pandemic-plagued environment and the U.S. Fed's backing. But that doesn't grant a free pass to pay whatever price Mr. Market is asking for at any given instance.

While a name like Shopify deserves a premium valuation, just how much of a premium remains the million-dollar question. Shopify stock will probably never trade at a multiple that's anything short of absurdly expensive.

That said, one has to draw the side somewhere. If you're in the belief that paying for many years' worth of (potentially unsustainable) growth right off the bat is a risky proposition, then it may be time to take profits in 2020 winners such as Shopify before the appetite for speculation has a chance to nosedive.

The 56 times sales multiple on shares of Shopify is excessive, to say the least. For those who've already doubled or tripled their money on the name, it's only prudent to think about playing with the house's money now that the stakes have been raised that much higher in this new year.

Should investors expect a tech-led market crash?

Margin debt is uncomfortably high, Bitcoin and other such speculative momentum plays are not looking back, IPOs are way oversubscribed and overbought, and the "new normal" may also be describing lofty valuations in some tech plays out there.

That said, I have no idea if or when Mr. Market will correct any isolated pockets of overvaluation. But when he does, the "sexiest" plays could be at risk of crumbling like a paper bag, doling out amplified losses to those who went all-in on the "hottest" investment themes of this past year.

Stay cautious, my friends.

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