Better Buy: Tech or ESG?

Description

Is it just me, or are bubbles popping up everywhere?

One of my pieces a while back discussing whether the Canadian Cannabis sector or the cryptocurrency fad was a bigger bubble got a lot of attention. Right now, I think we may be seeing a few more bubbles surfacing. In this article, I'm going to discuss why I think we could be seeing bubbles forming in the technology and ESG sectors today.

Tech valuations approaching absurd levels

Similar to my previous discussion around the valuations of Canadian cannabis companies being absurd, certain technology stocks are approaching these levels now. Various Canadian cannabis players hit valuations above 100 times sales at their peaks. These levels are simply mindboggling to most fundamental investors.

Simple ratios and elementary valuation multiple analysis should have put forward enough red flags to keep investors away. That said, hype is dangerous. Momentum investing can feel like gambling, making such investments thrilling for adrenaline junkie investors.

In my view, **Shopify Inc.**'s (TSX:SHOP)(NYSE:SHOP) valuation of more than 50-time sales in July approaches a similar obscene level. Like its cannabis peers, Shopify does not yet have a track record of four quarters of consecutive profitability. The company is still in its early stages of growth. When fundamental analysis gets thrown out the window in favor of a storybook style momentum trade, danger almost always looms around the corner.

The valuations of a number of U.S. technology players also make absolutely zero fundamental sense right now. These are just as dangerous to long term investors. Hope stocks like **Tesla Inc**. with cultlike followings are examples. Any stock that has more than doubled since the beginning of the year (following a global pandemic outbreak) ought to be checked. Right now they're not.

ESG noble, but safe?

The move toward environmental, social, and governance (ESG) oriented investing reminds me in some ways of the bullish story around cryptocurrency in years past. The story is good. Moving toward sustainable and equitable investing, or away from the evils of the centralized global banking system, can get many investors who agree with these ideas to jump aboard. Absent the details, the 100,000-foot view looks good.

That said, like cryptocurrency, many ESG investments have risks that are not being priced in right now. In the renewables space, the cost of production for wind, solar, hydro, and other energy types is rapidly declining. This means that the massive capital outlays of companies in renewable technology options may underperform for companies that will wait. Additionally, these technologies may be obsolete in coming years.

The multiples many ESG investments are now receiving relative to “dirty” energy options largely resemble the valuation gap between high tech and low-tech companies. These factors present unique risks to investors who care about equity valuations and fundamentals.

CATEGORY

1. Coronavirus
2. Dividend Stocks
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POST TAG

1. bubble
2. coronavirus
3. ESG
4. pandemic
5. technology
6. value investing

TICKERS GLOBAL

1. NYSE:SHOP (Shopify Inc.)
2. TSX:SHOP (Shopify Inc.)

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chrismacdonald